



KANSAS INSURANCE DEPARTMENT

Vicki Schmidt, Commissioner

Proponent Testimony for SB 347 – Procurement & Exam Caps

February 12, 2020

Chairman Olson and Members of the Committee,

Thank you for the opportunity to provide testimony in support of SB 347. The bill updates existing law in order to make the Department's regulation of insurance more effective and efficient and help us comply with the NAIC standards required for accreditation. There are two components of this bill. One addresses obstacles the Department faces in efficiently procuring specialized professional services to fulfill the duties and responsibilities outlined in Chapter 40; and the second addresses limitations that hinder adequate oversight of companies domiciled in Kansas.

Under current law and processes, the Department must go through the Department of Administration's procurement process, including for matters specific to insurance regulation. It can be quite challenging to get the right company or consultant hired, often with a lot of back and forth with individuals reviewing the contracts, that do not have the subject matter expertise to understand why a company or consultant that has the lowest bid may not be the right one. This may seem to be the standard process and one generally applicable to state procurement, but there are a number of issues that can arise.

For example, when the Department conducts an examination of a company, that exam must be completed within 18 months as of the year examined, to be in compliance with NAIC accreditation standards. That sounds like a long time, but the reality is it is not when all the factors are considered. First, a company's year-end has to be closed out and then the company submits year-end financial statements to the Department. Once the Department receives those, they are analyzed internally, and Department staff evaluates what expertise will be needed to conduct the exam along with which exams can be conducted internally and which need to be conducted by outside consultants. Even for examinations which can be completed with in-house examination staff, the Department must still retain outside actuarial services as the Department does not have a licensed staff actuary. In both scenarios (the exam completed primarily by internal staff and those which will be outsourced to an examination consultant) the Department must proceed through the bureaucratic Request for Proposal (RFP) process. The RFP process takes several months and significantly shortens the time available for the actual exam work to be conducted. As often is the case, issues are discovered during the examination process which require analysis or additional testing which was not anticipated when the consultant was hired as a result of the RFP process. This creates timing issues if another RFP process must be completed to retain the appropriate expertise to review the identified problem.

In summary, the duration and scope of the work needed for any given examination depends on the size of the company, and the complexity of its business and financial investments. The bottom line is that the Department's responsibilities are stymied by the current procurement requirements and how they interplay with the timing in which examinations must be completed and create impediments to the Department's ability to quickly retain consultants with particular expertise to analyze problems discovered during the exam process.

The Department would offer that our staff are experts on the types of consultants and level of expertise needed for the regulation and supervision of insurers in this state. However, the procurement requirements involve a burdensome process in which the Department's expertise is not given deference and instead the focus is on the consultant submitting the lowest bid. The Department's overarching interest is to retain the consultant(s) which is/are best able to address the work required for a given examination, analysis or actuarial review, not in retaining the cheapest. Again, examinations of some companies involve very complex holding company structures, and complex products, business models, reserving methodologies and investment strategies. To fully protect the policyholders of this state, the Department believes it is paramount to have authority to procure experts in a timely manner utilizing the expertise of staff rather than using a procurement process better suited to the purchase of supplies and materials. It is a reality that not all consultants working in the insurance regulation industry are of equal capability. The Department believes we should be able to retain consultants outside of current constraints which emphasize cost over quality and competency.

The second item we're seeking to address in SB 347 are statutory caps on exam fees which can be incurred for outside consultants. While not directly related to procurement, there can be an interplay between the two. The standards for conducting examinations of companies have changed. The NAIC now requires Departments to utilize what are called "risk focused" examination procedures. Under these procedures, examiners identify during the first phases of the exam, areas which may indicate possible risk to the financial stability of the company. Examiners must then determine, based on those indicators of risk, testing which should be done during later phases of the exam process. What this means, for purposes of explaining why expenditure caps are problematic from a regulatory oversight perspective, is when the Department starts the process of examining a company, it is not known what will be identified as problematic during that exam. If problems are identified that require further exploration, we could encounter a situation that due to the expenditure cap the Department is not able to contract for additional services to evaluate those risks and, as a consequence, would not be able to thoroughly complete an exam in accordance with the risk-based examination requirements.

This is important because our fellow regulators rely on Kansas to ensure that companies domiciled in our state are solvent. If another state in which a Kansas-domiciled company was doing business had reason to believe that an adequate examination was not conducted by Kansas, that state could subject the Kansas-domiciled company to an examination conducted by its staff or consultants according to that state's standards. We fully understand the concern that arises when we suggest there be no cap. However, we are equally concerned that we are now the only state with exam caps, creating reservation for other states regarding the quality of work and putting Kansas-domiciled companies at risk for additional regulation by other states.

We want companies to be domiciled in Kansas. We want to maintain our state regulatory oversight of our domiciled companies in Kansas. We believe it is important to take these measures to give our fellow regulators the confidence that Kansas domiciled companies have appropriate oversight. We believe it is equally important to protect our Kansas companies from regulators in other states subjecting them to further exam costs because of concern about the regulatory oversight of their home state. Most importantly, the Department must maintain the confidence of the NAIC that we are adequately, thoroughly and completely complying with all aspects of required examination procedures to maintain the Department's accreditation.

Thank you for the opportunity to testify on SB 347 and I would be happy to stand for questions.

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