

MINUTES OF THE Senate Committee on Financial Institutions and Insurance.

The meeting was called to order by Chairperson Dick Bond at 9:00 a.m. on March 6, 1995 in Room 529-S of the Capitol.

Members present were: Senator Clark, Senator Corbin, Senator Emert, Senator Lee, Senator Petty, Senator Praeger, Senator Steffes

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

Conferees appearing before the committee: Anita Larson, Security Benefit Group of Companies
Tom Wilder, State Insurance Department
William Sneed, American Investors Life Insurance Company

Others attending: See attached list

Senator Emert made a motion to approve the minutes of the meeting of February 23 as submitted. Senator Steffes seconded the motion; the motion carried.

The chairman opened the hearing on **HB 2201**. Anita Larson, Security Benefit Group, testified as a proponent of this bill, stating that it would remove two restrictions to life insurance companies purchasing common stock in domestic and Canadian corporations. (Attachment #1-1,2) Ms. Larson stated that a committee of the National Association of Insurance Commissioners has drafted a Model Investment Law which does not include the two restrictions that this bill would delete from Kansas statute.

Tom Wilder, State Insurance Department, also appeared as a proponent of **HB 2201**, testifying that the language in the bill was drafted according to the law governing property and casualty insurers. The restrictions on page 2, lines 21-26, was requested by the Insurance Department, which supports this legislation. (Attachment #2-1,2) In response to Senator Steffes' question, Mr. Wilder explained the restrictions and how they would apply.

William Sneed, American Investors Life Insurance Company, also appeared as a proponent of this legislation and stated that it is in the best interest of the entire domestic insurance industry. (Attachment #3)

There being no further questions and no other conferees, the hearing was closed. Senator Steffes made a motion, seconded by Senator Praeger, to pass **HB 2201** favorably. The motion carried. Senator Steffes will carry this bill on the Senate floor.

The hearing was opened on **HB 2211**, concerning insurance companies investing in asset backed securities. Anita Larson, SBG, explained that asset backed securities are bonds or notes backed by loan paper or accounts receivables and that this bill would allow life insurance companies to invest in other types of asset backed securities, such as credit card receivables and automobile loans, subject to qualitative and quantitative restrictions. (Attachment #1-2,3)

Tom Wilder, State Insurance Department, testified that the Insurance Department supports this bill and that new section 2 was added at their request. (Attachment #2-2,3)

William Sneed, Amvestors Corporation, testified that his client also supports this legislation. (Attachment #4)

The hearing was closed. Senator Steffes moved to pass the bill favorably. The motion was seconded by Senator Emert; the motion carried.

The chairman opened the hearing on **HB 2212**, which would allow life insurance companies to clear through and register their investments with an international clearing corporation as long as the clearing house is subject to certain regulations. Anita Larson, SBG, also appeared as a proponent of this legislation. (Attachment #1-3,4,5) In reference to the language in section (c)(4), Senator Bond questioned how the State Insurance Commissioner or State Bank Commissioner would acquire the expertise to approve an international clearing house. Ms. Larson clarified for Senator Emert the need to use an international clearing house.

CONTINUATION SHEET

MINUTES OF THE Senate Committee on Financial Institutions & Insurance, Room 529-S Statehouse, on March 6, 1995.

Tom Wilder, State Insurance Department, also appeared as a proponent of this bill and testified that the Insurance Department requested the bill to be amended to provide that insurance companies could only use a foreign clearing house if it is owned or operated by an entity which is regulated by the SEC or is subject to federal and state banking laws. (Attachment #2-3) Mr. Wilder also agreed with Senator Bond about the need to delete the language authorizing the State Insurance Commissioner to approve clearing houses.

William Sneed, Amvestors Corporation, stated that the expansion allowed by this bill is in the best interest of the domestic insurance industry, and urged its passage. (Attachment #5)

Bud Cornish, Kansas Association of Insurance Companies, stated that his organization supports each of the three bills heard today.

There were no other conferees and the hearing on HB 2212 was closed. Senator Steffes made a motion to conceptually amend the bill to delete the language authorizing the State Insurance Commissioner to approve international clearing houses, and to pass the bill as amended. Senator Corbin seconded the motion. The motion carried. Senator Corbin will carry this bill on the Senate floor.

The chairman advised that HB 2343, also scheduled for hearing at today's meeting, would be heard on Wednesday, March 8. Chairman Bond also expressed his concerns with the language in the bill and requested Mr. Wilder to draft some clarifying language and present it to the committee on Wednesday.

The committee adjourned at 10:01 a.m. The next meeting is scheduled for March 7, 1995.



**The Security Benefit
Group of Companies**

Security Benefit Life Insurance Company
Security Benefit Group, Inc.
Security Distributors, Inc.
Security Management Company

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Topeka, Kansas 66636-0001
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March 6, 1995

Subj: House Bill No. 2201 -- Purchases of Common Stock
House Bill No. 2211 -- Investments in Asset-backed Securities
House Bill No. 2212 -- International Clearing Corporations

Dear Chairman and Committee Members:

The Security Benefit Group of Companies is a diversified financial services organization offering life insurance, mutual funds, annuities and retirement plans. The parent company, Security Benefit Life Insurance Company, has been in business for over 100 years. The Security Benefit Group of Companies has over \$4 billion in assets under management and employs approximately 550 Kansans. We support House Bills 2201, 2211 and 2212 as amended by House Committee.

House Bill 2201 -- Purchases of Common stock

K.S.A. 40-2b07 presently provides that a life insurance company may invest its funds in the common stock of domestic or Canadian corporations subject to a number of restrictions, including the following:

- All common stock held by the insurer cannot exceed 15% of admitted assets.
- Bonds, if any, issued by the corporation must be investment grade.
- The stock must be registered with a national securities exchange or regularly traded on a national or regional basis.
- The insurer cannot invest in more than 5% of the total number of outstanding shares of the corporation.
- The insurer cannot purchase more than 2% of its admitted assets in any one corporation.
- The corporation must have paid cash dividends during each of the last three years.
- The corporation must have earnings in three of the last five years.

House Bill 2201 would delete the last two restrictions if the issuing company has, at a minimum, net assets of \$10 million, a net worth of \$1 million, and an aggregate market value of \$500 million.

Many corporations do not pay dividends. Instead of paying dividends, such corporations reinvest the money in the company's operations. Often, this is the financially responsible decision for the company and its stockholders. A company's payment of dividends is not an indicator of a company's solvency. For example, Federal Express, Compac Computer, Fruit of the Loom, FMC and Microsoft have not paid dividends in each of the last three years. Microsoft has not issued any debt

*Senate 7141
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Attachment #1*

securities. However, if the companies on this list have issued debt securities, the securities have been rated investment grade.

Companies that have established histories of strong performance may have temporary periods of negative earnings. Negative earnings are not necessarily indicative of a poor investment risk. A company could experience reduced or negative earnings due to a restructure or change in operations which could enhance the company's long term profitability. Cyclical industries, those directly affected by economic changes, may experience times of negative earnings during economic downturns. General Motors is a classic example. The restriction regarding earnings precludes insurers from investing in the following companies: IBM, Georgia-Pacific Corporation, General Motors and Coca-Cola Enterprises. Debt securities issued by these companies are currently rated investment grade.

In regard to insurers' investments in common stock, Kansas law is more restrictive than the laws of most other states. Twenty- six states have neither a dividend nor earnings requirement. This list includes the neighboring states Missouri, Oklahoma, Iowa, Texas and Illinois. Nineteen states have a dividend **or** earnings requirement, but do not have both. Colorado falls within this category. Only five other states have dividends **and** earnings requirements regarding the purchase of common stock: Alaska, Georgia, Indiana, New Jersey and Vermont.

A committee of the National Association of Insurance Commissioners has drafted a Model Investment Law. This model has not been adopted and is not in final form; however, the most recent draft does not contain the two restrictions HB 2201 would delete. The draft contains a per issuer limitation of 3% and an aggregate limitation of 10%. We hope that you will vote in favor of House Bill 2201 as amended by House Committee.

House Bill 2211 -- Asset-backed Securities

Asset-backed securities are bonds or notes backed by loan paper or accounts receivables. Currently, life insurers are authorized to invest in certain types of asset-backed securities, namely mortgage-backed securities. House Bill 2211 would allow life insurers to invest in other types of asset-backed securities such as those backed by credit card receivables and automobile loans.

Under the provisions of House Bill 2211, insurers' investments in asset-backed securities would be subject to certain qualitative and quantitative limitations. In order to qualify as an admitted asset under the section, at the time of acquisition the security must be designated "1 or "2" by the National Association of Insurance Commissioners. In addition, an insurer could not invest more than 2% of its admitted assets in any one

issue of asset-backed securities, and in the aggregate, could not invest more than 20% of its admitted assets in asset-backed securities.

Illinois, Minnesota, Nebraska and Michigan specifically authorize life insurers to invest in asset-backed securities. Although the remaining states do not expressly authorize investments in asset-backed securities, such investments are not necessarily prohibited. For example, New York allows investments in "American Institutions." New York law does not specifically authorize investments in asset-backed securities. However, an opinion issued by the General Counsel of the New York Insurance Department states that, under the general provision allowing investments in American Institutions, asset-backed securities issued by American Institutions are permissible investments.

Finally, the current draft of the Model Investment Law specifically authorizes investments in asset-backed securities. The Model contains a per issue limitation of 3% of an insurer's admitted assets, but does not impose an aggregate limitation for asset-backed securities rated investment grade by the NAIC.

Even though the investments authorized by House Bill 2211 are investment grade obligations, as with any investment, each issue must be closely analyzed by an investment professional. However, by adding asset-backed securities to the list of investments expressly authorized by Kansas law, insurers can further diversify their holdings without sacrificing the quality of their portfolios. We hope that you will vote in favor of House Bill 2211 as amended by House Committee.

House Bill 2212 -- International Clearing Corporations

House Bill 2212 would amend K.S.A. 40-2b20 to allow insurance companies to clear through and register securities with an international clearing corporation so long as the clearing corporation is subject to certain regulations or is deemed satisfactory by the commissioner of insurance. Specifically, the international clearing corporation must be operated or owned by a bank or other entity that is subject to regulation by the United States Federal Reserve Board or the United States Comptroller of the Currency, or must be registered with the Securities and Exchange Commission.

Under current law, insurers in Kansas can use certain domestic clearing corporations. International clearing corporations are not authorized. We are not aware of a determination being made that international clearing corporations are unsafe or risky. We believe that international clearing corporations simply were not contemplated. Due to the globalization of financial markets and the increase in cross-border investment activity, authorization to use international clearing corporations is crucial.

Traditionally, when an investor purchased a security, the investor received a physical certificate evidencing ownership. Now, securities are seldom held in physical form.

Trades are effected through book entry. A security is registered in an owner's name in the records of a clearing corporation. If it is sold, upon receipt of the purchase price, the clearing corporation re-registers the security in the purchaser's name.

International clearing corporations operate in the same manner as domestic clearing corporations. The difference is that international clearing corporations are used to clear and register internationally traded securities issued by foreign and United States entities.

The world's largest international clearing system is Euroclear. Euroclear is used by approximately 3,000 banks, brokers and other securities institutions that are active in the international market. Euroclear is used for settlement of over 54,000 debt and equity securities, including securities of foreign and United States entities.

Euroclear is a safe and reliable system. Book entry settlement is much safer than physical form because it eliminates the risk of physical loss or damage. However, since trades are effected by computer entry, computer system security safeguards and disaster relief programs have been implemented. Likewise, procedures for validation of trade instructions have been developed.

The Euroclear system is operated by Morgan Guaranty Trust Company of New York, Brussels Office. Morgan Guaranty Trust is fully regulated by the U.S. Federal Reserve Board and State of New York Banking Department. Finally, if Euroclear were declared insolvent, securities registered with Euroclear would not become a part of the Morgan Guaranty Trust's estate.

Euroclear has been in operation for over 25 years. Daily securities and cash transactions average \$66 billion. In 1993, \$17 trillion dollars of securities cleared through Euroclear. On average, Euroclear processes 40,000 transactions every day. At year end 1993, securities valuing approximately \$1.5 trillion were held by Euroclear.

The number of entities that issue securities through international clearing corporations continues to increase. Issuers of securities choose the international market to maximize the number of potential investors. In addition, a United States corporation may choose to issue debt securities in the global market because foreign investors may be willing to receive a lower rate of interest in exchange for payments made in United States dollars.

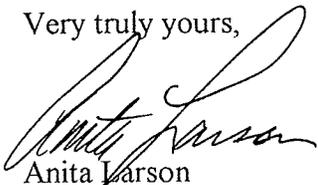
This bill only relates to the registration and clearing of securities only. It does not expand the type of securities in which life insurers are authorized to invest. The existing limitations on investments in foreign securities remain unchanged. A life insurer can invest no more than 5% of its admitted assets in obligations of foreign

governments, other than obligations of Canada. Investments in obligations of foreign companies are not specifically authorized. However, such investments may be made under the "leeway clause," and consequently cannot in the aggregate exceed 10% of an insurer's admitted assets.

Other states have reacted to the continued trend towards globalization of financial markets. Our research indicates that fourteen states have taken specific steps to authorize the use of international clearing corporations. We hope that Kansas will join these states by adopting House Bill 2212 as amended by House Committee.

Thank you for your time and consideration. I would be happy to address any questions you have.

Very truly yours,



Anita Larson
Assistant Counsel
Security Benefit Group, Inc.



Kathleen Sebelius
Commissioner of Insurance
Kansas Insurance Department

MEMORANDUM

To: Senate Financial Institutions and Insurance Committee

From: Tom Wilder, Director of Governmental Relations
Kansas Department of Insurance

Re: H.B. 2201; H.B. 2211 and H.B. 2212

Date: March 6, 1995

These three house bills are legislative proposals introduced at the request of Security Benefit Group to allow life insurance companies greater flexibility in their ability to invest assets of the company. The Kansas Department of Insurance supports the concept of giving insurance companies more investment choices and would ask for your support of H.B. 2201, H.B. 2211 and H.B. 2212. The House Financial Institutions and Insurance Committee adopted amendments to the three bills at the request of the Department of Insurance. This memorandum addresses each of the specific investment bills which are being considered by the Senate Committee on Financial Institutions and Insurance.

(1.) **H.B. 2201:**

The legislative proposal amends the investment statutes to allow insurance companies to invest in the common stock of corporations which have not paid cash dividends or shown earnings for three out of the last five years prior to the date of the investment. The current statutes allow insurance companies to invest in common stock of a corporation (a) if the shares are "qualified investments" as defined by the insurance code; (b) if the stock is registered with a national securities exchange; (c) if cash dividends have been paid during each of the last three years and (d) if the company has shown earnings in three of the last five years. The bill removes restrictions (c) and (d) from the present law.

*Senate 7/41
3/6/95
Attachment #2*

It is true Kansas insurance companies can not presently invest in corporate securities of a number of companies, such as General Motors, because the corporations have not shown book profits or paid dividends, even though the securities of these corporations are generally considered "investment grade." However, there should be some limits on the new investment powers set out in the proposal. The Department of Insurance requested an amendment to H.B. 2201 which was adopted by the House. This amendment permits insurance companies to invest in shares of stock of a company which has not paid dividends or shown earnings for three out of five years prior to the date of acquisition if as of the date of acquisition:

- (a.) The issuing corporation has net assets of \$10,000,000 (ten million dollars) or more:
and
- (b.) The issuing corporation has a net worth of \$1,000,000 (one million dollars) or more;
and
- (c.) the issuing corporation has an aggregate market value of \$500,000,000 (five hundred million dollars) or more.

The original House Bill only applied to life insurance companies. The House Financial Institutions and Insurance Committee also adopted an amendment which extends the investment authority to all other types of insurance companies.

(2.) H.B. 2211:

The bill would add a new statute to allow insurance companies to invest in asset-backed securities. Currently, insurers may invest in securities which are based on the value of "pools" of real estate mortgages. The proposal would permit companies to invest in securities backed by other assets such as automobile loans or credit card obligations. The Department of Insurance believes these types of investments should be permitted. The House Financial Institutions and Insurance Committee adopted amendments at the request of the Department of Insurance which places the following additional restrictions on investments in asset backed securities:

- (a.) The aggregate investment in asset backed securities should not exceed 20% (20 percent) of the admitted assets of the company.

(b.) The securities should be those rated by the National Association of Insurance Commissioners as Category "1" or "2" investments (the highest ratings available).

(c.) All insurance companies should be permitted to make these investments pursuant to K.S.A. 40-2a01 et seq.

(3.) H.B. 2212:

The proposal allows life insurance companies to hold securities in "clearing corporations" which are situated outside of the United States. A clearing corporation is an organization which holds and trades securities for other companies. Insurance companies are permitted under existing law to hold securities in United States clearing corporations which are subject to the regulation of the Federal Reserve System or subject to supervision or regulation by the banking laws of this state.

The Department of Insurance is concerned about the impact of H.B. 2212 because the Department does not have the resources to monitor the legitimacy or activities of foreign clearing corporations operations. The clearing companies in this country are subject to some oversight of the United States government but the Department is not aware of any similar government agency which could indicate whether a clearing corporation is solvent. The Department of Insurance requested the House Financial Institutions and Insurance Committee amend this bill to provide the insurance companies could invest in foreign clearing corporations if they are owned or operated by an entity which is regulated by the Securities and Exchange Commission or are subject to federal or state banking laws.

The Department of Insurance requests the Senate Committee approve H.B. 2201, H.B. 2211 and H.B. 2212 as amended.

MEMORANDUM

TO: The Honorable Dick Bond, Chairman
Senate Financial Institutions and Insurance Committee

FROM: William W. Sneed, Legislative Counsel
American Investors Life Insurance Company

DATE: March 6, 1995

RE: H.B. 2201

Mr. Chairman, Members of the Committee: My name is Bill Sneed and I represent American Investors Life Insurance Company. American Investors is a wholly-owned subsidiary of AmVestors Financial Corporation. American Investors is an insurance company predominantly active in the annuity business and is a domestic insurer within the State of Kansas.

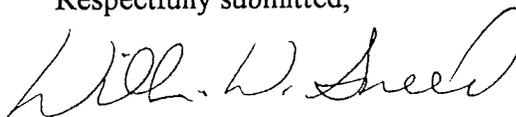
H.B. 2201 is an amendment to K.S.A. 40-2b07. K.S.A. 40-2b07 is one of a series of statutes relating to the investments that are allowable by a domestic life insurance company. The proposed amendment would remove the current restrictions which prevent a life insurance company from investing in common stocks of a corporation which has not paid cash dividends in each of the last three years and has generated profits in at least three of the last five years. This restriction had its genesis when it was believed that as a general rule the common stock of a corporation could only be considered a "good" investment if such corporation had been paying dividends and generating "profits." However, the corporate world has changed substantially, and in particular, as it relates to the payment of dividends. This is uniquely true for those companies that have made a corporate determination that it is better to reinvest funds (either from profits or dividends) back into the company as it continues to grow. It is my client's position that such company should not be summarily discounted from review for investment purposes and should be reviewed on its total corporate financial status as opposed to one or two

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Attachment #3*

components of its financial status. Further, the overall limitation of 15% of the insurance company's total admitted assets is still in place, and as such, there are ample safeguards with respect to the investment of a life insurance company into these types of corporations.

Therefore, in an effort to continue to keep our domestic insurance industry available to all investment strategies, this amendment would be in the best interest of the entire domestic industry. Thus, on behalf of my client, I support H.B. 2201 and respectfully request your favorable consideration.

Respectfully submitted,



William W. Sneed

MEMORANDUM

TO: The Honorable Dick Bond, Chairman
Senate Financial Institutions and Insurance Committee

FROM: William W. Sneed, Legislative Counsel
American Investors Life Insurance Company

DATE: March 6, 1995

RE: H.B. 2211

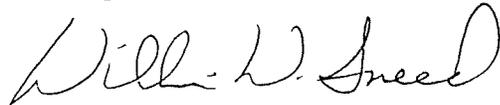
Mr. Chairman, Members of the Committee: My name is Bill Sneed and I represent American Investors Life Insurance Company. American Investors is a wholly-owned subsidiary of AmVestors Financial Corporation. American Investors is an insurance company predominantly active in the annuity business and is a domestic insurer within the State of Kansas.

H.B. 2211 would create a new section in the investment code for domestic life insurance companies. Specifically, the new statute would allow life insurance companies to invest in "asset backed" securities subject to certain limitations. Currently Kansas law allows for the investment by domestic life insurance companies in "mortgage backed" securities, which are secured instruments collateralized by mortgages. In today's marketplace, mortgage backed securities are only a part of the asset backed securities in that many securities are collateralized by various other well-sounded assets. Thus, this proposal would allow domestic life insurance companies to continue to be involved in the foreground of the current marketplace. Further, such investments are limited so that they cannot exceed 2% of the total admitted assets of the domestic life insurance companies. With this safeguard, such investments could be made but only on a small basis as compared to the total investment portfolio of the domestic life insurance companies. With these safeguards, it is my client's position that such a statute

is well reasoned and would continued to allow our domestic life insurance industry to grow in today's marketplace.

Thus, on behalf of my client, I support H.B. 2211 and respectfully request your favorable consideration.

Respectfully submitted,



William W. Sneed

MEMORANDUM

TO: The Honorable Dick Bond, Chairman
Senate Financial Institutions and Insurance Committee

FROM: William W. Sneed, Legislative Counsel
American Investors Life Insurance Company

DATE: March 6, 1995

RE: H.B. 2212

Mr. Chairman, Members of the Committee: My name is Bill Sneed and I represent American Investors Life Insurance Company. American Investors is a wholly-owned subsidiary of AmVestors Financial Corporation. American Investors is an insurance company predominantly active in the annuity business and is a domestic insurer within the State of Kansas.

H.B. 2212 is an amendment to K.S.A. 40-2b20. K.S.A. 40-2b20 is one of a series of statutes which regulates the investments of a domestic life insurance company. Specifically, this statute details mechanically how a domestic life insurance company can hold securities when the company transacts the buying and selling of these securities in the marketplace. This amendment would allow a domestic life insurance company to invest securities cleared and settled through a clearing corporation handling international securities. Currently the investment statutes allow such securities to be cleared and settled only through United States clearing corporations. In today's market setting, this in essence prevents domestic life insurance companies from investing in securities cleared and settled outside of the United States. The actual investing in these securities is allowed through other statutes. It is simply the mechanism by which these securities are bought and sold which is causing the difficulty. Thus, the only expansion found in this particular amendment is with what entity the domestic life insurance company may do business of buying and/or selling these types of securities.

*Senate 714
3/6/95
Attachment #5*

In today's world market the inability of a domestic company to utilize these sources places the domestic life insurance company at a disadvantage with its competitors who may not be domesticated in Kansas. Thus, this would allow the Kansas domestic company to be on the same footing as its major competitors. This, coupled with all the other safeguards in the investment statutes, demonstrates that such expansion is in the best interest of the domestic industry, and ultimately, its policyholders.

Thus, on behalf of my client, I support H.B. 2212 and respectfully request your favorable consideration.

Respectfully submitted,



William W. Sneed