Approved: February 22, 2005
Date

MINUTES OF THE HOUSE INSURANCE COMMITTEE

The meeting was called to order by Chairman Clark Shultz at 3:30 P.M. on February 17, 2005 in Room 527-S of the Capitol.

All members were present except:
Representative Scott Schwab- excused
Representative Steve Brunk- excused

Committee staff present:
Melissa Calderwood, Kansas Legislative Research Department
Terri Weber, Kansas Legislative Research Department
Ken Wilke, Revisor of Statutes Office
Sue Fowler, Committee Secretary

Conferees appearing before the committee:
Chris Swickard, Topeka, KS
Dave Hanson, Topeka, KS
Jarrod Forbes, Topeka, KS
Larry Magill, Topeka, KS
Allen Patek, Green Bay, WI
Lew Ebert, Topeka, KS
Cliff Sones, Wichita, KS
Bill Sneed, Topeka, KS
Ashley Sherard, Lenexa, KS
Kevin Robertson, Topeka, KS
Bob Tomlinson, Topeka, KS
Larry Magill, Topeka, KS
Doug Wareham, Topeka, KS
Bill Henry, Topeka, KS
Phillip R. O'Connor, Chicago, IL
Dennis Phillips, Topeka, KS

Others attending:
See attached list.

Hearing on:

HB 2323: Insurance company structure; statutory changes compatible with corporation code.

Terri Weber, Kansas Legislative Research Department, gave a brief overview of **HB 2323.**

Proponents:

Chris Swickard, The Security Benefit Group of Companies, (Attachment #1), appeared before the committee in support of **HB 2323**.

Dave Hanson, Kansas Life & Health Insurance Association, (Attachment #2), presented written testimony in support of **HB 2323**.

Hearing closed on **HB 2323**.

Hearing on:

HB 2325: Life insurance; regulation of certain types of contracts.

Proponents:

Chris Swickard, The Security Benefit Group of Companies, (Attachment #3), appeared before the committee

MINUTES OF THE House Insurance Committee at 3:30 P.M. on February 17, 2005 in Room 527-S of the Capitol.

insupport of **HB 2325**.

Dave Hanson, Kansas Life & Health Insurance Association, (Attachment 4), presented written testimony in support of **HB 2325**.

Hearing closed on **HB 2325**.

HB 2326: Kansas Insurance Guaranty Association, handling of claims.

Melissa Calderwood, Kansas Legislative Research Department, gave a brief overview of **HB 2326**.

Proponents:

Jarrod Forbes, Kansas State Department of Insurance, (Attachment #5), appeared before the committee in support of **HB 2326**.

Dave Hanson, Kansas Insurance Guaranty Association, (Attachment #6), gave testimony in support of **HB 2326**,

Opponent:

Larry Magill, Kansas Association of Insurance Agents, (Attachment #7), presented testimony in opposition to **HB 2326**.

Hearing closed on **HB 2326**.

Hearing on:

HB 2366: Accident and health insurance; removal on limitation on deductibles, coinsurance and similar payments.

Melissa Calderwood, Kansas Legislative Research Department, gave a brief overview of **HB 2366**.

Proponents:

Allen Patek, Humana, (Attachment #8), appeared before the committee in support of **HB 2366**.

Lew Ebert, The Kansas Chamber, (Attachment #9), gave testimony in support of **HB 2366.**

Cliff Sones, Wichita Independent Business Association, (Attachment #10), presented written testimony in support of **HB 2366**.

Bill Sneed, America's Health Insurance Plans, (Attachment #11), presented written testimony in support of **HB 2366.**

Ashley Sherard, Lenexa Chamber of Commerce, (Attachment #12), presented written testimony in support of **HB 2366**.

Opponent:

Kevin Robertson, Kansas Dental Association, (Attachment #13), presented written testimony in opposition to **HB 2366**.

Neutral:

Bob Tomlinson, Kansas State Department of Insurance, (Attachment #14), gave neutral testimony before the

MINUTES OF THE House Insurance Committee at 3:30 P.M. on February 17, 2005 in Room 527-S of the Capitol.

committee on **HB 2366**.

Larry Magill, Kansas Association of Insurance Agents, (Attachment #15), gave neutral testimony before the committee on **HB 2366**.

Hearing closed on **HB 2366**.

Hearing on:

HB 2184: Insurance; property/casualty insurance modernization act.

Proponents:

Phillip R. O'Connor, Constellation New Emergy, Inc.,(Attachment #16), appeared before the committee in support of **HB 2184**.

Larry Magill, Kansas Association of Insurance Agents, (Attachment #17), gave testimony in support of **HB 2184**.

Bill Sneed, The State Farm Insurance Companies, Inc., (Attachment #18), gave testimony in support of **HB 2184**.

Opponents:

Bob Tomlinson, Kansas State Department of Insurance, (Attachment #19), presented testimony in opposition to **HB 2184**.

Dennis Phillips, Kansas State Council of Fire Fighters, (Attachment #20), presented testimony in opposition to **HB 2184**.

Hearing closed on **HB 2184**.

Representative Dillmore moved to favorably pass **HB 2138**. Seconded by Representative Kelsey. Motion carried.

Representative Dillmore moved to favorably pass **HB 2160.** Seconded by Representative Cox. Discussion followed.
Representative Dillmore withdrew the motion. Seconded by Representative Cox. Motion carried.
Representative Faber moved to amend **HB 2160** with four changes to make sure the bill does not apply to Workers Compensation . Seconded by Representative Dillmore. Motion carried. Representative Dillmore moved to pass **HB 2160** as amended. Seconded by Representative Cox. Motion carried.

Representative Dillmore moved to pass and put on consent calendar **HB 2203**. Seconded by Representative Cox. Motion carried.

Next meeting will be Tuesday, February 22, 2005.

Meeting adjourned at 5:30 p.m.

House Insurance Committee
Guest Sign Sheet
Thursday, February 17, 2005

Name	Representing
Alex Kotsyantz	PIA
[illegible]	KAMMCO
Danielle Davey	Intern - Dillmore
Bruce Witt	Preferred Health Systems
Natalie Haag	Security Benefit
Chris Swickard	Security Benefit
LARRY MAGILL	KAIA
[illegible]	KAIA
Dennis Phillips	KSCOF
Allan Patel	Humana
[illegible]	KID
Bob Tonkin	KID
Bill Sneed	State Farm
Bill Sneed	FARMERS
Brad Smoot	AIA / BCBS
[illegible]	Jackie Braden
LEW EHRET	KS Chamber
Bill Henry	Ks Credit Union Assn
David Hanson	Ks Insur Assns
[illegible]	KAHP

HOUSE COMMITTEE ON INSURANCE
Testimony on House Bill 2323
February 16, 2005
By: Chris Swickard, Second Vice President and Counsel
Security Benefit Life Insurance Company

Thank you for the opportunity to be here today. My name is Chris Swickard and I am Second Vice President and Counsel for Security Benefit Life Insurance Company ("Security Benefit"). I am here to testify in favor of House Bill No. 2323.

HB 2323 amending K.S.A. 40-305, 40-306 and 40-502.

Background & Reasons for Support:
K.S.A. 40-305, which applies to domestic insurance companies having capital stock, sets forth certain requirements regarding the number of directors an insurer must have and how directors are to be elected. It also currently states that "directors shall take the oath of office as in other corporations" the implication being that, as a general matter, directors of a corporation are required by Kansas law to take an oath of office. This is not the case. The Kansas Corporation Code (Chapter 17 of the Kansas statutes) does not require directors of a general business corporation to take an oath of office. We are aware of only two instances in which the Kansas Corporation Code requires something akin to an oath of office. Section 2208 of Article 22 of Chapter 17 applicable to credit unions provides that "all members of the board and committees and all officers shall be sworn . . ." and Section 2331 of Article 23 of Chapter 17 applicable to development credit corporations provides that, "directors shall be annually sworn to the proper discharge of their duties . . ." The presence or absence of an oath of office has no bearing on the responsibilities, the duties or the standard of care imposed upon a director of an insurance company. In addition, except in the very isolated instances noted above, the requirement that an oath be administered is inconsistent with requirements of the Kansas Corporation Code. We also note that oaths are not required under the Delaware Corporation Code or the American Bar Association's Model Business Corporation Act which many states have adopted. In view of this, Security Benefit supports the amendment of K.S.A. 40-305 as proposed in HB 2323.

K.S.A. 40-306 deals with, among other things, the organization of stock insurance companies and provides that the board of directors of a company "shall elect from their number a President and Vice President, and shall appoint a Secretary, Treasurer and such other officers as shall be prescribed in the bylaws, and shall fill any vacancies that may occur" (emphasis added). In modern corporate law and governance, officers are not required to come from the board of directors unless that requirement is specified in the company's articles of incorporation or bylaws. In addition, the Kansas Corporation Code does not specify the officers a general business corporation is required to have. Ordinarily, it is the bylaws which specify which officers a company will have and how they are to be elected or appointed. Limiting the pool of candidates for President and Vice-President by law to the members of the board of directors is not only untraditional, it unnecessarily limits the pool of qualified candidates for these positions or forces companies to first put them on the board – whether they are qualified to be directors or

not. HB 2323 removes the words "from their number" in K.S.A. 40-306 and also removes the specific listing of officers a stock insurer must have. The language being removed regarding officers is replaced with language from the Kansas Corporation Code (K.S.A.17-6302) providing that officers shall be as stated in the bylaws or as provided by the Board of Directors. Thus, the proposed changes will better align the provisions in the Kansas Insurance Code dealing with officers of a stock insurance company with existing provisions in the Kansas Corporation Code. Security Benefit supports the amendment of K.S.A. 40-306 as proposed in HB 2323.

K.S.A. 40-502, which applies to mutual life insurance companies and mutual holding companies, parallels 40-305 and 40-306 in that 40-502 requires directors to take an oath of office "as in other corporations." It also specifies the officers a mutual organization must have and that such officers shall be elected "from among their number." HB 2323 removes the words "from their number" in K.S.A. 40-502 and also removes the specific listing of officers a mutual organization must have. The language being removed regarding officers is replaced with language from the Kansas Corporation Code (K.S.A.17-6302) providing that officers shall be as stated in the bylaws or as provided by the Board of Directors. Thus, the proposed changes will better align the provisions in the Kansas Insurance Code dealing with officers of a mutual organization with existing provisions in the Kansas Corporation Code. Security Benefit supports the amendment of K.S.A. 40-306 as proposed in HB 2323.

Thank you. I would be happy to address any questions you may have at this time.

KANSAS LIFE & HEALTH INSURANCE ASSOCIATION

DAVID A. HANSON, LEGISLATIVE COUNSEL
800 S.W. JACKSON, SUITE 900
TOPEKA, KS 66612-1259

TELEPHONE NO. (785) 232-0545
FAX NO. (785) 232-0005

House Insurance Committee
Testimony on House Bill 2323

February 17, 2005

Mr. Chairman and Members of the Committee:

Thank you for this opportunity to present information on behalf of the Kansas Life & Health Insurance Association, whose members are domestic insurance companies in Kansas.

The provisions of the bill will help modernize and simplify companies, organizational requirements, making them more compatible with our corporation code. We support these changes and recommend them for your favorable consideration.

Respectfully,

DAVID A. HANSON
Legislative Counsel

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House Insurance
Date: 2-17-05
Attachment # 2

HOUSE COMMITTEE ON INSURANCE
Testimony on House Bill 2325
February 16, 2005
By: Chris Swickard, Second Vice President and Counsel
Security Benefit Life Insurance Company

Thank you for the opportunity to be here today. My name is Chris Swickard and I am Second Vice President and Counsel for Security Benefit Life Insurance Company ("Security Benefit"). I am here to testify in favor of House Bill No. 2325.

HB 2325 amends K.S.A. 40-401, 40-436 and 40-3641.

Background and Reasons for Support:
The proposed changes in HB 2325 would modernize the Kansas Insurance Code to reflect more fully what is occurring in the marketplace with respect to funding agreements, guaranteed investment contracts ("GICs") and synthetic guaranteed investment contracts ("synthetic GICs") and to remove any ambiguity regarding these products' status under the Kansas Insurance Code.

A "funding agreement" is an agreement under which an insurer accepts one or more deposits, typically from an institutional investor, and provides for (1) the deposits to be accumulated at a fixed or floating rate of interest and (2) one or more future payments to be made by the insurer to the policyholder. Obligations under a funding agreement are not based on mortality or morbidity contingencies, but normally do provide for a return of the principal amount invested as well as all or a portion of the interest credited under the agreement. Typical purchasers of funding agreements are mutual funds and large business entities.

A "guaranteed investment contract," or a "GIC," is very similar to a funding agreement. A GIC is a contract under which one or more deposits are accepted and that guarantees to the owner the return of principal, plus a fixed or floating rate of interest for a predetermined period of time. Like funding agreements, GICs are not based on mortality or morbidity contingencies. The typical purchaser of a GIC is a defined benefit or defined contribution retirement plan. Although there is no statute or regulation which provides for this, many view a GIC as an instrument purchased by a retirement plan and a funding agreement as the comparable instrument purchased by institutions which do not enjoy the tax-exempt status of a retirement plan.

A "synthetic GIC" is a contract under which the insurer's obligation is established by reference to a portfolio of assets that the insurer does not own. A synthetic GIC simulates the performance of a traditional GIC and is sometimes colloquially referred to as a "wrapper agreement" as it "wraps" the assets in question. In a typical synthetic GIC arrangement the insurer agrees to purchase from the policyholder, such as a defined benefit retirement plan, securities owned by the plan at the price the plan paid for the securities (i.e., at book value) if the plan must sell the securities in order to make benefit payments. Thus, the plan is assured of having sufficient assets to fund benefit payments.

Unfortunately, none of these products are mentioned specifically in the Kansas Insurance Code. K.S.A. 40-401 deals with the formation of life insurance companies and sets forth the types of products which life insurers are permitted to issue. However, it makes no reference to funding agreements, GICs or synthetic GICs, products that were not in existence in 1927 when the statute was adopted. Similarly, K.S.A. 40-436 authorizes life insurers to create separate accounts, accounts which are not charged with the liabilities arising from any other business the insurer conducts. However, the only types of products specifically mentioned under 40-436 are life insurance and annuity contracts. Thus the ability of a life insurer to create separate accounts to support funding agreements and GICs is unclear. Finally, K.S.A. 40-3602 *et. seq.* governs the priority status of claims against the estate of an insolvent insurer. K.S.A. 40-3641 identifies claims under life insurance and annuity policies as Class 3 "loss claims" but makes no mention of funding agreements, GIC and synthetic GICs.

Given that the Kansas Insurance Code does not specifically mention funding agreements, GICs and synthetic GICs, confusion can be created in the minds of potential purchasers about these products' status. The lack of clarity in the Kansas Insurance Code can have detrimental effects on Security Benefit in a couple of ways. First, purchasers may prefer to deal with insurers domiciled in states where the statutes are clearer. Second, Security Benefit is regularly asked by purchasers to be provided an opinion of outside counsel (at considerable expense to the Company and, thus, its policyholders) attesting to the validity of the contracts under Kansas law. The Kansas Insurance Department (the "Department") has worked cooperatively with Security Benefit in dealing with these issues and we appreciate their support. For example, the Department's General Counsel issued an opinion in May of 2000 indicating that funding agreements were viewed by the Department as annuities and therefore a life insurer was permitted to issue them under K.S.A. 40-401. The opinion also indicated that the Department believed funding agreements should be accorded Class 3 loss claim status. However, the opinion is getting dated and in any event, obviously does not carry the weight of a statute adopted by the Legislature.

A number of other states have recognized these problems and amended their laws to specifically provide statutory authority and insolvency claim priority for products like funding agreements. New York, California, Connecticut and Nebraska have specifically dealt with this issue.

Attached to my testimony is a propose amendment to correct a technical error where the word "guaranteed" was left out of Section 1, line 21. With this amendment to HB 2325, Security Benefit supports the adoption of the Bill as introduced in order to clarify the cited sections of the Kansas Insurance Code and to remove competitive barriers.

Thank you. I would be happy to address any questions you may have at this time.

Session of 2005

HOUSE BILL No. 2325

By Committee on Insurance

2-7

AN ACT relating to insurance; pertaining to guaranteed investment contracts and related types of insurance contracts; amending K.S.A. 40-401, 40-436 and 40-3641 and repealing the existing sections.

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

Section 1. K.S.A. 40-401 is hereby amended to read as follows: 40-401. Any 10 or more persons, a majority of whom are citizens of this state, may associate in accordance with the provisions of this code and form an incorporated company, upon either the stock or mutual plan, to make insurance upon the lives of persons and every insurance appertaining thereto or connected therewith and to grant, purchase or dispose of annuities, *and to issue funding agreements, guaranteed investment contracts and synthetic investment contracts*. Such companies may incorporate: (a) In their policies provisions or conditions for the waiver of premiums or for the granting of an annuity to the insured, or for special surrender values or other benefits in the event the insured shall from any cause become unemployed or totally and permanently disabled; (b) in their policies provisions for acceleration of life or annuity benefits in advance of the time they would otherwise be payable subject to such reserve and other regulatory standards as the commissioner may prescribe by rules and regulations, except that any provision providing for acceleration of life or annuity benefits for persons diagnosed as having a medical condition usually requiring continuous confinement for the rest of the person's life in a nursing home or other eligible facility as defined in the policy, may also provide for acceleration of benefits upon diagnosis of such condition even if the person is not confined in a nursing home or similar facility; (c) in their policies and annuity contracts provisions or conditions for waiver of surrender charges upon terms and conditions as specified in the policy or contract, subject to rules and regulations adopted by the commissioner of insurance; or (d) in their policies provisions for the payment of a larger sum if death is caused by accident than if it results from any other causes.

Prior to the payment of any accelerated benefit, the insurer shall receive from any assignee or irrevocable beneficiary of the policy a signed acknowledgment of concurrence for the payment. For the purposes of

KANSAS LIFE & HEALTH INSURANCE ASSOCIATION

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House Insurance Committee
Testimony on House Bill 2325

February 17, 2005

Mr. Chairman and Members of the Committee:

Thank you for this opportunity to present information on behalf of the Kansas Life & Health Insurance Association, whose members are domestic insurance companies in Kansas.

We support the inclusions of the references to the types of contracts as shown in House Bill 2325. We believe this will help provide clarity in identifying and regulating these types of contracts. We support these changes and recommend them for your favorable consideration.

Respectfully,

David A. Hanson

DAVID A. HANSON
Legislative Counsel

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House Insurance
Date: 2-17-05
Attachment # 4

Kansas
Insurance
Department

Sandy Praeger COMMISSIONER OF INSURANCE

COMMENTS ON
HB 2326—RELATING TO THE KANSAS INSURANCE GUARANTY ASSOCIATION
HOUSE COMMITTEE ON INSURANCE
February 17, 2005

Mr. Chairman and members of the committee:

Thank you for the opportunity to visit with you on behalf of the Kansas Insurance Department. House Bill 2326 provides for amendments to the Kansas Insurance Guaranty Association.

The Kansas Insurance Department supports the changes proposed in this bill and urges this committee to recommend HB 2326 favorable for passage.

With your permission Mr. Chairman, I would now like to introduce David Hanson who is legal counsel for the Kansas Guaranty Association to discuss the proposed amendments in detail.

Jarrod Forbes
Assistant Director
Government Affairs

House Insurance
Date: 2-17-05
Attachment # 5

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Kansas Insurance Guaranty Association
David A. Hanson, general counsel

Overview

Since the late 1960s, state guaranty associations have evolved, largely being driven by external pressures. In 1970, the Kansas Insurance Guaranty Association system was created with relatively broad provisions of coverage for insureds and claimants whose insurer became insolvent. The insolvencies at that time were largely personal lines and the persons protected were largely individuals and small businesses, so the broad provisions of coverage were workable.

In recent years, the guaranty association laws in other states have been amended to restore coverage to its intended purpose, namely, to provide a safety net for individuals and small businesses who would be harmed the most financially by the insolvency of their insurer. The recent efforts to amend guaranty association provisions began as a response to the commercial lines insolvencies of the mid-1980s, in which guaranty fund assessments soared to pay the claims of large commercial lines policyholders. The guaranty fund claimants of the 1980s and 1990s changed from individuals and small business to major US corporations, which had the resources to withstand the insolvency of one of their insurers and the ability to choose a financially solvent insurer in the first place. It should also be noted that the guaranty associations are the payor of the last resort and therefore exhaustion of all other solvent coverage is generally required before the guaranty assocaitions will provide coverage. Often, commercial claimants against the guaranty funds had other solvent coverage or replaced their insolvent coverage quickly, but yet taxed the guaranty fund system with large commercial claims. Finally, guaranty fund coverage was intended to be limited. There are statutory caps and exclusions from coverage in place in all states. Because of the multi-state nature of the risks insured, the commercial lines claims have caused problems in the state guaranty fund system by being able to forum shop for coverage among the funds.

Most recently, guaranty fund assessments have reached record levels due to another round of commercial lines insolvencies, which is marked by the largest property-casualty insurers that have ever become insolvent. States like Kansas, which have not made the necessary adjustments in their guaranty fund law to limit commercial lines coverage and to refocus coverage on individuals and small businesses, are hit particularly hard. In addition, the state guaranty fund laws are really showing their age in the context of the current insolvencies. The variety of commercial insurance products that the guaranty funds have recently encountered present new legal, operational and financial challenges that the 35 year old guaranty fund laws do not clearly address and resolve.

The state guaranty association system is based on the approach embodied in the NAIC Model Post Assessment Property-Casualty Guaranty Fund Act, and also more recently, on the model guaranty fund legislation of the National Conference of Insurance Guaranty Funds (NCIGF), the association of the state guaranty funds. In addition, the NCIGF commissioned a special task force that reviewed the new issues from recent insolvencies and recommended legislative solutions. The suggested changes to the Kansas Insurance Guaranty Association law in 2005 are the priority issues that we believe need to be enacted in Kansas, including the following:

1. **Covered claim clarifications – amending K.S.A. 40-2903**
2. **Guaranty Association trigger – amending K.S.A. 40-2903 and 40-2906**
3. **Extent covered claims payable – amending K.S.A. 40-2906**
4. **Claim bar date – amending K.S.A. 40-2906**
5. **Limiting unearned premium claims – amending K.S.A. 40-2903 and 40-2906**
6. **Exhaustion and offset other insurance – amending K.S.A. 40-2910**
7. **Fabe cure – amending K.S.A. 40-3641**

1. Covered claim clarifications:

The proposed amendments relating to the residency of claimants and the location of property that has been damaged will help clarify the intent of the limitations in our existing law. Clarifications to what is considered a "covered claim" also would confirm that punitive or exemplary damages are not included in a "covered claim", unless coverage for those types of damages was provided in the policy of the insolvent insurer. "Covered claim" would also exclude first party claims by an insured whose net worth exceeds $25,000,000 or who is an affiliate of the insolvent insurer. The rationale for these limitations on first party claims would be that the existing and limited resources of the Kansas Guaranty Association would be preserved to pay individual claimants and small businesses by the addition of first and third party net worth exclusions. These exclusions work largely to exclude claims of commercial insureds, who can better survive the insolvency of an insurer, and likely had resources in the first place to choose a financially sound insurer.

It should be noted that the net worth of the insured is calculated as of the date of the insolvency of the insurer, and not as of the date the insured bought the coverage. The net worth of the insured, namely, the insured's ability to withstand the insolvency of the insurer, is measured as of the insolvency because significant changes can take place in the net worth of the insured between the time they bought the policy and the time their insurer becomes insolvent. Net worth calculated as of the date of the insolvency is more equitable to the insured and accomplishes the purposes of excluding from coverage those who are currently able to financially withstand the insolvency of their insurer.

It should also be noted that Guaranty Association coverage comes after the claimant has exhausted all other insurance coverage. The Guaranty Association payments are intended to be the last resort. If there is no Guaranty Association coverage because of net worth, the claimants can still file claims against the liquidator of the insolvent insurer's estate, either for the full amount of their claims or the amount in excess of the Guaranty Association's coverage limits. Thus, limiting or eliminating guaranty fund coverage does not mean that those claimants will not receive some distribution out of the estate. Granted, it may be a percentage on the dollar, but then again, the wealthy claimants are in a position to make the best out of a bad situation. Other states that have adopted first and third party net worth exclusions are shown on the lists that follow.

States with First Party Net Worth Exclusion

State	Applicable Net Worth
Alabama	$25 million
Arkansas	$50 million
Colorado	$10 million
Connecticut	$25 million
Delaware	$10 million
Georgia	$3 million
Hawaii	$25 million
Illinois	$25 million
Indiana	$5 million
Kentucky	$25 million
Louisiana	$25 million
Maine	$25 million
Maryland	$50 million
Michigan	.1% of aggregate premiums written by insolvent insurer in previous year
Minnesota	$25 million
Missouri	$25 million
Nevada	$25 million
New Hampshire	$25 million
North Carolina	$50 million
North Dakota	$10 million
Oregon	$25 million
Pennsylvania	$25 million
South Carolina	$10 million
South Dakota	$50 million
Tennessee	$10 million
Texas	$50 million
Utah	$25 million
Wisconsin	$10 million

Sept. '04

States with Third Party Net Worth Exclusion

State	Applicable Net Worth
Alabama	$25 million
Arkansas	$50 million
Colorado	$25 million
Connecticut	$50 million
Delaware	$25 million
District of Columbia	$50 million
Georgia	$3 million
Hawaii	$50 million
Illinois	$25 million
Indiana	$50 million
Kentucky	$25 million
Louisiana	$25 million
Michigan	.1% of aggregate premiums
Minnesota	$25 million
Missouri	$25 million
Montana	$50 million
Nevada	$25 million
New Hampshire	$25 million
North Carolina	$50 million
North Dakota	$25 million
Ohio	$50 million
Oklahoma	$50 million
Oregon	$25 million
Pennsylvania	$50 million
Rhode Island	$50 million
South Carolina	$25 million
South Dakota	$50 million
Tennessee	$25 million
Texas	$50 million
Utah	$25 million
Virginia	$50 million
Wisconsin	$10 million

Sept. '04

2. Guaranty Association trigger:

This proposed legislation would clarify that an insolvent insurer would be defined not just as one who is determined to be insolvent, but also against whom a final order of liquidation has been entered by a court of competent jurisdiction in the insurer's sate of domicile. Kansas is one of a handful of states that still triggers Guaranty Association coverage upon a "finding of insolvency." This could trigger the Kansas Guaranty Association at an earlier date than other states in a multi-state insolvency. For example, the Kansas Guaranty Association could be triggered to pay covered claims of an insurer in rehabilitation, while guaranty fund coverage in other states for the same insurer would be triggered only after a court order of liquidation has been issued. Guaranty Association coverage is intended to provide claimants with a limited payment as a last resort after the insolvency of their insurer. Guaranty fund coverage is not intended to be used to rehabilitate a financially troubled insurer, which could happen under current Kansas law.

3. Extent covered claims payable:

Kansas Insurance Guaranty Association currently limits payment of covered claims to an amount in excess of $100, but less than $300,000. The first $100 of a claim is therefore treated as a deductible and not paid. The $100 deductible made sense when the laws were first enacted, but the cost of administration now seems to exceed any benefits from it. The Guaranty Association laws were enacted 35 years ago largely to respond to personal lines insolvency. While the $100 deductible might have been a meaningful amount several decades ago, in the current law and practice, the costs of processing thousands of claims and applying the $100 deductible often burdens the Guaranty Association without any of the intended benefits. This is especially true when we are trying to get a claim settled and we agree upon an amount and then have to explain that the first $100 is not payable. The proposed amendments would also clarify that coverage is limited to the first $300,000 of a claim, consistent with the concept that the Guaranty Association should be the payor of last resort.

4. Claim bar date:

When the guaranty associations were originally created, a claims filing bar date was not an issue, as most insolvencies were personal lines insurers whose policies had no claims tail. The insureds and claimants knew whether or not they had a claim under their policy almost immediately. When commercial lines insurers became insolvent, however, the estates often involved long tail claims, and state liquidation courts began allowing long periods of time in which to file a claim against the estate and the Guaranty Association. This places an increased financial and administrative burden on the Guaranty Association, and makes the Association's liability seemingly endless. Many such long tail claims were from mass tort claims, and complex environmental and other coverage for policyholders and claimants not intended to be the primary beneficiaries of guaranty fund coverage. We are proposing the bar date be set at the earlier of 18 months after the order of liquidation or the final date set by the court for filing claims in the liquidation. An independent bar date for the guaranty fund has solved this problem in many other states. A listing of other states is attached.

Guaranty Fund Bar Dates

STATE	BAR DATE?	CITE	SAME AS LIQUIDATOR'S?
Alabama	Yes	§27-42-8 (a) (1)	Yes
Alaska	Yes	§21.80.060	Yes
Arizona	Yes	§20-679	Yes – 4 months from the date of notice to creditors
Arkansas	Yes	§23-90-111 (c)	Yes
California	Yes	Ins. §1063.1 (c) (1) (iii)	Yes (of the domiciliary state)
Colorado	Yes	§10-4-508 (1) (a)	Yes
Connecticut	Yes	§38a-841 (1) (a) (ii) (B)	No – 2 years from the date of insolvency
Delaware	Yes	18 Del. Code §4208 (a) (iii)	No – the earlier of 24 months after the date of the order of liquidation or the liquidator's bar date
District of Columbia	Yes	§31-1319 (a) (24) (6) (1)	No – the earlier of the liquidator's deadline or 18 months from the order of liquidation
Florida	Yes	§631.68	No – settlement or suit must be instituted within one year of liquidator's bar date
Georgia	Yes	§33-36-11 (a)	Yes
Hawaii	Yes	§431:16-108	Yes
Idaho	Yes	§41-3608 (1) (a)	No—the earlier of 18 months after the order of liquidation or the liquidator's bar date
Illinois	Yes	§215 ILCS 5/194	No—the earlier of 18 months after the order of liquidation or the liquidator's bar date
Indiana	Yes	§27-6-8-4 (4)	No – claim must be both timely with liquidator and within 1 year of liquidation order
Iowa	Yes	§515B.17	Yes
Kansas	No		
Kentucky	Yes	§304.33-360	No—the earlier of 12 months after the order of liquidation or the liquidator's bar date
Louisiana	Yes		No—the earlier of 5 years after the order of liquidation or the liquidator's bar date
Maine	Yes	24-A M.R.S. §4438 (1) (A) (3)	No – the earlier of 24 months after the date of the order of liquidation or the liquidator's bar date
Maryland	Yes	Md. Ins. Code §9-226	No—the earlier of 18 months after the order of liquidation or the liquidator's bar date
Massachusetts	No		
Michigan	Yes	§500.7925 (1) (c)	Yes – (of the domiciliary state)
Minnesota	Yes	§60C.09	Yes, except for workers comp claims and excused late filings under 60B.37
Mississippi	No		
Missouri	Yes	§375.775 (1) (a)	No – no later than the final date set by the court for filing against the liquidator, except that if the time first set is one year or less from the date of insolvency and the court grants a filing extension, claims must be filed with the association no later than the new date set by the court or one year after the date of insolvency, whichever occurs first

Guaranty Fund Bar Dates

STATE	BAR DATE?	CITE	SAME AS LIQUIDATOR'S?
			For claims arising from insolvencies after Sept 1, 2000, the earlier of 18 months after the final order of liquidation or the liquidator's bar date
Montana	No		
Nebraska	Yes	§44-2406 (2)	Yes – only timely filed claims with the receiver will be forwarded to fund
Nevada	Yes	§687A.033 (2) (c)	No – the earlier of the liquidator's bar date or 18 months after the date of the order of liquidation
New Hampshire	Yes		No—the earlier of 36 months after the order of liquidation or the liquidator's bar date
New Jersey	Yes		The liquidator's bar date unless unusual hardship can be shown; For insolvencies pending after 1996, the later of 1 year after the effective date of the 1996 amendments or the liquidator's bar date;
New Mexico	No		
New York	No		
North Carolina	Yes	§58-48-35 (a) (1)	Yes
North Dakota	Yes	Plan of Operation	No—the earlier of 18 months after the order of liquidation or the liquidator's bar date;
Ohio	Yes	§3955.08 (A) (1)	No – the earlier of the liquidator's bar date or 18 months after the order of liquidation
Oklahoma	Yes	36 Okla. St.§2014	Yes
Oregon	Yes	§734.510	Yes
Pennsylvania	Yes	§40.P.S.221.37	Yes
Rhode Island	Yes	§27-34-8 (a) (1) (iii)	Yes
South Carolina	Yes	§38-31-60 (a) (iv) (2)	No – the earlier of the liquidator's bar date or 18 months after the order of liquidation
South Dakota	Yes	§58-29A-6B	No – the earlier of the liquidator's bar date or 18 months after the order of liquidation
Tennessee	Yes	§56-12-121 (a)	No – the earlier of the liquidator's bar date or 18 months after the order of liquidation
Texas	Yes	Ins. Art. 21.28-C, §8 (d)	No – the later of the liquidator's bar date or 18 months after the order of liquidation
Utah	Yes	§31A-28-207 (5) (i)	No – also see 31A27-315 and 31A-27-328 – liquidator's bar date but allows for discretion if won't prejudice liquidation proceeding
Vermont	Yes	8 V.S.A. §3615 (a) (i)	No – liquidator's bar date but not more than 3 years after determination of insolvency
Virginia	Yes	§38.2 – 1512	Yes
Washington	Yes	§48.32.030 (4)	Yes
West Virginia	Yes	§33-26-8 (1) (a)	Yes
Wisconsin	Yes	§646.13 (c)	No – the earlier of the liquidator's extended bar date or 18 months after the order of liquidation
Wyoming	Yes	§26-31-111 (c)	Yes

Sept. '04

5. Limits unearned premium claims:

Most state guaranty association laws allow insureds to recover paid but unearned premiums when their insurer becomes insolvent. A $10,000 cap on such claims is high enough so that individuals and small businesses can recover in full, and so that the limited resources of the guaranty fund will be conserved to pay both the unearned premium and other claims of such persons. It would likely limit the recovery of large corporate purchasers of insurance who possess, or have access to, a high degree of insurance risk management skills to carefully choose a financially sound insurer in the first place. Additionally, such insureds should have the resources to survive even in the event of the insolvency of their insurer, by contrast to the personal lines or small commercial lines policyholders.

6. Exhaustion and offset of other insurance:

As in most states, current law in Kansas specifies that a claim that may be covered under several policies must first exhaust coverage under policies other than the insolvent insurer and that any covered claim payable by the Guaranty Association is reduced by any recovery from such other insurance. These provisions help assure that the Guaranty Association is the payor of last resort and also prevents the potential for a double recovery by the claimant. Our proposed amendments are intended to reinforce these concepts and clarify that the exhaustion and offset requirements apply to all claims under any kind of insurance, regardless of whether first party or third party claims, and including claims under accident and sickness insurance, health insurance and workers' compensation coverage similar to provisions adopted in some of the other states.

7. Fabe cure amendments

Enacted in 1797, the federal superpriority statute, 31 U.S.C. § 3713, provides that claims of the federal government shall be paid first when any person indebted to the federal government becomes insolvent. The statute also imposes personal liability on persons, such as receivers, who violate the law and pay others first.

Over the last two decades, the federal government began to aggressively assert the 200 year old federal superpriority statute in state insurance receiverships, arguing that it preempts the state priority provisions on all types of claims in an insurer insolvency. In *U.S. Department of Treasury v. Fabe,* 508 U.S. 491 (1993), the U.S. Supreme Court gave its interpretation of the federal superpriority statute vs. state insurance priority laws. The court said that under McCarran-Ferguson, Congress had preserved for the states the right to regulation the business of insurance As such, state laws giving priority to administrative expenses and claims of policyholders could be paid before the claims of the federal government, because those provisions were enacted for the purposes of insurance regulation. However, giving priority to other classes of claims such as employee wage claims, over the federal government did not regulate the business of insurance and are preempted by the federal superpriority statute.

After *Fabe*, the state guaranty associations have been active in amending the priority provisions in the state liquidation laws to confirm to the *Fabe* ruling. Under the revised state laws, administrative expenses are a Class 1 priority. All claims under policies, including those of the federal government, are Class 2 priorities. All other claims of the federal government (non-policy) are now in Class 3.

Without these amendments, if the federal government prevails, and there may be a substantial number of federal claims in an insurer insolvency, the federal government may well take all of the remaining assets of an insolvent insurer's estate. The states could be left with little or no funding even to administer the insolvent insurer's estate, leaving it to the state to appoint and compensate a receiver and staff for an insolvent insurer. The guaranty funds, which pay covered claims up to the statutory caps, would also have no assets in an insolvent insurer's estate to look to be reimbursed for the claims of policyholders and third party claimants that they have paid. Kansas is in a small minority of states that have not yet adopted the "*Fabe cure*" provisions.

States Enacting Fabe Cure Legislation

1. Arizona 1997
2. Arkansas 1997
3. California 1997
4. Colorado
5. Connecticut
6. Delaware
7. Florida
8. Georgia
9. Hawaii
10. Idaho
11. Indiana
12. Illinois
13. Iowa
14. Kentucky
15. Louisiana
16. Maryland
17. Massachusetts
18. Michigan
19. Minnesota
20. Mississippi
21. Missouri
22. Montana
23. Nevada
24. New Hampshire
25. New York
26. North Carolina
27. North Dakota
28. Ohio
29. Oklahoma
30. Oregon
31. Pennsylvania
32. South Carolina
33. Tennessee
34. Texas
35. Utah
36. Vermont
37. Virginia
38. Washinton
39. West Virginia
40. Wisconsin

States That Have Not Enacted Fabe Cure

1. Alabama
2. Alaska
3. Kansas
4. Maine
5. New Jersey
6. New Mexico
7. Puerto Rico
8. Rhode Island
9. South Dakota
10. Wyoming

Session of 2005

HOUSE BILL No. 2326

By Committee on Insurance

2-7

AN ACT concerning insurance; pertaining to the Kansas Insurance Guaranty Association; relating to claims; amending K.S.A. 40-2903, 40-2906, 40-2909, 40-2910 and 40-3641 and repealing the existing sections.

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

Section 1. K.S.A. 40-2903 is hereby amended to read as follows: 40-2903. As used in this act: (a) "Association" means the Kansas insurance guaranty association created by this act.

(b) "Commissioner" means the commissioner of insurance of this state.

(c) "Covered claim" means an unpaid claim, including one for unearned premiums, which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy to which this act applies issued by an insurer, if such insurer becomes an insolvent insurer after the effective date of this act and:

(1) The claimant or insured is a resident of this state at the time of the insured event. *For entities other than an individual, the residence of a claimant, insured or policyholder is the state in which the principal place of business of such claimant, insured or policyholder is located at the time of the insured events*; or

(2) the ~~property from which the claim arises~~ *claim is a first party claim for damage to property that* is permanently located in this state.

"Covered claim" shall not include ~~any~~:

(1) ~~Amount~~ due any reinsurer, insurer, insurance pool or underwriting association, as subrogation recoveries or otherwise. any amount

(2) any amount awarded as punitive or exemplary damages , unless such damages were covered under the policy of the insolvent insurer

(3) any amount sought as a return of premium under any retrospective rating plan;

(4) any first party claim, including any claim for unearned premiums, by an insured whose net worth exceeds $10,000,000 on December 31 of the year prior to the year in which the insurer becomes an insolvent insurer. An insured's net worth on that date shall be deemed to include the aggregate net worth of the insured and all of such insured's subsidiaries as calculated on a consolidated basis; or

(5) *any first party claim by an insured that is an affiliate of the insolvent insurer.*

(d) "Insolvent insurer" means ~~(1) an~~ *An* insurer licensed by the commissioner to transact insurance in this state either at the time the policy was issued or when the insured event occurred; and

(2) determined to be insolvent by a court of competent jurisdiction *and against whom a final order of liquidation has been entered by a court of competent jurisdiction in the insured's home state.*

(e) "Member insurer" means any person who (1) is authorized to write any kind of insurance to which this act applies under K.S.A. 40-2902, *and amendments thereto,* including the exchange of reciprocal or inter-insurance contracts; and

(2) is licensed by the commissioner to transact insurance in this state. *Provided,.* This act shall not apply to those persons transacting business pursuant to the provisions of K.S.A. 40-202, *and amendments thereto.*

(f) "Net direct written premiums" means first gross premiums written in this state on insurance policies to which this act applies, less return premiums thereon and dividends paid or credited to policyholders on such direct business. "Net direct written premiums" does not include premiums on contracts between insurers or reinsurers.

(g) "Person" means any individual, corporation, partnership, association or voluntary organization.

Sec. 2. K.S.A. 40-2906 is hereby amended to read as follows: 40-2906. (a) In the event of the determination of insolvency *and order of liquidation* of a licensed insurer after the effective date of this act, the association shall:

(1) Be obligated to the extent of the covered claims existing prior to the determination of insolvency and arising within ~~thirty (30)~~ *30* days after the determination of insolvency, or before the policy expiration date if less than ~~thirty (30)~~ *30* days after the determination, or before the insured replaces the policy or causes its cancellation, if such insured does so within ~~thirty (30)~~ *30* days of the determination, but such obligation shall include only that amount of each covered claim which ~~is more than one hundred dollars ($100) and less than three hundred thousand dollars ($300,000) $300,000,~~ except that the association shall pay the full amount of any covered claim arising out of a workmen's compensation policy. In no event shall the association be obligated to the policyholder or claimant in an amount in excess of the face amount of the policy from which the claim arises.

does not exceed the first $300,000 of any claim,

(2) Be deemed the insurer to the extent of its obligation on the covered claims and to such extent shall have all rights, duties and obligations of the insolvent insurer as if the insurer had not become insolvent.

(3) Assess insurers amounts necessary to pay the obligations of the association under subsection (1) subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, and the cost of examinations under K.S.A. 40-2911, *and amendments thereto*, and other expenses authorized by this act. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding calendar year bears to the net direct written premiums of all member insurers for the preceding calendar year. Each member insurer shall be notified of the assessment not later than ~~thirty (30)~~ *30* days before it is due. No member insurer may be assessed in any year an amount greater than ~~two percent (2%)~~ *2%* of that member insurer's net direct written premiums for the preceding calendar year. If the maximum assessment, together with the other assets of the association, does not provide in any one year an amount sufficient to make all necessary payments, the funds available shall be prorated and the unpaid portion shall be paid as soon thereafter as funds become available. The association may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance, or if the commissioner advises the association that such assessment would in such commissioner's opinion, be detrimental to the solvency of a member insurer. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer.

(4) Investigate claims brought against the association and adjust, compromise, settle and pay covered claims to the extent of the association's obligation and deny all other claims and may review settlements, releases and judgments to which the insolvent insurer or its insureds were parties to determine the extent to which such settlements, releases and judgments may be properly contested.

(5) Notify such persons as the commissioner directs under K.S.A. 40-2908 (b)(1), *and amendments thereto*.

(6) Handle claims through its employees or through one or more insurers or other persons designated as servicing facilities. Designation of a servicing facility is subject to the approval of the commissioner, but such designation may be declined by a member insurer.

(7) Reimburse each servicing facility for obligations of the association paid by the facility and for expenses incurred by the facility while handling claims on behalf of the association and shall pay the other expenses of the association authorized by this act.

(b) The association may:

(1) Employ or retain such persons as are necessary to handle claims and perform other duties of the association.

(2) Borrow funds necessary to effect the purposes of this act in accordance with the plan of operation.

(3) Sue or be sued.

(4) Negotiate and become a party to such contracts as are necessary to carry out the purposes of this act.

(5) Perform such other acts as are necessary or proper to effectuate the purposes of this act.

(6) Refund to the member insurers in proportion to the contribution of each member insurer to the association that amount by which the assets of the association exceed the liabilities, if, at the end of any calendar year, the board of directors finds that the assets of the association exceed the liabilities of the association as estimated by the board of directors for the coming year.

(c) The association shall issue to each insurer paying an assessment under this act a certificate of contribution, in a form prescribed by the commissioner, for the amount so paid. All outstanding certificates shall be of equal dignity and priority without reference to amounts or dates of issue. A certificate of contribution may be shown by the insurer in its financial statement as an asset in such form and for such amount, if any, and period of time as the commissioner may approve.

(d) Notwithstanding any other provisions of this act:

(1) A covered claim shall not include a claim filed with the association after the earlier of:

(A) Eighteen months after the date of the order of liquidation; or

(B) the final date set by the court for the filing of claims against the liquidator or receiver of an insolvent insurer.

(2) A covered claim shall not include any claim filed with the association or a liquidator for protection afforded under the insured's policy for incurred-but-not-reported losses.

(3) Any obligation of the association to defend an insured on a covered claim shall cease upon the association's:

(A) Payment, by settlement releasing the insured or on a judgment, of an amount equal to the lesser of the association's covered claim obligation limit or the applicable policy limit; or

(B) tender of such amount.

The association shall pay only that amount of each covered unearned premium claim that does not exceed $10,000.

Sec. 3. K.S.A. 40-2909 is hereby amended to read as follows: 40-2909. (a) Any person recovering under this act shall be deemed to have assigned his rights under the policy to the association to the extent of his recovery from the association. Every insured or claimant seeking the pro-

tection of this act shall cooperate with the association to the same extent as such person would have been required to cooperate with the insolvent insurer. The association shall have no cause of action against the insured of the insolvent insurer for any sums it has paid out, except such causes of action as the insolvent insurer would have had if such sums had been paid out by the insolvent insurer. In the case of an insolvent insurer operating on a plan with assessment liability, payments of claims of the association shall not operate to reduce the liability of insureds to the receiver, liquidator, or statutory successor for unpaid assessments.

(b) The receiver, liquidator or statutory successor of an insolvent insurer shall be bound by settlements of covered claims by the association or a similar organization in another state. The court having jurisdiction shall grant such claims priority equal to that which the claimant would have been entitled in the absence of this act against the assets of the insolvent insurer. The expenses of the association or similar organization in handling claims shall be accorded the same priority as the liquidator's expenses. *For purposes of this subsection, expenses for the investigation or defense of claims against insureds under policies with an insolvent insurer shall be considered expenses of the association or other similar organization in handling claims.*

(c) The association shall periodically file with the receiver or liquidator of the insolvent insurer statements of the covered claims paid by the association and estimates of anticipated claims on the association which shall preserve the rights of the association against the assets of the insolvent insurer.

(d) The association shall have the right to recover ~~form~~ the following persons the amount of any covered claim paid on behalf of the person pursuant to the act: from

(1) An insured whose net worth on December 31 of the year immediately preceding the date the insurer becomes an insolvent insurer exceeds $25 million and whose liability obligations to other persons are satisfied in whole or in part by payments made under this act; and

(2) any person who is an affiliate of the insolvent insurer and whose liability obligations to other persons are satisfied in whole or in part by payments made under this act.

Sec. 4. K.S.A. 40-2910 is hereby amended to read as follows: 40-2910. (a) Any person having a claim against an insurer under any provision in an insurance policy other than a policy of an insolvent insurer which is also a covered claim shall be required to exhaust first his right under such policy. *A claim under an insurance policy shall include a claim under any kind of insurance, whether such claim is a first party or third party claim, and shall include, without limitation, accident and health insurance, workers' compensation, Blue Cross and Blue Shield and all other*

coverages except for policies of an insolvent insurer. Any amount payable on a covered claim under this act shall be reduced by the amount of any recovery under such *other* insurance policy.

(b) Any person having a claim which may be recovered under more than one insurance guaranty association or its equivalent shall seek recovery first from the association of the place of residence of the insured except that if it is a first party claim for damage to property with a permanent location, from the association of the location of the property, and if it is a workmen's compensation claim, from the association of the residence of the claimant. Any recovery under this act shall be reduced by the amount of the recovery from any other insurance guaranty association or its equivalent.

Sec. 5. K.S.A. 40-3641 is hereby amended to read as follows: 40-3641. The priority of distribution of claims from the insurer's estate shall be in accordance with the order in which each class of claims is herein set forth. Every claim in each class shall be paid in full or adequate funds retained for such payment before the members of the next class receive any payment. No subclasses shall be established within any class. The order of distribution of claims shall be:

(a) Class 1. The costs and expenses of administration during rehabilitation and liquidation including, but not limited to the following;

(1) The actual and necessary costs of preserving or recovering the assets of the insurer;

(2) compensation for all authorized services rendered in the rehabilitation and liquidation;

(3) any necessary filing fees;

(4) the fees and mileage payable to witnesses;

(5) authorized reasonable attorney fees and other professional services rendered in the rehabilitation and liquidation;

(6) the reasonable expenses of a guaranty association or foreign guaranty association ~~for unallocated loss adjustment expenses~~ *in handling claims*.

(b) Class 2. ~~Reasonable compensation to employees for services performed to the extent they do not exceed two months of monetary compensation and represent payment for services performed within one year before the filing of the petition for liquidation or, if rehabilitation preceded liquidation, within one year before the filing of the petition for rehabilitation. Principal officers and directors shall not be entitled to the benefits of this priority except as otherwise approved by the liquidator and the court. Such priority shall be in lieu of any other similar priority which may be authorized by law as to wages or compensation of employees.~~

~~(c) Class 3.~~ All claims under policies including claims for unearned

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premium or other premium refunds and such claims of the federal or any state or local government for losses incurred, ("loss claims") including third-party claims and all claims of a guaranty association or foreign guaranty association *other than those claims included in Class 1.* All claims under life insurance and annuity policies, whether for death proceeds, annuity proceeds or investment values shall be treated as loss claims. That portion of any loss, indemnification for which is provided by other benefits or advantages recovered by the claimant, shall not be included in this class, other than benefits or advantages recovered or recoverable in discharge of familial obligation of support or by way of succession at death or as proceeds of life insurance, or as gratuities. No payment by an employer to an employee shall be treated as a gratuity.

(c) Class 3. Claims of the federal government not included in Class 2.

(d) Class 4. Reasonable compensation to employees for services performed to the extent they do not exceed two months of monetary compensation and represent payment for services performed within one year before the filing of the petition for liquidation or, if rehabilitation preceded liquidation, within one year before the filing of the petition for rehabilitation. Principal officers and directors shall not be entitled to the benefits of this priority except as otherwise approved by the liquidator and the court. Such priority shall be in lieu of any other similar priority which may be authorized by law as to wages or compensation of employees. Where there are no claims and no potential claims of the federal government in the estate, claims in this class will have priority over claims in Class 2 and below.

~~(d) Class 4.~~ *(e) Class 5.* Claims of general creditors including claims of ceding and assuming companies in their capacity as such.

~~(e) Class 5.~~ *(f) Class 6.* Claims of ~~the federal or~~ any state or local government except those under Class ~~3~~ 2. Claims, including those of any governmental body for a penalty or forfeiture, shall be allowed in this class only to the extent of the pecuniary loss sustained from the act, transaction or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby. The remainder of such claims shall be postponed to be equal to the class of claims under subsection ~~(h)~~ *(i).*

~~(f) Class 6.~~ *(g) Class 7.* Claims filed late or any other claims other than claims under subsections ~~(g) and (h)~~ *(h) and (i).*

~~(g) Class 7.~~ *(h) Class 8.* Surplus or contribution notes, or similar obligations, and premium refunds on assessable policies. Payments to members of domestic mutual insurance companies shall be limited in accordance with law.

~~(h) Class 8.~~ *(i) Class 9.* The claims of shareholders or other owners

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in their capacity as shareholders.

For any claims other than claims which are currently pending or instituted on or after July 1, 2005, the provisions of this section in existence on June 30, 2005, shall apply.

Sec. 6

Sec. 6. K.S.A. 40-2903, 40-2906, 40-2909, 40-2910 and 40-3641 are hereby repealed.

Sec. 7

Sec. 7. This act shall take effect and be in force from and after its publication in the statute book.

Sec. 8

Testimony
Before the House Insurance Committee
On House Bill 2326
By Larry Magill
Kansas Association of Insurance Agents
February 17, 2005

Thank you mister Chairman and members of the Committee for the opportunity to appear today in opposition to House Bill 2326 which makes a number of major changes to the Kansas Guaranty Fund. My name is Larry Magill and I am representing the Kansas Association of Insurance Agents. We have approximately 550 member agencies and branches throughout the state and our members write approximately 70% of the commercial insurance in Kansas. Our members are independent agents free to represent many different insurance companies.

The Kansas Guaranty Fund is the safety net for Kansas consumers and businesses that provides limited protection from the insolvency of their admitted insurance company. As such, our association views it as an extremely important part of insurance regulation in Kansas. The changes before you in HB 2326 are quite significant and we can support some of the changes but not all.

For example, Kansas law allows insurance for vicarious punitive damages and many policies cover punitive damages so long as the state law allows it. Therefore, we would suggest that you add language on line 35 of page 1 of the bill that includes coverage for punitive damages if the insolvent carrier's policy covered them. We see no logical basis to carve out coverage for punitive damages when other kinds of liability claims are covered.

We suggest that you strike (4) on page 1 lines 38 to 43 that eliminates Guaranty Fund coverage for large insureds. They may represent a more sophisticated buyer of insurance but that is no reason to leave them "bare" on the risk of carrier insolvency. Remember that the best regulatory minds in the country that examine insurance companies constantly as their profession are not able to see insolvencies coming. How can even a sophisticated insured be expected to? They will rely on the regulators to protect them just as they protect smaller businesses. There is no exception for FDIC insurance on bank accounts based on the size of the depositor. There should be none in insurance.

We have a problem with the exception to Guaranty Fund coverage at the top of page 2, lines 1-2 where first party coverage for an affiliate of an insurance company that becomes insolvent is not covered. Our concern is that the affiliate may very well have bought that coverage through their insurance agent and could claim later that the agent should have known that the parent insurer was in trouble. Carving out coverage for the affiliate, may have what is probably the unintended consequence of shifting that liability to the agent. And just as with the large commercial account, agents are not equipped to do a better job discovering the true financial strength of an insurer than the insurance

department and rating organization professionals whose careers and businesses are built on doing that.

The most common claim covered by the Guaranty Fund is the claim virtually every insured has for return of their unearned premium. This is a huge issue in the bill and we ask that you strike the provision on page 4, line 38-39 that limits that coverage to $10,000. As it is, the insured has to wait years for the return premiums in most insolvencies and meanwhile pay another insurer for the same coverage. This would add insult to injury and, again, the liability would most likely fall squarely on the agent.

We also ask that you delete the changes on page 29-35 that take away liability claims coverage for insureds with $25 million in assets or more and for affiliates of the insolvent insurer.

With these changes, we think this is a good updating of the current Guaranty Fund act and have no problem with the rest of them. But without our amendments, we are opposed to passage of the bill. Thank you for your time today. We would be happy to provide additional information or answer questions.

HUMANA.

Kansas

House Bill 2366

House Insurance Committee

February 17, 2005

Thank you Chairperson Shultz and members of the House Insurance Committee for the opportunity to testify today. My name is Allan Patek and I am the Government Relations Director for Humana.

I am here today on behalf of Humana to testify in support of House Bill 2366 which would increase affordable health insurance options for Kansas consumers and businesses. This bill places more control over coverage decisions in the hands of consumers and purchasers.

Rising health care costs, largely due to increased hospital, physician and prescription drug costs,[1] have put affordable health insurance coverage out of reach for thousands of individuals and their families and led to an increasing number of uninsured around the country. Studies show that many of the uninsured are from working families, and those employed by small businesses are particularly vulnerable. In fact, result surveys indicate that only about 40% of Kansas firms with less than fifty employees offer health insurance coverage to their employees, compared to 97.6% of firms with more than 50 employees.[2]

The legislation before this committee today provides for lower cost options to help make affordable health coverage more widely available. **House Bill 2366 would do this by removing some of the barriers that prevent health plans from offering more affordable health care choices to Kansas residents.** The problem is restrictions

[1] The Center for Studying Health System Change.
[2] *State Health Facts Online* , The Henry J. Kaiser Family Foundation.

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under current statutes and regulations prohibit certain consumer choice health plans with higher coinsurance levels can be offered to consumers and employers.

For example, some customers want to choose a health plan with a less expensive monthly premium in exchange for broader cost-sharing when they seek out-of-network care. Premiums can be reduced simply by broadening the cost-sharing provisions for out-of-network coverage. **House Bill 2366 clarifies that insurers may offer more flexible products in the individual and group markets with a broad range of cost-sharing arrangements, giving employers and consumers the choice of a wide variety of low, medium and high-cost health plan options.** This change can be accomplished while maintaining the strong consumer protection provided to employers and consumers in required disclosures that outline key benefit provisions including cost sharing at the time or sale and when plans are issued.

While the private sector is already developing and offering new, innovative consumer choice products in the marketplace, the existing law hinders health plans from introducing more affordable options. At Humana, we have developed new products such as SmartSuite and SmartSelect consumer choice options to give employees as many as 50 benefit plan choices, information, and guidance to balance their coverage and costs in ways that are right for them. But even more choices can be made available if additional flexibility is provided to health plans. We believe House Bill 2366 will continue to encourage innovative plan designs and expand the private sector's activities to increase access to affordable health coverage.

With rising health care costs threatening access to health insurance coverage, employers and consumers need -- and *deserve* -- more affordable and attractive health insurance options. While House Bill 2366 is not a panacea to the lower premium costs, it is a start. **It will encourage less expensive consumer choice plan designs in the individual and group markets, while giving consumers the freedom to choose the type of coverage most tailored to fit their individual health care needs.**

Thank you again, Chairperson Shultz for the opportunity to speak before your committee on this important legislation.

Allan Patek
Corporate Director
Government Relations Department
920-337-5618
apatek@humana.com

Legislative Testimony

HB 2366

February 17, 2005

Testimony before the Kansas House Insurance Committee
By Lew Ebert, President and CEO

THE KANSAS CHAMBER

The Force for Business

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Madam Chair and members of the Committee;

I am Lew Ebert with the Kansas Chamber of Commerce and we are appearing in support of HB 2366 on behalf of over 10,000 small, medium and large business members that have made it clear to us that health care and health insurance costs are their number one priority.

HB 2366 arose from a Health Care Working Group that we convened last fall to study a wide range of ideas directed toward addressing the health care cost problems our members face in Kansas. The Work Group discovered that member firms were finding it difficult to purchase health insurance products with benefit designs that many believe would work to lower health insurance costs. As an example, the new wording at the top of page two of the bill would address regulatory restrictions on the maximum differential between coinsurance levels insurance companies are allowed to impose on insured persons for services they receive at in-network providers as compared to out-of-network providers. This amendment would suggest that insurers ought to be free to design benefit plans with a wide range of flexibility governing deductibles, coinsurance and co-payment levels. We support that sort of flexibility and think that regulatory restrictions that sometimes date from decades past ought to be revisited if they no longer make sense in the type of cost environment we now find ourselves in.

As for the wording stricken from section 1(d), the Work Group found it confusing and unnecessary. This section of existing law appears to give the Commissioner the authority to disapprove insurance contracts that were previously approved by the Commissioner, if the Commissioner deems the premiums associated with those contracts to be unreasonable in relation to the premium charged. We think that since the Commissioner has the right to review both premiums and contracts before either are approved for use in Kansas, there really isn't a need for a retrospective disapproval process.

As you might suspect, Kansas based businesses believe they are at their best when freed of unnecessary regulatory red tape and when competition is allowed to manifest itself in lower costs. Those concepts are what are in play in HB 2366. Providing flexibility to insurers by eliminating unnecessary regulation will allow for innovate benefit designs that can only work to our advantage in our push to impact health care costs.

With that, I would be happy to answer any questions you may have.

The Kansas Chamber, with headquarters in Topeka, is the statewide business advocacy group moving Kansas towards becoming the best state in America to do business. The Kansas Chamber and its affiliate organization, The Kansas Chamber Federation, have more than 10,000 member businesses, including local and regional chambers of commerce and trade organizations. The Chamber represents small, medium and large employers all across Kansas.

House Insurance
Date: 2-17-05
Attachment # 9

Wichita Independent Business Association

THE VOICE OF INDEPENDENT BUSINESS

Testimony by Cliff Sones
in Support of HB 2366
House Insurance and Labor Committee
February 17, 2005

Chair Shultz and Honorable Committee Members,

Health care and health insurance costs are an extremely important issue for the members of WIBA/KOPE and we support HB 2366.

The business community statewide has found it difficult to purchase health insurance products with benefit designs that many believe would work to lower health insurance costs. As an example, the new wording at the top of page two of the bill would address regulatory restrictions on the maximum differential between coinsurance levels insurance companies are allowed to impose on insured persons for services they receive at in-network providers as compared to out-of-network providers. This amendment would suggest that insurers ought to be free to design benefit plans with a wide range of flexibility governing deductibles, coinsurance and co-payment levels. We support that sort of flexibility and think that regulatory restrictions that are totally outdated ought to be revisited and abandoned if they no longer make sense in today's health care system.

Kansas based businesses believe they are at their best when freed of unnecessary regulatory red tape and when competition is allowed to manifest itself in lower costs. These concepts are available in HB 2366. Providing flexibility to insurers by eliminating unnecessary regulation will allow for innovative benefit designs that will work to everyone's advantage as health care costs continue to escalate.

The members of WIBA/KOPE urge you to support HB 2366.

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316-267-8987 / 1-800-279-9422 / FAX 316-267-8964 / E-mail: info@wiba.org / Web Site: www.wiba.org

Polsinelli | Shalton
Welte | Suelthaus PC

Memorandum

TO: THE HONORABLE CLARK SHULTZ, CHAIR
HOUSE INSURANCE COMMITTEE

FROM: WILLIAM W. SNEED, LEGISLATIVE COUNSEL
AMERICA'S HEALTH INSURANCE PLANS

RE: HOUSE BILL 2366

DATE: FEBRUARY 17, 2005

Mr. Chairman, Members of the Committee: My name is Bill Sneed and I represent America's Health Insurance Plans (AHIP). AHIP is the national trade association representing nearly 1300 member companies providing health insurance coverage to more than two hundred million Americans. We appreciate the opportunity to testify in favor of House Bill 2366.

First, it is our understanding that the proponent's of the bill are going to request lines 31-43 on page one, and the stricken language on line 1 of page two, to be restated. We believe this is appropriate. This adds the ability to have multiple deducts, etc. Thus, allowing additional insurance products in the market place.

Based upon the foregoing, we respectfully request that the committee to act favorably on House Bill 2366.

Respectfully submitted,

William W. Sneed

WWS:pmk

030825 / 066955

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House Insurance
Date: 2-17-05
Attachment # 11

Lenexa
Chamber of Commerce

The Historic Lackman-Thompson Estate
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Fax 913.888.3770

TO: Representative Clark Shultz, Chairman
Members, House Insurance Committee

FROM: Ashley Sherard, Vice-President
Lenexa Chamber of Commerce

DATE: February 17, 2005

RE: **HB 2366—Removal of Certain Limitations on Accident and Health Insurance Plans**

The Lenexa Chamber of Commerce would like to express its support for the concepts embodied in HB 2366, which would remove certain limitations on accident and health insurance plan deductibles, coinsurance, and similar payments.

Most health care coverage in the U.S. is provided through an employer. Unfortunately, employers have absorbed several years of double-digit cost increases for employee health benefits. Higher costs mean fewer employers can afford to provide quality health care coverage for their employees, particularly among small businesses. In some cases benefits may be eliminated altogether. Of those employers that continue to provide coverage, substantial cost increases are often managed by reducing benefits or by requiring employees to contribute more toward their plans.

This prevention or loss of health care coverage endangers employees and their families, promotes costly emergency health care, and makes it more difficult for businesses to attract and retain quality employees.

We believe HB 2366 is a key step in the right direction. Allowing insurers additional flexibility in the design of accident and health insurance plans would help ensure that businesses and employees have a range of affordable coverage options from which to choose.

For these reasons, the Lenexa Chamber of Commerce urges the committee to consider the concepts in HB 2366 favorably. Thank you for your time and consideration of this important issue.

House Insurance
Date: 2-17-05
Attachment # 12

KANSAS DENTAL ASSOCIATION

Date: February 17, 2005

To: House Committee on Insurance

From: Kevin J. Robertson, CAE
Executive Director

RE: Testimony on HB 2366

Chairman Schultz and members of the committee I am Kevin Robertson, executive director of the Kansas Dental Association (KDA) representing 1,168, or some 80% of the state's licensed dentists. I am sorry I cannot be with you in person today, but I am currently in Salina preparing for our fourth Kansas Mission of Mercy (KMOM) project this weekend.

The **KDA opposes HB 2366** as it would remove the oversight of the Commissioner of Insurance and her ability to protect the best interest of the citizens of Kansas with regard to their health insurance options. The KDA believes this oversight over the insurance industry is essential, and the power of the Commissioner of Insurance, a statewide elected official, should not be usurped.

I urge you to oppose HB 2366.

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Topeka, Kansas 66604-2398
Phone: 785-272-7360
Fax: 785-272-2301

House Insurance
Date: 2-17-05
Attachment # 13

Kansas
Insurance
Department

Sandy Praeger COMMISSIONER OF INSURANCE

COMMENTS ON
HOUSE BILL 2366
ASSISTANT COMMISSIONER ROBERT TOMLINSON
HOUSE COMMITTEE ON INSURANCE
FEBRUARY 17, 2005

Mr. Chairman and Members of the Committee,

Thank you for the opportunity to appear before you to present testimony on House Bill 2366. The Kansas Insurance Department supports the intention of this legislation to provide more flexible insurance plans for consumers and for employers.

Commissioner Praeger strongly supports public policy which addresses skyrocketing health insurance premiums, and enables small businesses to find affordable health insurance plans. We understand that HB 2366 is an effort to do that, and the Kansas Insurance Department would like to be a partner in that effort.

As you will note, we are neutral on this bill because we have not yet been able to determine the impact of this particular language on the body of the Kansas insurance code. We would invite the opportunity to discuss this public policy initiative and move forward with providing Kansas consumers and small businesses the best options possible for affordable health care insurance.

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Testimony
Before the House Insurance Committee
On House Bill 2366
By Larry Magill
Kansas Association of Insurance Agents
February 17, 2005

Thank you mister Chairman and members of the Committee for the opportunity to appear today as a neutral party with concerns about House Bill 2366. The bill makes a number of significant changes to the Kansas' individual and group health insurance statutes. My name is Larry Magill and I am representing the Kansas Association of Insurance Agents. We have approximately 550 member agencies and branches throughout the state and our members write approximately 70% of the commercial insurance in Kansas. Our members are independent agents free to represent many different insurance companies.

We are not entirely sure what the stricken language and the new wording on page 2 do but it appears to take away the Department's ability to approve health insurance forms. One concern with this would be if it were used to increase the penalty for going out of network. Right now the Department has a rule that the penalty in the co-payment can be no more than 30%. The language at the top of page 2 appears to take that lid off. My members who do a lot of health insurance think that's a pretty significant penalty now and would hate to see it go higher.

But generally we are in favor of anything that will bring more health insurance markets to Kansas and increase competition and choices for the consumer.

House Insurance
Date: 2-17-05
Attachment # 15

TESTIMONY OF PHILIP R. O'CONNOR, Ph.D.
WITH RESPECT TO HOUSE BILL No. 2184
February 17, 2005

Thank you Mr. Chairman and members of the Committee, my name is Philip R. O'Connor. I am appearing here today in support of House Bill No. 2184. My support is based on my experience both as an insurance regulator in Illinois and as a long-time analyst of the merits of relying on competitive forces in the setting prices for both business and personal lines property and casualty insurance rates.

There are several salient points that deserve attention and which I think are amply supported by over thirty-years of experience around the country and by a substantial body of academic and governmental research. Part of the personal experience I draw on is that of serving as chairman of the National Association of Insurance Commissioners (NAIC) group tasked with drafting the first model competitive rating law in 1980. Also, as Director of Insurance for the State of Illinois, I had the good fortune to operate with the most competitively oriented rate regulatory situation in the country. I would be happy to expand on Illinois' experience if asked.

First, House Bill No. 2184 takes a well traveled path in that it presumes that which can be easily observed, a currently competitive market in personal lines P&C insurance. The bill then provides for a regulatory review of personal lines of P&C coverage as a backstop in the event that the Insurance Commissioner determines that the market for personal lines insurance is non-competitive. This same approach is in place for business insurance lines in Kansas and for personal and business lines in many other states.

Second, by starting with the rebuttable presumption of a competitive market, the Legislature and the State's regulatory designee, the Commissioner of Insurance, will be making a policy decision to focus limited governmental and analytical resources on the things that really matter rather than on things that are best left to the dynamics of the market. Any state department of insurance has capable, astute professionals whose

talents are made best of use of in addressing problems and complex issues as opposed to reviewing filings on a largely ministerial basis.

Third, the Legislature would justifiably have a reasonable expectation that over time reliance on competitive pricing rather than prior approval rate making will benefit insurance consumers. Insurers are more likely to be attracted to a market in which improved efficiency, better product offerings and market responsive pricing will be stronger determinants of success and profit than will be the skills associated with navigating regulatory waters. More choices and better pricing flow from a stronger competitive climate.

Fourth, there is no basis in experience for expecting that moving from prior approval to competitive pricing will disadvantage insurance consumers. My own research, conducted fairly regularly since 1978 is consistent with the overwhelming body of research on the topic of competitive pricing. Competitive pricing works and works well. Competitive pricing does not produce results that can be considered less beneficial than those of prior approval ratemaking. Competitive pricing appears to actually produce better results by virtually every measure. Such measures include lower residual market populations, overall price levels, numbers of companies attracted to the market and ability of customers to find what they need to meet their insurance requirements.

Finally, Kansas has generally maintained a reputation as having a good insurance department and a reasonably attractive market. However, if there is one thing certain in life it is that no matter how well you are doing something there is a better way to do it. In that respect, House Bill No. 2184 provides an approach that has the imprimatur of the National Conference of Insurance Legislators (NCOIL) and is consistent with the various competitive rate regulatory models bills developed by the National Association of Insurance Commissioners (NAIC). It is a reasonable forward step in further updating Kansas ratemaking law that has its origins in measures adopted in the aftermath of World War II when conditions in personal lines insurance were quite different.

Thanks you for the opportunity to present my views and I would be happy to answer any questions you may have to the extent that I can.

PHILIP R. O'CONNOR, PH.D.

Phil O'Connor is President of PROactive Strategies, a Chicago firm providing policy analysis and advice in the regulation of insurance. He is also currently Vice President of Constellation NewEnergy, Inc., the nation's leading provider of competitive retail electricity. Over the past two decades, Dr. O'Connor has been recognized as an expert in the use of competition as a regulator of both the insurance and utility industries. He has spoken and written widely on these topics. During his service as Illinois Director of Insurance, 1979-82, Dr. O'Connor chaired the NAIC Task Force that drafted the Model Alternative Open Competition Rating Law covering all property and casualty lines, including workers compensation. Prior to serving as Director he was Deputy Director for Research and Urban Affairs.

From 1983 through 1985, Dr. O'Connor was Chairman of the Illinois Commerce Commission, the utility regulatory body in Illinois, and was an early advocate of competition in telecommunications, natural gas and electricity, all of which have emerged as public policies around the country. After leaving State government, Dr. O'Connor formed Palmer Bellevue Corporation, an energy and insurance consulting firm that became a part of Coopers & Lybrand in 1993. In July 1998, he established the Midwest business of NewEnergy.

Dr. O'Connor has been an expert witness in a variety of significant insurance regulatory matters. He has also frequently testified to state legislative bodies on competitive pricing in the property and casualty and workers compensation markets, and has served on the boards of several U. S. life insurance companies.

During his tenure as Illinois Director of Insurance, Dr. O'Connor chaired the NAIC task force which prepared the model property and casualty competitive rating law and was responsible for securing passage in 1982 of legislation making Illinois the first state to implement competitive pricing in worker's compensation insurance.

Dr. O'Connor has had extensive political experience including service as Political Director of Governor Jim Thompson's successful third-term election campaign in 1982 and as General Chairman of Governor Jim Edgar's successful 1994 re-election campaign. He also was administrative assistant to U.S. Representative George Miller of California in the mid-1970s. He was appointed by three governors as a member of the Illinois State Board of Elections from 1998 to 2004 and served as a member of the Bush-Cheney Transition Advisory Committee on Energy.

A native of California, O'Connor attended the University of San Francisco, the Loyola University of Chicago-Rome Campus of Liberal Arts in Italy, graduated *magna cum laude* from Loyola University of Chicago, and received his Masters and Doctoral degrees in Political Science from Northwestern University.

Testimony
Before the House Insurance Committee
On House Bill 2184
By Larry Magill
Kansas Association of Insurance Agents
February 17, 2005

Thank you mister Chairman and members of the Committee for the opportunity to appear today with "conditional" support for House Bill 2184 which makes a number of major changes to the Kansas' insurance rating laws. My name is Larry Magill and I am representing the Kansas Association of Insurance Agents. We have approximately 550 member agencies and branches throughout the state and our members write approximately 70% of the commercial insurance in Kansas. Our members are independent agents free to represent many different insurance companies.

We have to confess that we have not had time to study the bill. My Government Affairs Committee has not met since the bill came out and neither has my Board. We began considering support for some "loosening" of Kansas' rating laws over a year ago but frankly haven't been able to devote much time or resources to it.

But we do recognize that Kansas is among a shrinking minority of states that are characterized as "prior approval". I realize the Department may think of themselves as a "file and use" state since we have a "deemer clause" that allows an insurer to deem its rates approved if it hasn't heard from the Department within 30 days. However, in most instances the insurance companies are reluctant to use the clause and the Department generally does respond with questions before the 30 days has run.

This can be an impediment to attracting new insurance companies into the Kansas' marketplace. Our association is always interested in bringing in quality new markets because our smaller members constantly struggle to find insurers willing to write in small towns and rural areas and especially property insurance in the Wichita area and western Kansas. We approached Auto Owners a year ago because we heard they were a good personal lines market and were expanding into new states. Their first and just about only question for me was whether we were still a prior approval state. That was the end of the conversation.

A second, very important reason we are considering changing our stance on Kansas' rating law is the Federal Government's continued interest in regulating insurance. The "SMART" act has been proposed by Representatives Oxley and Baker and may get hearings this session of Congress. It sets up limited federal regulation. We think one way to stave off this intervention is for the states to go to more of a competition based rating law.

However, we are not willing at this time to eliminate the Department's form approval authority. We would like to move gradually and our experience has shown that this is

the area where the insurance industry and we most often disagree about how to treat exposures and recent trends in society.

Because of the size, complexity and importance of this subject, we would suggest that you refer it for an interim study. We would be happy to answer questions or provide additional information.

Polsinelli | Shalton
Welte | Suelthaus PC

Memorandum

TO: THE HONORABLE CLARK SHULTZ, CHAIRMAN
HOUSE INSURANCE COMMITTEE

FROM: WILLIAM W. SNEED, LEGISLATIVE COUNSEL
THE STATE FARM INSURANCE COMPANIES, INC

RE: HOUSE BILL 2184

DATE: FEBRUARY 17, 2005

Mr. Chairman, Members of the committee: My name is William Sneed and I represent the State Farm Insurance Companies ("State Farm"). State Farm is the largest insurer of home and automobiles in Kansas. State Farm insures one out of every three cars and one out of every four homes in the United States. We appreciate the opportunity to present our thoughts regarding House Bill 2184. Please be advised that as written, we support House Bill 2184.

First, a brief overview of the current insurance rating law in Kansas.

The Kansas insurance rating law is codified in K.S.A. 40-951 through 967.

- All lines are covered except reinsurance, accident and health, aircraft, property and casualty policies sold to large sophisticated insurance consumers called large risks and special risks
- Large Risks have over $5M insured property values or $10M annual gross revenues or insurance premiums in excess of $50k property /$100K general liability
- Special risks are risks designated by the Commissioner, including but not limited to commercial aviation, credit insurance, boiler and machinery , inland marine, fidelity, surety and guaranty bond insurance risks

Current Rate Filing Mechanism in Kansas

- Worker's Compensation rates require prior approval. The KID must first approve the rate before it is implemented.
- Personal lines rates require file and use with a 30-day deemer. Insurer files the rate and must wait 30 days to use subject to the KID disapproval. KID can disapprove if inadequate, excessive, or unfairly discriminatory or if it otherwise fails to meet the requirements of the rating act.

- Commercial is file and use subject to 30-day deemer.
- Large Risks no file per exemption from act.

KID can disapprove a rate if it is:

- Excessive- not assumed excessive in a competitive market, which does not include personal lines. For noncompetitive markets a rate is if it produce or is likely to produce unreasonable profits for the line of insurance or if expenses are unreasonably high in relation to the services provided.
- Inadequate - clearly insufficient, along with investment income, to sustain projected losses and expenses in class of business which it applies.
- Unfairly Discriminatory – in a same class if it fails to reflect differences in expected losses and expenses.

The Effect of Disapproval is as follows:

- Under each rating method if a rate is disapproved the insurer is required to refund the overcharge to affected policyholders unless the overcharge is de minimus.
- The refund is done retrospectively. It begins the date the rate was used not the date of KID disapproval. Thus, although Kansas is use and file, it is this provision that causes insurers not to use the rate until the 30-day period has elapsed.
- At the time the disapproval order is issued, the interim rate will take effect for insurance written or renewed 15 days after the order is issued.
- KID will specific an interim rate at the time the order is issued.
- Insurer may appeal the order and charge the disapproved rate so long as the insurer deposits with the commissioner the difference in total premiums between the disapproved rate and the prior rate to be returned to the insurer or insured as the court deems appropriate. At the court's discretion, the insurer may post a bond in lieu of deposits.
- Most insurers are unwilling to use the disapproved rate due to this section. They will charge the prior rate and litigate the rejection of the disapproved. This hinders our response to market forces be they good, bad or indifferent.

HOUSE BILL 2184 RATE MODERNIZATION

The bill adopts the NCOIL Rate Modernization Act. The Act is a collaborative effort between state legislators, consumers and the industry.

The Lines Covered are:

(a) Commercial and personal property and casualty lines, except ocean marine, aircraft liability, reinsurance, surplus lines and workers compensation, and

(b) Also exempted are title and med malpractice to insure that they are still governed by the current ratemaking system.

The Rate Filing Mechanism_divides the P & C markets into competitive, noncompetitive and large risks. Use and file for personal lines and small commercial lines, that are competitive. Under use and file insurer must file the rate no later than 30 days after rate is in use. In a noncompetitive market, it is use and file with a30 day deemer. Commentary: This means if the personal lines market becomes uncompetitive they revert to the current system. This should give the legislators a level of comfort. Large commercial risks are no file. Markets are assumed to be competitive but KID can hold a hearing to declare a market or line uncompetitive.

Disapproval Grounds available to KID are fair and adequate

(1) Excessive - the rate is likely to produce a long term profit that is unreasonably high for insurance provided. Rates in a competitive market cannot be excessive. If a market is competitive an insurer has to sell at the market price or less to grow or at least maintain market share.

(2) Inadequate - Unreasonably low for insurance provided and endangers solvency of the insurer or the rate may create a monopoly. Prevents large insurers, in personal and commercial lines, from using their economies of scale, to create a monopoly.

(3) Unfairly Discriminatory - Cannot be actuarially justified. In a competitive market, only unfairly discriminatory if it classifies based on color, race creed or origin. In a competitive market an insurer who uses rates that are not actuarially sound will either price themselves out of the market or charge a rate so low that it may be unprofitable.

KID can only disapprove rates prospectively. The order can only affect policies entered into or renewed 30 days after the date of the order. The insurer can appeal the order and the "disapproved" rate can remain in effect so long as the insurer deposits the difference between the disapproved rate and the prior rate, prospectively, in a reserve established by the insurer. The court will have the power of disbursement over the fund.

COMPARISON OF THE TWO SYSTEMS

- The change from file and use to the NCOIL Rate Modernization Act is an evolution not a revolution
- It places reasonable limitations on KID's ability to disapprove rates in a competitive market
- By making rate disapproval prospective it gives insurers the opportunity to respond to market forces without being subjected to retaliatory measures should KID disapprove their rate
- In a competitive market, KID can only disapprove a rate if it is inadequate or discriminates based on creed, race or national origin. The reason in a competitive market, in order to grow or retain market share, an insurer is more likely to underprice its product than overprice.

THE CASE FOR COMPETITION

- Consumers, regulators and insurers are best served by a marketplace in which competition is the primary regulator of insurance rates
- Competition has been tried, tested and proven successful in all segments of our economy including the insurance industry. Strict rate regulation also serves as a disincentive for insurers to enter the market and makes it difficult for insurers to do business there. As of March 2004, only 55 insurers sold homeowners insurance in Texas. The population of Texas is 21 million. That compares unfavorably with 221 insurers in Illinois (12.4 million population) and 112 in South Carolina (4.1 million population). South Carolina moved from prior approval on auto insurance to flex band in 1996. Since the enactment of that measure the number of auto insurers doing business in that state has increased from 78 to 183. In fact, South Carolina was so impressed with these results, that in 2003, they moved from prior approval to flex for homeowners.
- Competition drives innovation. In a competitive market, insurers will develop more innovative policies and pricing structures in an effort to capture a greater share of the market
- Consumers should be allowed to enjoy the benefits of competition with other products and services they purchase such as insurance.
- Kansas would not be alone. Over the last two years, 9 states have adopted some form of rate modernization. 2003- Nebraska (commercial lines) New Hampshire (commercial lines) New Jersey (auto) and Louisiana (personal lines) 2004 – Massachusetts (commercial), Oklahoma (personal lines), Rhode Island (personal lines), South Carolina (homeowners) and South Dakota (Personal and commercial) These changes range from creating a flex in Louisiana to the NCOIL model in Oklahoma.
- In personal lines, 18 states have prior approval, 23 have file and use and 9 have use and file or no file. The use and file states are Oklahoma, Arizona, Idaho, Iowa, Utah and Wisconsin. The no file states are Illinois, Wisconsin and Wyoming.
- Rate regulation increases uncertainty and thereby increases the cost of capital for insures thus discouraging capital commitment and making ultimate rate levels higher
- The majorities of states have use and file for commercial insurance. Modernizing personal lines rate regulation has been more contentious because some public policy makers contend that individual consumers do not have the information to effectively purchase insurance in an open market. However, experience shows that a competitive market is more responsive to the demands of almost every consumer. Competition forces insurers to eliminate inefficiencies and stimulates companies' efforts to attract and retain customers, offering innovative products that provide greater value to consumers. In addition, the internet and cable business channels provide a multitude of information regarding property and casualty personal insurance.

Thus, based upon the foregoing, we respectfully request that the committee to act favorably on House Bill 2184.

I am available for questions at your convenience.

Respectfully submitted,

William W. Sneed

WWS:pmk

019646 / 032884
WWSNE 1169889

18-5

Kansas
Insurance
Department

Sandy Praeger COMMISSIONER OF INSURANCE

COMMENTS ON
HOUSE BILL 2184
ASSISTANT COMMISSIONER ROBERT TOMLINSON
HOUSE COMMITTEE ON INSURANCE
FEBRUARY 17, 2005

Mr. Chairman and Members of the Committee,

Thank you for the opportunity to appear before you to present testimony on House Bill 2184. The Kansas Insurance Department is opposed to this bill because it is not necessary legislation. Furthermore, we feel this legislation damages Kansas consumer protection.

Currently, Kansas already has statutes allowing file and use with a 30-day approval window. During the time period I have been involved in insurance issues in this state, the Kansas Insurance Department has made every effort to move products to market in this short time frame. In fact, in the cases when products do not make it to market within this time frame it is often due to incomplete information on a company's filing. Currently, the National Association of Insurance Commissioners is looking at the possibility of creating a matrix of requirements in each state so that companies will be able to easily provide all necessary information on their first filing. We are exploring the feasibility of this matrix to make filings in individual states easier.

The current 30-day window is crucial for the protection of Kansas insurance consumers. Having the ability to review products before consumers pay their hard-earned dollars for coverage is the cornerstone of effective consumer protection. We believe strongly in the importance of speed-to-market, and we take seriously the need to have the shortest review process possible. As you know, Kansas is one of 12 states with an elected Insurance Commissioner. Mr. Chairman, I believe this fact indicates that Kansans feel they should have a strong voice in the regulation of the insurance industry. Unfortunately, in an effort to speed up the delivery of products to the market, the intent of this bill effectively dilutes the voices of our state's citizens.

Mr. Chairman, I appreciate the opportunity to appear before you today, and I would be happy to stand for any questions you or your committee may have.

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February 17, 2005

To: Members of the State of Kansas House of Representatives Insurance Committee

I appreciate this opportunity to address the committee regarding HB 2184 on behalf of the Kansas State Council of Fire Fighters (KSCFF). This bill would erode much of the protections that insurance consumers have in the State of Kansas at this time, under the present laws.

The Kansas Insurance Commissioners Office has protected the citizens of Kansas for many years under the present law, but if HB 2184 was to pass the citizens of Kansas would be the big loser. We feel this bill would reduce the Insurance Commissioner's office ability to protect the consumer from unfair insurance rates. The Kansas Insurance Commissioner's office sets these rates at the present time but we feel under HB 2184 the insurance companies would be setting their own rates without any input from the Kansas Insurance Commissioner.

This bill would allow the insurance companies to be able to charge different fire rates to home owners depending on what part of the fire district they live in. At the present time fire departments are given a rating by the Insurance Services Office (ISO) which is a national organization. What that means is, whatever rating a fire department is given that is for their whole fire district. We feel under HB 2184 the insurance companies would be able to give different ratings in a fire district depending on where you live, which could cause many problems for the homeowners in the State of Kansas.

For the reasons stated above , the members of the Kansas State Council of Fire Fighters would ask you to vote against HB 2184.

If you have any questions please contact me at (785) 286-2929 or email: djpiaff83@yahoo.com.

Respectfully submitted,

Dennis J. Phillips

Dennis J. Phillips
Lobbyist, KSCFF

House Insurance
Date: 2-17-05
Attachment # 20