HOUSE BILL No. 2177

AN ACT concerning insurance; relating to the accounting treatment of certain derivative instruments used in hedging transactions; version of risk-based capital instructions in effect; exempting certain domestic insurers from filing enterprise risk reports; defining amount involved for fraudulent insurance acts; amending K.S.A. 2018 Supp. 40-2,118, 40-2c01 and 40-3305 and repealing the existing sections; also repealing K.S.A. 2018 Supp. 40-2,118a.

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

New Section 1. (a) As used in this section:

(1) "Eligible derivative asset" means an option, as defined in K.S.A. 40-2b25, and amendments thereto, that is purchased or written to hedge the growth in interest credited to an indexed product as a direct result of changes in each related external index.

(2) "External index" means a list of securities, commodities or other financial instruments that is published or disseminated by a source other than an insurance company, including Standard & Poor's, nasdaq and dow jones.

(3) "Hedging transaction" has the meaning specified in K.S.A. 40-2b25, and amendments thereto.

(4) "Indexed annuity products" means contracts that:

(A) Provide a minimum guaranteed interest accumulation on a portion of all premium payments; and

(B) include provisions under which interest is credited based upon the performance of one or more external indices.

(5) "Indexed life products" means life insurance policies that:

(A) Provide a minimum guaranteed interest accumulation on a portion of all premium payments; and

(B) include provisions under which interest is credited based upon the performance of one or more external indices.

(6) "Indexed products" means indexed annuity products and indexed life products.

(7) "Interest-crediting period" means the length of time over which the performance of each external index is measured for purposes of determining the amount of interest credited under an indexed product.

(b) (1) Any insurance company may account for eligible derivative assets at amortized cost if the insurance company can demonstrate that such eligible derivative assets meet the following criteria for an economic hedge:

(A) At inception of the hedge, or as of the date that an insurance company begins using the accounting practices set forth herein, if later, there must be a formal documentation of the economic hedging relationship and the insurance company's risk management objective and strategy for undertaking the economic hedge, including identification of the specific eligible derivative assets purchased to hedge indexed products, the nature of the particular risk being hedged, and how the eligible derivative assets' effectiveness will be assessed, retrospectively and prospectively, on a qualitative basis; and

(B) at inception of the hedge, or as of the date that an insurance company begins using the accounting practices set forth herein, if later, and at the end of each quarterly reporting period thereafter, the insurance company must maintain documentation that the economic hedge is expected to be and continues to be highly effective as defined by the criteria in subparagraph (A) in achieving offsetting changes in fair value attributable to the hedged risk during the period that the economic hedge is designated.

(2) Eligible derivative assets purchased or written with a year or less to maturity or expiration shall not be required to be amortized.

(c) (1) The following accounting practices shall apply to the indexed annuity product reserves:

(A) Indexed annuity product reserve calculations shall be based on actuarial guideline XXXV assuming the market value of the eligible derivative assets associated with the current interest crediting period is zero, regardless of the observable market for the eligible derivative

assets.

(B) At the conclusion of each interest-crediting period, the interest credited to an indexed annuity product shall be reflected in the indexed annuity product reserve as realized, based on the actual performance of the relevant external index or external indices.

(2) The accounting practices specified in this subsection shall not apply to the calculation of indexed life product reserves.

(d) (1) If an insurance company elects to use the alternative accounting practices prescribed herein, it shall report quarterly to the commissioner of insurance, for analysis purposes, the market value of its eligible derivative assets and what the actuarial guideline XXXV reserve would be, using the market value of such eligible derivative assets.

(2) An insurance company that elects to use the alternative accounting practices prescribed herein shall not change its accounting practices back to those that would apply in the absence of the statute without the prior approval of the commissioner of insurance.

(e) The commissioner of insurance shall have the power to adopt all reasonable rules and regulations necessary to implement this section.

Sec. 2. K.S.A. 2018 Supp. 40-2c01 is hereby amended to read as follows: 40-2c01. As used in this act:

(a) "Adjusted RBC report" means an RBC report which has been adjusted by the commissioner in accordance with K.S.A. 40-2c04, and amendments thereto.

(b) "Corrective order" means an order issued by the commissioner specifying corrective actions which the commissioner has determined are required to address an RBC level event.

(c) "Domestic insurer" means any insurance company or risk retention group which is licensed and organized in this state.

(d) "Foreign insurer" means any insurance company or risk retention group not domiciled in this state which is licensed or registered to do business in this state pursuant to article 41 of chapter 40 of the Kansas Statutes Annotated*, and amendments thereto,* or K.S.A. 40-209, and amendments thereto.

(e) "NAIC" means the national association of insurance commissioners.

(f) "Life and health insurer" means any insurance company licensed under article 4 or 5 of chapter 40 of the Kansas Statutes Annotated, and amendments thereto, or a licensed property and casualty insurer writing only accident and health insurance.

(g) "Property and casualty insurer" means any insurance company licensed under articles 9, 10, 11, 12, 12a, 15 or 16 of chapter 40 of the Kansas Statutes Annotated, and amendments thereto, but shall not include monoline mortgage guaranty insurers, financial guaranty insurers and title insurers.

(h) "Negative trend" means, with respect to a life and health insurer, a negative trend over a period of time, as determined in accordance with the "trend test calculation" included in the RBC instructions defined in subsection (j).

(i) "RBC" means risk-based capital.

(j) "RBC instructions" means the risk-based capital instructions promulgated by the NAIC, which are in effect on December 31,~~ 2017~~ *2018*, or any later version promulgated by the NAIC as may be adopted by the commissioner under K.S.A. 2018 Supp. 40-2c29, and amendments thereto.

(k) "RBC level" means an insurer's company action level RBC, regulatory action level RBC, authorized control level RBC, or mandatory control level RBC where:

(1) "Company action level RBC" means, with respect to any insurer, the product of 2.0 and its authorized control level RBC;

(2) "regulatory action level RBC" means the product of 1.5 and its authorized control level RBC;

(3) "authorized control level RBC" means the number determined

under the risk-based capital formula in accordance with the RBC instructions; and

(4) "mandatory control level RBC" means the product of 0.70 and the authorized control level RBC.

(l) "RBC plan" means a comprehensive financial plan containing the elements specified in K.S.A. 40-2c06, and amendments thereto. If the commissioner rejects the RBC plan, and it is revised by the insurer, with or without the commissioner's recommendation, the plan shall be called the "revised RBC plan."

(m) "RBC report" means the report required by K.S.A. 40-2c02, and amendments thereto.

(n) "Total adjusted capital" means the sum of:

(1) An insurer's capital and surplus or surplus only if a mutual insurer; and

(2) such other items, if any, as the RBC instructions may provide.

(o) "Commissioner" means the commissioner of insurance.

Sec. 3. K.S.A. 2018 Supp. 40-3305 is hereby amended to read as follows: 40-3305. (a) Every insurer ~~which~~ *that* is authorized to do business in this state and ~~which~~ *that* is a member of an insurance holding company system shall register with the commissioner of insurance, except a foreign insurer subject to registration requirements and standards adopted by statute or regulation in the jurisdiction of its domicile ~~which~~ *that* are substantially similar to those contained in this section. Any insurer ~~which~~ *that* is subject to registration under this section shall register within 15 days after it becomes subject to registration, and annually thereafter by May 1 of each year unless the commissioner of insurance for good cause shown extends the time for registration, and then within such extended time. The commissioner of insurance may require any authorized insurer ~~which~~ *that* is a member of an insurance holding company system and ~~which~~ *that* is not subject to registration under this section to furnish a copy of the registration statement, the summary specified in subsection (c) or other information filed by such insurance company with the insurance regulatory authority of domiciliary jurisdiction.

(b) Pursuant to subsection (a), every insurer subject to registration shall file a registration statement on a form provided by the commissioner of insurance, ~~which~~ *that* shall contain current information about:

(1) The capital structure, general financial condition, ownership and management of the insurer and any person controlling the insurer;

(2) the identity and relationship of every member of the insurance holding company system;

(3) the following agreements in force and transactions currently outstanding or ~~which~~ *that* occurred during the last calendar year between such insurer and its affiliates:

(A) Loans, other investments, or purchases, sales or exchanges of securities of the affiliates by the insurer or of the insurer by its affiliates;

(B) purchases, sales~~,~~ or exchanges of assets;

(C) transactions not in the ordinary course of business;

(D) guarantees or undertakings for the benefit of an affiliate ~~which~~ *that* result in an actual contingent exposure of the insurer's assets to liability, other than insurance contracts entered into in the ordinary course of the insurer's business;

(E) all management agreements, service contracts and cost sharing arrangements;

(F) reinsurance agreements;

(G) dividends and other distributions to shareholders; and

(H) consolidated tax allocation agreements;

(4) other matters concerning transactions between registered insurers and any affiliates as may be included from time to time in any registration forms adopted or approved by the commissioner of insurance;

(5) any pledge of the insurer's stock, including stock of any

subsidiary or controlling affiliate, for a loan made to any member of the insurance holding company system;

(6) ~~if requested by the commissioner of insurance, the insurer shall include~~ financial statements of or within an insurance holding company system, including all affiliates*, if requested by the commissioner of insurance*. Financial statements may include, but are not limited to, annual audited financial statements filed with the U.S. securities and exchange commission (SEC) pursuant to the securities act of 1933, as amended, or the securities exchange act of 1934, as amended. An insurer required to file financial statements pursuant to this paragraph may satisfy the request by providing the commissioner of insurance with the most recently filed parent corporation financial statements that have been filed with the SEC;

(7) statements that the insurer's board of directors and principal officers oversee corporate governance and internal controls and that the insurer's principal officers have approved, implemented and continue to maintain and monitor corporate governance and internal control procedures; and

(8) any other information required by the commissioner of insurance by rules and regulations.

(c) All registration statements shall be accompanied by a summary outlining all items in the current registration statement representing changes from the prior registration statement.

(d) No information need be disclosed on the registration statement filed pursuant to subsection (b) if such information is not material for the purpose of this section. Unless the commissioner of insurance by rules and regulations or order provides otherwise, sales, purchases, exchanges, loans or extensions of credit, investments or guarantees, involving *0.*5% or less of an insurer's admitted assets as of the December 31 immediately preceding shall be deemed immaterial for purposes of this section.

(e) Each registered insurer shall keep current the information required to be disclosed in such insurer's registration statement by reporting all material changes or additions on amendment forms provided by the commissioner of insurance within 15 days after the end of the month in which it learns of each such change or addition, except each registered insurer shall report all dividends and other distributions to shareholders within five business days following its declaration. Any such dividend or distribution shall not be paid for at least 10 business days from the commissioner's receipt of the notice of its declaration.

(f) Any person within an insurance holding company system subject to registration shall provide complete and accurate information to an insurer, where such information is reasonably necessary to enable the insurer to comply with the provisions of this act.

(g) The commissioner of insurance shall terminate the registration of any insurer ~~which~~ *that* demonstrates that such insurer no longer is a member of an insurance holding company system.

(h) The commissioner of insurance may require or allow two or more affiliated insurers subject to registration hereunder to file a consolidated registration statement.

(i) The commissioner of insurance may allow an insurer ~~which~~ *that* is authorized to do business in this state and ~~which~~ *that* is part of an insurance holding company system to register on behalf of any affiliated insurer ~~which~~ *that* is required to register under subsection (a) and to file all information and material required to be filed under this section.

(j) The provisions of this section shall not apply to any information or transaction if and to the extent the commissioner of insurance by rule and regulation or order ~~shall exempt~~ *exempts* the same from the provisions of this section.

(k) Any person may file with the commissioner of insurance a disclaimer of affiliation with any authorized insurer or such a disclaimer may be filed by such insurer or any member of an insurance holding company system. The disclaimer shall fully disclose all

material relationships and bases for affiliation between such person and such insurer as well as the basis for disclaiming such affiliation. After a disclaimer has been filed, the insurer shall be relieved of any duty to register or report under this section which may arise out of the insurer's relationship with such person unless and until the commissioner of insurance disallows such a disclaimer. The commissioner of insurance shall disallow such a disclaimer only after furnishing all parties in interest with notice and opportunity to be heard in accordance with the provisions of the Kansas administrative procedure act.

(l) (1) Except as provided in paragraph (2), the ultimate controlling person of every insurer subject to registration also shall file an annual enterprise risk report. The report, to the best of the ultimate controlling person's knowledge and belief, shall identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer. *The report shall be appropriate to the nature, scale and complexity of the insurer.* The report shall be filed with the lead state commissioner of insurance of the insurance holding company system as determined by the procedures within the financial analysis handbook adopted by the national association of insurance commissioners. The first enterprise risk report shall be filed no later than May 1, 2015, and annually thereafter by May 1 of each year unless the commissioner of insurance extends the time for filing for good cause shown.

(2) The ultimate controlling person of ~~an~~ *a domestic* insurer *that is authorized, admitted or eligible to engage in the business of insurance only in this state* with total direct and assumed annual premiums of less than $300 million is not required to submit an enterprise risk report *under paragraph (1) unless the ultimate controlling person of the domestic insurer also controls other insurers that do not meet the requirements of this subsection. For the purposes of this subsection, an insurer is not considered to be authorized, admitted or eligible to engage in the business of insurance only in this state if the insurer directly or indirectly writes or assumes insurance in any other manner in another state*.

(m) The failure of an insurer or an ultimate controlling person of the insurer to file a registration statement, any summary of the registration statement or enterprise risk filing within the specified time for filing shall be a violation by the insurer or by the ultimate controlling person of the insurer, as applicable.

Sec. 4. K.S.A. 2018 Supp. 40-2,118 is hereby amended to read as follows: 40-2,118. (a) For purposes of this act a "fraudulent insurance act" means an act committed by any person who, knowingly and with intent to defraud, presents, causes to be presented or prepares with knowledge or belief that it will be presented to or by an insurer, purported insurer, broker or any agent thereof, any written, electronic, electronic impulse, facsimile, magnetic, oral, or telephonic communication or statement as part of, or in support of, an application for the issuance of, or the rating of an insurance policy for personal or commercial insurance, or a claim for payment or other benefit pursuant to an insurance policy for commercial or personal insurance which such person knows to contain materially false information concerning any fact material thereto; or conceals, for the purpose of misleading, information concerning any fact material thereto.

(b) An insurer that has knowledge or a good faith belief that a fraudulent insurance act is being or has been committed shall provide to the commissioner, on a form prescribed by the commissioner, any and all information and such additional information relating to such fraudulent insurance act as the commissioner may require.

(c) Any other person ~~that~~ *who* has knowledge or a good faith belief that a fraudulent insurance act is being or has been committed may provide to the commissioner, on a form prescribed by the commissioner, any and all information and such additional information relating to such fraudulent insurance act as the commissioner may request.

(d) (1) Each insurer shall have antifraud initiatives reasonably calculated to detect fraudulent insurance acts. Antifraud initiatives may include fraud investigators, who may be insurer employees or independent contractors and an antifraud plan submitted to the commissioner no later than July 1, 2007. Each insurer that submits an antifraud plan shall notify the commissioner of any material change in the information contained in the antifraud plan within 30 days after such change occurs. Such insurer shall submit to the commissioner in writing the amended antifraud plan.

The requirement for submitting any antifraud plan, or any amendment thereof, to the commissioner shall expire on the date specified in subsection (d)(2) unless the legislature reviews and reenacts the provisions of subsection (d)(2) prior to such date.

(2) Any antifraud plan, or any amendment thereof, submitted to the commissioner for informational purposes only shall be confidential and not be a public record and shall not be subject to discovery or subpoena in a civil action unless following an in camera review, the court determines that the antifraud plan is relevant and otherwise admissible under the rules of evidence set forth in article 4 of chapter 60 of the Kansas Statutes Annotated, and amendments thereto. The provisions of this paragraph shall expire on July 1, 2021, unless the legislature reviews and reenacts this provision prior to July 1, 2021.

(e) Except as otherwise specifically provided in K.S.A. 2018 Supp. 21-5812(a), and amendments thereto, and K.S.A. 44-5,125, and amendments thereto, a fraudulent insurance act shall constitute a severity level 6, nonperson felony if the amount involved is $25,000 or more; a severity level 7, nonperson felony if the amount *involved* is at least $5,000 but less than $25,000; a severity level 8, nonperson felony if the amount *involved* is at least $1,000 but less than $5,000; and a class C nonperson misdemeanor if the amount *involved* is less than $1,000. Any combination of fraudulent acts as defined in subsection (a) which occur in a period of six consecutive months which involves $25,000 or more shall have a presumptive sentence of imprisonment regardless of its location on the sentencing grid block.

(f) In addition to any other penalty, a person who violates this statute shall be ordered to make restitution to the insurer or any other person or entity for any financial loss sustained as a result of such violation. An insurer shall not be required to provide coverage or pay any claim involving a fraudulent insurance act.

(g) *For the purposes of this section:*

(1) "Amount involved" means the greater of: (A) The actual pecuniary harm resulting from the fraudulent insurance act; (B) the pecuniary harm that was intended to result from the fraudulent insurance act; or (C) the intended pecuniary harm that would have been impossible or unlikely to occur, such as in a government sting operation or a fraud in which the claim for payment or other benefit pursuant to an insurance policy exceeded the allowed value. The aggregate dollar amount of the fraudulent claims submitted to the insurance company shall constitute prima facie evidence of the amount of intended loss and is sufficient to establish the aggregate amount involved in the fraudulent insurance act, if not rebutted; and

(2) "pecuniary harm" means harm that is monetary or that otherwise is readily measurable in money, and does not include emotional distress, harm to reputation or other non-economic harm.

(h) This act shall apply to all insurance applications, ratings, claims and other benefits made pursuant to any insurance policy.

Sec. 5. K.S.A. 2018 Supp. 40-2,118, 40-2,118a, 40-2c01 and 40-3305 are hereby repealed.

Sec. 6. This act shall take effect and be in force from and after its publication in the statute book.

I hereby certify that the above BILL originated in the HOUSE, and was adopted by that body

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HOUSE adopted
Conference Committee Report_____

_____
Speaker of the House.

_____
Chief Clerk of the House.

Passed the SENATE
as amended _____

SENATE adopted
Conference Committee Report_____

_____
President of the Senate.

_____
Secretary of the Senate.

APPROVED _____

_____
Governor.