Approved: ARB/jsb

Date: 2/17/2010

MINUTES OF THE HOUSE FINANCIAL INSTITUTIONS COMMITTEE

The meeting was called to order by Chairman Anthony Brown at 3:35 p.m. on February 10, 2010, in Room 784 of the Docking State Office Building.

All members were present except:

Representative Tom Burroughs- absent
Representative Dale Swenson - absent
Representative Bob Grant- excused

Committee staff present:

Bruce Kinzie, Office of the Revisor of Statutes
Sean Ostrow, Office of the Revisor of Statutes
Melissa Calderwood, Kansas Legislative Research Department
Lauren Douglass, Kansas Legislative Research Department
Joyce Bishop, Committee Assistant

Conferees appearing before the Committee:

Kathleen A. Olsen, Sr. Vice President, General Counsel, Kansas Banker's Association

Others attending:

See attached list.

Chairperson Brown opened the floor for discussion and possible action on **HB 2473 - Prohibiting sellers, lessors and credit card issuers from imposing a surcharge on credit and debit card transactions.**

Rob Olson made a motion to recommend **HB 2473** favorable for passage and place it on the consent calendar. Phil Hermanson seconded the motion. The motion passed unanimously.

Chairperson Brown opened the floor for discussion and possible action on **HB 2608 - Financial institutions, examinations and annual assessments.**

Rob Olson made the motion to recommend **HB2608** favorably for passage. Cindy Neighbor seconded the motion. The motion passed unanimously.

Chairperson Brown opened the floor for discussion and possible action on **HB 2609 - Banks and banking, general power, purchase life insurance.**

Cindy Neighbor moved to recommend **HB 2609** favorably for passage. Rob Olson seconded the motion.

Richard Proehl distributed an amendment for **HB 2609** (Attachment 1)

Richard Proehl made a substitute motion to amend **HB 2609.** Cindy Neighbors seconded the motion.

Nile Dillmore requested an explanation of the amendment.

Bruce Kinsey explained the amendment inserts language that clarifies the interagency statement and who is making the statement to the agencies.

The Motion to amend **HB 2609** passed unanimously.

Richard Proehl introduced a second amendment to **HB 2609** (Attachment 2).

Richard Proehl then made a motion to amend **HB 2609.** Cindy Neighbor seconded the motion.

Mario Goico asked to know if the bill and amendment effects credit unions. Richard Proehl said it only effects banks.

Rob Olson asked what this amendment does.

Minutes of the House Financial Institutions Committee at 3:30 p.m. on February 10, 2010, in Room 784 of the Docking State Office Building.

Chairperson Brown asked Kathleen Olsen, General Counsel of the Kansas Banker's Association to address the committee regarding the question on the amendment.

Kathleen Olson explained the amendment basically allows banks to hold stock of another state's Bankers Bank.

The amendment passed unanimously.

Neighbor made the motion to pass **HB 2609** out of committee as amended. Rob Olson seconded the motion. The motion passed unanimously.

The next meeting will be scheduled after Turn Around.

The meeting was adjourned at 3:45p.m.

HOUSE FINANCIAL INSTITUTIONS COMMITTEE
3:30pm,
Room 784, Docking State Office Building

GUEST LIST

DATE: February 10, 2010

NAME	REPRESENTING
TED HENRY	CAPITOL STRATEGIES
Kathy Olsen	Ks Bankers Assn.
John Peterson	Capitol Strategies
Chris Gigstad	Federico Consulting
Matt Goddard	Heartland Community Bankers Assoc.
Tom Thull	Office of the State Bank Commissioner
SHAWN MITCHELL	COMMUNITY BANKER ASSOC.
Debra Higgins	Credit union of america

~~policies for the sole purpose of providing employee deferred compensation and benefit plans subject to the limitations listed herein. If the bank has the authority to direct the investments of the cash surrender value of the policy, those investments shall be limited solely to assets which may be directly purchased by the bank for its own account. The limitations set forth in paragraphs (a) and (b) of this subsection do not apply to any such life insurance policies in place before July 1, 1993. Funding for the payment of employee compensation and benefit plans as well as the benefits derived may be made or split in a joint manner between the bank, employee or bank holding company as in "split dollar" or other insurance plans.~~

~~(a) Life insurance purchased and held on the life of executive officers and directors are~~ *in a manner consistent with the parameters outlined in the interagency statement of the purchase and risk management of life insurance, federal deposit insurance corporation financial institution letter 127-2004, effective December 7, 2004,* subject to the following limitations:

issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Thrift Supervision on December 7, 2004; and set out in the respective agencies' issuances, including the

~~(i)~~ *(a)* The cash surrender value of any life insurance policy ~~on an executive officer or director~~ *or policies* underwritten by any one life insurance company ~~cannot~~ *shall not* at any time exceed 15% of the bank's capital stock, surplus, undivided profits, ~~loan loss reserve~~ *allowance for loan and lease losses*, capital notes and debentures and reserve for contingency, unless the bank has obtained the prior approval of the state bank commissioner;

~~(ii)~~ *(b)* the cash surrender value of life insurance policies ~~on executive officers or directors~~, in the aggregate from all companies, cannot at any time exceed 25% of the bank's capital stock, surplus, undivided profits, ~~loan loss reserve~~ *allowance for loan and lease losses*, capital notes and debentures and reserve for contingency, unless the bank has obtained the prior approval of the state bank commissioner; *and*

(c) the limitations set forth in paragraphs (a) and (b) shall not apply to any life insurance policy in place prior to July 1, 1993.

~~(iii) the authority to hold life insurance on any executive officer ceases if the executive officer is no longer employed by the bank or no longer meets the definition of an executive officer;~~

~~(iv) the authority to hold life insurance on a director ceases when that director is no longer a member of the board of directors;~~

~~(v) the bank's board of directors must approve and document the purchase of any life insurance, including the reasonableness of such purchase; and~~

~~(vi) except as part of a reasonable compensation or benefit plan, a bank is not authorized to purchase life insurance as an estate management device for the benefit of officers, directors or employees who are also~~

HOUSE FINANCIAL INSTITUTIONS
DATE: 2/10/2010
ATTACHMENT: 1

KANSAS

MARK PARKINSON, Governor

OFFICE OF THE STATE BANK COMMISSIONER

J. THOMAS THULL, Bank Commissioner

HOUSE FINANCIAL INSTITUTIONS COMMITTEE

February 8, 2010

Chairman Brown and Members of the Committee:

My name is Judi Stork and I am the Deputy Commissioner for the Banking Division. I am here today in support of HB 2609. This bill amends K.S.A. 9-1101, which is the powers section for the state banks of Kansas. Currently, subsection (24) sets forth certain provisions under which a state bank may purchase life insurance. In 2005, the Commissioner issued Special Order 2005-1 that granted parity for state banks with national banks with regard to the purchase of life insurance. It allows state banks to purchase life insurance for the same reasons and to the same extent as national banks. An example of this would be the allowance for a bank to purchase insurance in connection with <u>current</u> employee benefit plans. The Kansas statute only allowed for <u>deferred</u> compensation and benefit plans. The Special Order also incorporated the requirement for a bank to have a thorough pre-purchase analysis as well as guidelines the banks must follow in the purchase of the product, to ensure the bank understands the risks of BOLI. It further requires a comprehensive risk management process for holding the BOLI. The amendment of this statute is simply to codify the authority Kansas banks have had for five years under the Special Order. It will also eliminate confusion of any reader who looks only to K.S.A. 9-1101 and is unaware of the existence of the Special Order.

I would be happy to stand for questions from the committee.

700 S.W. Jackson, Suite 300 · Topeka, Kansas · 66603-3796 · 785-296-2266 · Fa

HOUSE FINANCIAL INSTITUTIONS
DATE: 2/10/2010
ATTACHMENT: 2-1

Financial Institution Letters

Bank-Owned Life Insurance
Interagency Statement on the Purchase and Risk Management of Life Insurance

FIL-127-2004
December 7, 2004

Summary: The federal banking agencies are providing guidance on the safe and sound banking practices they expect institutions to employ for the purchase and ongoing risk management of bank-owned life insurance.

Highlights:

- Institutions should have a comprehensive risk management process for purchasing and holding bank owned life insurance (BOLI).
- The safe and sound use of BOLI depends on effective senior management and board oversight.
- Institutions should establish policies and procedures governing their BOLI holdings, including meaningful risk limits.
- A sound pre-purchase analysis helps ensure that institutions understand the risks, rewards and unique characteristics of BOLI.
- Institutions also should monitor BOLI risks on an ongoing basis subsequent to purchase.

Continuation of FIL-127-2004

Distribution:
FDIC-Supervised Banks

Suggested Routing:
Chief Executive Officer
Chief Financial Officer
Chief Risk Officer

Related Topics:
Section 24 of the Federal Deposit Insurance Act and Part 362 of the FDIC's Regulations

Attachment:
Executive Summary
Interagency Statement on the Purchase and Risk Management of Life Insurance

Contact:
FDIC Regional Accountant or Christine M. Bouvier, Senior Policy Analyst, Division of Supervision and Consumer Protection cbouvier@fdic.gov or 202 898-7289.

Printable Format:
The following documents are formatted as PDF files.

PDF Help - Information on downloading and using the PDF reader.

FIL-127-2004 48k
Executive Summary 75k
Interagency Statement on the Purchase and Risk Management of Life Insurance Contents 15k
Interagency Statement on the Purchase and Risk Management of Life Insurance 126k

HOUSE FINANCIAL INSTITUTIONS
DATE: 2/10/2010
ATTACHMENT: 2-2

Note:
FDIC Financial Institution Letters (FILs) may be accessed from the FDIC's Web site at www.fdic.gov/news/news/financial/2004/index.html.

To receive FILs electronically, please visit http://www.fdic.gov/about/subscriptions/fil.html.

Paper copies of FDIC FILs may be obtained through the FDIC's Public Information Center, 801 17th Street, NW, Room 100, Washington, DC 20434 (1-877-275-3342 or (703) 562-2200).

Financial Institution Letters
FIL-127-2004
December 7, 2004

Bank-Owned Life Insurance
Interagency Statement on the Purchase and Risk Management of Life Insurance

The federal banking agencies are providing guidance on the safe and sound banking practices they expect institutions to employ for the purchase and ongoing risk management of bank-owned life insurance.

The federal banking agencies are issuing the attached Interagency Statement on the Purchase and Risk Management of Life Insurance to institutions to help ensure that their risk management processes for bank-owned life insurance (BOLI) are consistent with safe and sound banking practices. The interagency statement also provides guidance for split-dollar arrangements and the use of life insurance as security for loans. Among the safe and sound banking practices discussed in this interagency statement is the need for senior management and board oversight of BOLI, including both a thorough pre-purchase analysis of risks and rewards and post-purchase risk assessment. The guidance discusses the permissibility of BOLI purchases and holdings, as well as their risks and associated safety and soundness considerations. An appendix to the interagency statement describes the types of life insurance and the purposes for which institutions commonly purchase life insurance and also contains a glossary of BOLI-related terms.

The guidance in the Interagency Statement for the pre-purchase analysis of life insurance applies to all BOLI contracts entered into after December 7, 2004. The guidance concerning the ongoing risk management of BOLI subsequent to its purchase applies to all holdings of life insurance regardless of when purchased.

To provide institutions with an overview of the Interagency Statement, an executive summary of the guidance is attached. For complete information on the FDIC's supervisory expectations for institutions that purchase and hold BOLI, please refer to the statement itself.

Questions about the Interagency Statement on the Purchase and Risk Management of Life Insurance may be addressed to your FDIC Regional Accountant or Senior Policy Analyst Christine M. Bouvier, Division of Supervision and Consumer Protection, at (202) 898-7289 or cbouvier@fdic.gov.

Michael J. Zamorski
Director
Division of Supervision and Consumer Protection

HOUSE FINANCIAL INSTITUTIONS
DATE: 2/10/2010
ATTACHMENT: 2 - 3

Financial Institution Letters

Executive Summary - Interagency Statement on the Purchase and Risk Management of Life Insurance

Institutions purchase life insurance for a variety of purposes, including recovering the cost of providing employee benefits and protecting against the loss of "key persons." Institutions should have a comprehensive risk management process for purchasing and holding bank-owned life insurance (BOLI).

The two broad types of life insurance are temporary (term) insurance and permanent insurance. Temporary (term) insurance provides protection for a specified time period, its premiums do not have a savings component, and it does not create a cash surrender value (CSV). Permanent insurance is intended to provide life insurance protection for the entire life of the insured. Its premium structure includes a savings component, thereby creating a CSV. If permanent insurance is surrendered before death, surrender charges may be assessed against the CSV.

The ability of FDIC-supervised banks to purchase life insurance is governed by state law. Some state laws permit state-chartered banks to engage in activities (including making investments) that go beyond the authority of a national bank. Section 24 of the Federal Deposit Insurance Act generally requires FDIC-supervised banks to obtain the FDIC's consent before engaging as principal in activities that are not permissible for a national bank.

The safe and sound use of BOLI depends on effective senior management and board oversight. An institution's board of directors must understand the complex risk characteristics of the institution's insurance holdings and the role this asset is intended to play in the institution's overall business strategy.

Each institution should establish internal policies and procedures governing its BOLI holdings, including guidelines that limit the aggregate CSV of policies from any one insurance company as well as the aggregate CSV of policies from all insurance companies. It is generally not prudent for an institution to hold BOLI with an aggregate CSV that exceeds 25 percent of its Tier 1 capital. Therefore, the FDIC expects an institution that plans to acquire BOLI in an amount that results in an aggregate CSV in excess of this concentration limit, or any lower internal limit, to gain prior approval from its board of directors or the appropriate board committee. In this situation, management is expected to justify that any increase in BOLI resulting in an aggregate CSV above 25 percent of Tier 1 capital does not constitute an imprudent capital concentration.

The management of an institution should conduct a thorough pre purchase analysis to help ensure that the institution understands the risks, rewards, and unique characteristics of BOLI. The nature and extent of this analysis should be commensurate with the size and complexity of the potential BOLI purchases and should also take into account existing BOLI holdings. An effective pre-purchase analysis involves the following actions by management:

(1) Identify the need for insurance and determine the economic benefits and appropriate insurance type, i.e., permanent or temporary (term) insurance.
(2) Quantify the amount of insurance appropriate for the institution's objectives.
(3) Assess vendor qualifications, including its reputation, experience, financial soundness, and commitment to the BOLI product and the adequacy of its services.
(4) Review the characteristics of the available insurance products and select those that best match the institution's objectives, needs, and risk tolerance.
(5) Select an insurance company after evaluating and performing credit analyses on the companies from which insurance may be purchased.
(6) Determine the reasonableness of compensation provided to the insured employee if the insurance provides additional compensation to the employee.
(7) Analyze the risks associated with the insurance and the institution's ability to monitor and respond to these risks.
(8) Evaluate alternatives to the purchase of BOLI for accomplishing the institution's objectives.
(9) Document the pre-purchase analysis and the purchase decision.

A comprehensive assessment of BOLI risks on an ongoing basis is an important element of the risk management process, especially for an institution whose aggregate BOLI holdings represent a capital concentration. Management should review the performance of the institution's insurance assets with its board of directors at least annually.

The BOLI risks that should be assessed, managed, monitored, and controlled include liquidity, transaction/operational (including the tax and insurable interest implications), reputation, credit, interest rate, compliance/legal, and price risk. All of these risks are present in permanent insurance. In particular, the CSV of permanent life insurance is one of the least liquid assets on an institution's balance sheet. In contrast, temporary insurance does not expose an institution to liquidity, interest rate

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or price risk because it does not have a CSV. These risks need not be evaluated in the comprehensive assessment of the risks of temporary insurance.

Institutions should follow generally accepted accounting principles (GAAP) applicable to holdings of life insurance for reporting purposes. Under GAAP, only the amount that could be realized under an insurance contract as of the balance sheet date (that is, the CSV reported to the institution by the insurance carrier, less any applicable surrender charges not reflected by the insurance carrier in the reported CSV) is reported as an asset.

For risk-based capital purposes, an institution that owns general account permanent insurance should apply a 100 percent risk weight to its claim on the insurance company. If an institution owns a separate account policy and can demonstrate that it meets certain requirements, it may choose to apply a "look-through" approach to the underlying assets to determine the risk weight. In no case, however, may the risk weight for the separate account policy (excluding any general account and stable value protection portions, which generally receive a 100 percent risk weight) be less than 20 percent.

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