



Kansas Insurance Department

Sandy Praeger, Commissioner of Insurance

TESTIMONY ON SB 273

HOUSE INSURANCE COMMITTEE March 7, 2012

Chairman and Members of the Committee:

I am Kris Kellim with the Kansas Insurance Department, and with me today is Ken Abitz, who is the Director of our Financial Surveillance Division. Thank you for the opportunity to testify in support of SB 273.

SB 273 concerns examination fees and expenses that companies must pay for work done by *outside consultants* for the Department. Currently, the amount a company must pay for outside consulting fees and the pro rata amount used to purchase exam equipment and software for any examination of the company, including its subsidiaries, cannot collectively total more than \$25,000. This cap on financial examinations, which was put in place over twenty years ago, is simply outdated and inadequate.

The Legislature has established a statutory mechanism that requires the Department to conduct a financial examination on each domestic company doing business in the state at least once every five years. The purpose of the financial exam is to ensure the company will be able to meet its contractual obligations to consumers. As such, this ultimately is a consumer protection bill.

Bill Language and Background:

The current language of SB 273 has undergone multiple amendments and is the product of extensive discussions between the Department and Industry representatives.

SB 273, as amended, would replace the current one-size-fits-all cap of \$25,000 with a three-prong cap structure. The first and second prongs would apply to financial exams, which I will address in more detail. The third would apply to market regulation exams, and would leave the cap at its current level of \$25,000. This separate cap for market regulation exams was omitted from the original bill language, and was amended into the bill at the suggestion of Industry representatives.

The first and second prongs mentioned above essentially are separate tiered cap levels based on the size of companies' gross premiums. This approach is an effort to balance the need for a major increase in the current cap across the board against the relatively limited financial capacities of smaller, domestic companies. The first tier would apply to companies with less than \$200 million in gross premiums, direct and assumed, and would cap the outside fees and

expenses for a financial exam at \$50,000 per company. The original bill language separated companies based on \$50 million in gross premiums, and placed the cap on smaller companies at \$100,000. Both the increase in the threshold from \$50 to \$200 million in gross premiums, and the decreased cap on smaller companies from \$100,000 to \$50,000 resulted from discussions with Industry representatives.

The second cap level would apply to companies with gross premiums of \$200 million or greater. The bill currently sets this cap at \$200,000. As introduced, the bill did not include a cap on exam fees for companies in the second tier. Security Benefit Life Ins. Co. subsequently offered an amendment to set the cap at \$1 million. However, other Industry representatives did not agree with this figure, and extensive discussions about this cap were held. Although the parties did not reach an agreement on the exact figure on the second tier cap, the Senate Insurance committee amended the bill to include a \$200,000 second tier cap, which was a middle ground in the discussions at the time. The Department again has made concessions and is agreeable to the \$200,000 second tier cap. The Department is aware of three companies that agree to a \$200,000 cap: Blue Cross & Blue Shield of Kansas, Security Benefit Life Ins. Co., and Employers Reassurance Corp.

Financial Surveillance and Consumer Protection:

Without adequate funding for financial examinations, the Department cannot sufficiently monitor the financial stability of Kansas insurance companies, and cannot ensure they are able to pay their obligations to policyholders. The current \$25,000 cap for financial examinations is inadequate with respect to all domestic companies, regardless of size.

A proper examination of a company's financial condition involves a full-scope audit of the company's reserves. Under the current \$25,000 cap, the Department has only been able to hire outside actuaries to perform "peer reviews" of companies' reserve methods, which essentially is an audit of the companies' internal procedures. This level of financial surveillance is insufficient and does not fulfill the Department's duties to consumers.

Another major concern of the Department is that this inability to effectively evaluate claims and life reserves could jeopardize the Department's national accreditation. Loss of accreditation might cause other states in which a domestic company operates to not rely on Department examinations, exposing the company to examinations by all the states. This would be a strong incentive for such a domestic company to re-domicile in another state.

Another motivation for these amendments is that the Department's long-term ability to hire and retain qualified financial examiners and actuaries with the expertise to conduct full-scope financial condition exams is highly questionable. If the Department cannot employ its own financial examiners and actuaries, outside consulting will need to be used and related costs will only increase. Today, it costs about \$250 per hour to engage a life actuary, and \$160 per hour for a property and casualty actuary. Examination of a small company would typically require a single actuary, whereas a large company could require 2 or 3 actuaries. Contract financial examiners are often used in addition to actuaries and cost about \$140 per hour. The duration and scope of the work needed for any given examination depends on the size of the company, the

complexity of its business and financial investments. The bottom line is that the Department cannot conduct full-scope audits with its current staff and outside consulting, and the problem will only get worse if the Department cannot sustain its employment.

The Department and affected companies have agreed to a \$50,000 cap for companies with less than \$200 million in gross premiums. This threshold accounts for the smaller size and complexity of business for those companies. The Department believes a cap of \$200,000 for companies with gross premiums of \$200 million or more is realistic and responsible, given the size and scope of operations of such companies.

With a threshold of \$200 million in gross premiums, only 8 of the 40 domestic insurance companies would be subject to the \$200,000 cap on outside consulting fees for financial examinations. The gross premiums in 2010 of these 8 companies ranged from \$370 million to \$1.8 billion, with an average of \$1.09 billion. These are large, sophisticated companies with substantial investments and complicated financial dealings.

The Department also believes a \$200,000 cap for companies in the second tier is a fair figure when compared to the \$50,000 cap to which the first tier companies have agreed. The \$50,000 cap represents an exposure to outside exam fees of \$1.27 per \$1,000 in premium based on an average gross premium of \$39.3 million for the 32 companies under the \$200 million threshold. On the other hand, a \$200,000 cap for the 8 companies with \$200 million or more in gross premiums represents an exposure to outside exam fees of \$.18 per \$1,000 in premium based on an average gross premium of \$1.09 billion. (The company with the smallest gross premium of these, Security Benefit Life, agreed to a \$1 million cap). The main take away from these figures is that the financial exposure a \$200,000 cap represents to the 8 largest companies is on average about seven times smaller than the exposure to which the smaller companies have agreed.

Attached is a list of the domestic companies and their gross premiums written in 2010. Page two gives the totals and averages for the companies under and at/above \$200 million in gross premiums.

The current one-size-fits-all cap for financial condition exams is outdated and inadequate. This fact is recognized by all the Industry groups with whom we have consulted. These amendments are necessary to ensure the Department can utilize outside consultants to conduct proper, full-scope financial exams of domestic companies. Without full-scope exams, the Department's accreditation is in jeopardy, but more importantly, consumers are not adequately protected.

For these reasons, we would ask the Committee to recommend SB 273 favorable for passage.

Thank you for the opportunity to appear in support of this bill. I will be happy to stand for questions at the appropriate time.

Kris Kellim
Government Affairs Liaison
Kansas Insurance Department

**Kansas Insurance Companies
Gross Premiums Written**

<u>NAIC Code</u>	<u>Life Companies</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>	<u>Gross Premium < \$200 M</u>	<u>Gross Premium > \$200 M</u>
12143	Advance Ins. Co. of Kansas 12/31/2010	\$ 11,132,620	-	\$ 11,132,620	\$ 11,132,620	
60542	American Home Life Ins. Co. (The) 12/31/2010	36,309,123	\$ 534,150	36,843,273	36,843,273	
70729	Blue Cross and Blue Shield of Kansas, Inc. 12/31/2010	1,756,579,106	-	1,756,579,106		\$ 1,756,579,106
68276	Employers Reassurance Corp. 12/31/2010	-	1,348,811,854	1,348,811,854		1,348,811,854
71455	Financial American Life Ins. Co. 12/31/2010	21,166,647	-	21,166,647	21,166,647	
68284	Pyramid Life Ins. Co. 12/31/2010	1,764,137,507	-	1,764,137,507		1,764,137,507
68675	Security Benefit Life Ins. Co. 12/31/2010	350,870,486	19,670,531	370,541,017		370,541,017
13175	Surency Life & Health Ins. Co. 12/31/2010	771,195	-	771,195	771,195	
70408	Union Security Insurance Company 12/31/2010	1,083,111,125	218,670,978	1,301,782,103		1,301,782,103
70173	Universal Underwriters Life Ins. Co. 12/31/2010	13,637,913	588,795	14,226,708	14,226,708	
<u>NAIC Code</u>	<u>Property & Casualty</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>		
33154	Alliance Indemnity Co. 12/31/2010	20,504,881	3,285,071	23,789,952	23,789,952	
19186	Alliance Ins. Co., Inc. 12/31/2010	14,093,037	13,140,274	27,233,311	27,233,311	
10235	American Southern Ins. Co. 12/31/2010	35,323,795	8,181,076	43,504,871	43,504,871	
15954	AmTrust Insurance Company of Kansas, Inc. 12/31/2010	31,829,331	(2,843)	31,826,488	31,826,488	
41459	Armed Forces Ins. Exchange 12/31/2010	80,782,362	366,189	81,148,551	81,148,551	
41394	Benchmark Ins. Co. 12/31/2010	54,067,775	1,830,239	55,898,014	55,898,014	
15881	Bremen Farmers Mutual Ins. Co. 12/31/2010	21,204,910	-	21,204,910	21,204,910	
19194	Farmers Alliance Mutual Ins. Co. 12/31/2010	108,266,064	34,684,609	142,950,673	142,950,673	
21628	Farmers Ins. Co., Inc. 12/31/2010	869,337,927	95,576,898	964,914,825		964,914,825
10323	Farmers Mutual Ins. Co. 12/31/2010	2,556,341	-	2,556,341	2,556,341	
11118	Federated Rural Electric Ins. Exch 12/31/2010	143,358,905	2,995,929	146,354,834	146,354,834	
20419	Homesite Indemnity Co. 12/31/2010	53,777,136	52,183,048	105,960,184	105,960,184	
15962	Kansas Bankers Surety Co. 12/31/2010	9,869,114	-	9,869,114	9,869,114	
34703	Kansas Medical Mutual Ins. Co. 12/31/2010	32,010,987	-	32,010,987	32,010,987	
14362	Kansas Mutual Ins. Co. 12/31/2010	7,624,445	-	7,624,445	7,624,445	
<u>NAIC Code</u>	<u>Property & Casualty</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>		
12966	Key Ins. Co. 12/31/2010	22,245,978	-	22,245,978	22,245,978	
14451	Marysville Mutual Ins. Co. (The) 12/31/2010	17,786,778	-	17,786,778	17,786,778	
13126	Midwest Builders' Casualty Mutual Company 12/31/2010	16,267,997	696,448	16,964,445	16,964,445	
13816	MPM Ins. Co. of Kansas 12/31/2010	61,075	-	61,075	61,075	
11878	MutualAid eXchange 12/31/2010	15,004,171	3,938	15,008,109	15,008,109	
37060	Old United Casualty Co. 12/31/2010	118,695,457	4,412,337	123,107,794	123,107,794	

**Kansas Insurance Companies
Gross Premiums Written**

40584	Travel Air Ins. Co. (Kansas) 12/31/2010	-	-	-	-
10696	Travel Air Ins. Co., Ltd 12/31/2010	-	-	-	-
41181	Universal Underwriters Ins. Co. 12/31/2010	648,727,807	26,521,077	675,248,884	675,248,884
15296	Upland Mutual Ins. Co. 12/31/2010	16,155,274	-	16,155,274	16,155,274

<u>NAIC Code</u>	<u>Health Entities</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>	
95489	Coventry Health Care of Kansas, Inc. 12/31/2010	538,158,493	-	538,158,493	538,158,493
12805	UniCare Health Plan of Kansas, Inc. 12/31/2010	143,290,711	-	143,290,711	143,290,711
12969	ValueOptions of Kansas, Inc. 12/31/2010	21,186,262	-	21,186,262	21,186,262

<u>NAIC Code</u>	<u>Nonprofit Dental Service Corporation</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>	
54615	Delta Dental of Kansas, Inc. 12/31/2010	63,852,370	456,653	64,309,023	64,309,023

<u>NAIC Code</u>	<u>Prepaid Dental Service Plan</u>	<u>Direct Premium</u>	<u>Assumed Premium</u>	<u>Total Premium</u>	
52024	CIGNA Dental Health of Kansas, Inc. 12/31/2010	1,720,856	-	1,720,856	1,720,856

Total Premium				<u>\$ 1,257,909,423</u>	<u>\$ 8,720,173,789</u>
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Total Premium Greater Than \$200M

Fee Cap < \$200 M Gross Premium	\$	50,000	Average Gross Premium	\$	39,309,669	\$ 1,090,021,724
Fee Cap > \$200 M Gross Premium	\$	200,000	Fee Cap per \$1,000 Premium	\$	1.27	\$ 0.18
			Number of Companies		32	8



Employers Reassurance Corporation
7101 College Boulevard
Suite 1400
Overland Park, Kansas 66210

March 1, 2012

Via E-MAIL Clark.Shultz@house.ks.gov

Representative Clark Shultz
Capitol Office
Room: 166-W
Seat: 10
Topeka, KS 66612

RE: Proposed Bill (SB273) to amend K.S.A. 40-223

Dear Representative Shultz:

Employers Reassurance Corporation (ERAC) has been contacted by Ken Abitz, Director of Financial Surveillance with the Kansas Insurance Department (KID), to comment on the department's proposed bill (SB273) to amend K.S.A 40-223 regarding the use of consultants in the financial condition examinations of Kansas insurance companies.

We agree with the department that the current cap of \$25,000 on outside consultants' fees for work associated with financial examinations is low. ERAC is an insurance company that would fall into the greater than \$200,000,000 of gross premium tier proposed under the amendment. While we would prefer a lower cap on outside consultant fees for our tier, preferably not to exceed \$150,000, given KID's current process of bidding out the scope of service through RFPs in order to manage consultants' costs, we would be supportive of a \$200,000 cap as currently proposed in SB273.

Feel free to contact me should you require any clarifications.

Regards,

A handwritten signature in black ink, appearing to read 'Irwin Don', written in a cursive style.

Irwin Don
President

Cc: Ken Abitz, Director of Financial Surveillance, KID