Legal Issues for Boards

ARECA Insurance Exchange Workshop

C. Michael Mattix, J.D., CPCU
Vice President, Reinsurance
Federated Rural Electric Insurance Exchange
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Overview

• Board structure
• *Fundamental responsibility*
• *Fiduciary duties*
• *Role of Board officers*
• *Governance Issues*
  – *Cyber Liability*
  – *Enterprise Risk Management*
AIE Board of Trustees

• **ARECA Insurance Exchange**
  – An inter-insurance exchange whose subscribers inter-insure one another by exchanging contracts of insurance through an attorney-in-fact
  – An insurance exchange is similar to, but different than, a mutual insurance company

• **Two separate entities**
  – Reciprocal inter-insurance exchange
  – Attorney-in-fact (AIM)
AIE Board of Trustees

• Board of Trustees
  – Subscribers advisory committee (a/k/a Board of Trustees)
  – Composed of one person selected by each member that elects to choose a Trustee
  – Terms are for four (4) years
  – If a member elects not to select a person to serve on the Board, then it must be notified at least once every two years of its right to do so
Fundamental Responsibility

• **AIE Board of Trustees charged with:**
  - Supervision of finances
  - General oversight of operations
  - Procure audits/review investments
  - Review surplus requirements / adjust surplus accounts
  - Choosing/monitoring attorney-in-fact

• **AIE Board — matters of policy**

• **AIE Management — day-to-day**
Duty of Care (Diligence)

- Must act with the care that a reasonably prudent person in a similar position would use in similar circumstances
- Perform duties in good faith
- Attentive to the best interests of the cooperative and the membership
- Seek all material information reasonably available prior to making a decision
Duty of Loyalty

- In your role as a board member, your allegiance is to AIE not your local cooperative
- Required to refrain from engaging in personal activities which would injure or take advantage of the Exchange
- Undivided and unselfish loyalty to Exchange
- May not compete to the detriment of the system or usurp an Exchange opportunity

Avoid a conflict of interest
Conflict of Interest

• Importance of a policy
  – Applies to directors and employees
  – Disclosure of financial and other business interests
  – Training and annual review
  – Consistent enforcement
  – Annual written statements
Confidential Information

• Importance of a policy
  – Applies to directors and employees
  – Exclusive property of the Exchange
  – Definition – all information and any ideas in whatever form pertaining in any manner to the business of the Exchange
  – Duty to keep confidential
  – Duty to return upon resignation or retirement
Duty of Obedience

• **Required to perform duties in accordance with applicable statutes, regulations, ordinances, charter, bylaws, policies**

• **Keep the organization within the stated bounds of its mission**

• **Ultra vires acts are those which exceed the legal powers of the Exchange – voidable by law and may result in personal liability**
Role of the Board Chair

• AIE General Bylaw provisions:
  – Preside at all meetings of members and the Board
  – Sign documents as authorized by the Board or required by law
  – Ex officio member of all standing committees
  – Perform all duties incident to the office of Chair and such other duties as assigned by the Board
  – Appoints members of Executive Committee
Role of the Board Vice-Chair

- AIE General Bylaw provisions:
  - In the absence or disability of the Chair, the Vice Chair shall perform all the duties of (and be subject to all of the restrictions upon) the Chair
Role of the Board Secretary

- AIE General Bylaw provisions:
  - Keep a record of minutes of all meetings of the Board, both regular and special
  - Document the names of those present at Trustees’ meetings and the number of members present at members’ meetings
  - If a special meeting is called, the Secretary must record how the meeting was authorized and the manner and time of notice given
Nomination/Election of Board of Trustees

• One member, one vote
• Each member selects a representative to the subscribers’ advisory committee also known as the AIE Board of Trustees
• Four year terms
• If member chooses not to select Trustee, they must be notified at least every 2 years
• Board consists of at least 7
Executive Committee

• Appointed by Chairperson of the Board
• Consists of seven persons, including Chair
• May include individuals who are not Trustees, but no more than two
• EC has power of Board of Trustees while Board not in session (with limitations)
• Serves as the Board of ARECA
Governance Issues -- Cyber Security

- Data breaches have become commonplace
- Safeguard customer data
  - Cost of notice to customers
  - Price of credit monitoring
- Protect against interruption of service
- Enterprise Risk Management -- perform an audit of your IT risk profile
Questions to ask

- Does our organization have a social media policy and what does it cover?
- Is there a designated person in the organization to manage social media?
- Do we monitor social media internally, or is the function outsourced?
Questions to ask

• Does our organization have a cyber incident response plan to mitigate reputational damage from a cyber incident?

• What role would the board have in responding to a cyber incident, and is that role clearly defined?

• Where does the responsibility for risk and crisis management lie with the board?
Governance Issues -- Risk Management

- Identification of risk factors
- Review of key business controls
- Periodic review of external vendors
  - Auditors
  - Attorneys
  - Actuaries
  - Consultants
- Conflicts of interest
Questions to ask

• Does our organization have a strategy that we believe will enable us to achieve its goals?

• Does our organization have the resources necessary to achieve our objectives?

• Does our board have the right qualifications for the current environment?
Questions to ask

• What is the board’s working relationship with management?

• Is there a constructive, positive dialogue among directors and management regarding strategic choices?

• Are we confident management and the board are “on the same page” regarding strategy?
Questions to ask

• How aligned is our organization’s risk appetite with its strategic choices?

• Are we too risk averse to consider and fully explore alternative strategy alternatives?

• Or is our risk appetite so great that we are in danger of making unsound strategic choices?
Questions to ask

• Does the board hold strategic retreats or meetings? How often?

• Does each retreat build upon the prior retreats, so the board progressively expands its knowledge and understanding of strategic issues?
Summary

- **Fiduciary duties**
  - Duty of care, loyalty, obedience
- **Role of Board officers**
- **Governance issues**
  - Cyber Liability
  - Enterprise Risk Management
APPENDIX

• AIM Board Structure
• AIM Board Responsibilities
• More information re director compensation (for your home cooperative)
Fundamental Responsibility

- **AIM Board has broadly defined powers**
  - “...shall have control and management of the affairs and business of the corporation...”

- **AIM Board is “attorney-in-fact” of AIE**

- **AIM Board – matters of policy / general oversight functions**

- **AIE Management – day-to-day**
Role of the Board
President

• General Bylaw provisions:
  – Preside at all meetings of members and the Board
  – Fix the compensation of all employees and agents of the corporation, subject to approval
  – Sign documents as authorized by the Board or required by law
  – Perform all duties incident to the office of President and such other duties as assigned by the Board
Role of the Board President

- Providing leadership
- Making procedural decisions
- Setting the agenda for Board meetings
- Running an efficient meeting
- Encouraging Board members to voice their views
- Operating within the parameters established by the Board
Role of the Board President

- Lead the Board, not the CEO
- Lead the Board to define its own job
- Lead the Board to design its discipline
- Lead the Board to evaluate its performance
- Take responsibility for the agenda
- Run participative but efficient meetings
- Take the long view – build capability
Role of the Board Secretary

• **General Bylaw provisions:**
  – Preparing the minutes of the Board meetings
  – Authenticating the corporation’s records
  – Fixing the cooperative’s seal to any document authorized by the Board
  – Keep records of all shareholders, including number and class of shares
  – Performing all other duties as assigned
Role of the Board Secretary

- Seeing that all notices are duly given as required by bylaws or by law
- Safekeeping of the corporate books and records
- Keeping a register of the names and post office addresses of all members
- File of complete copy of Article of Incorporations and Bylaws, including amendments
  - Furnishing copies to each member
Role of the Board Secretary

- Minutes
  - Denoting adequate discussion
  - Recording votes
  - Ensuring an adequate file is kept of all documents and other information available to the Board
  - More than a minimalist approach
  - Less than a tape-recorded approach
  - Notes and other documents
Role of the Board Treasurer

- **General Bylaw provision** – custody or all corporate funds and securities and the receipt, deposit or investment of all corporate monies
- **Sign and endorse on behalf of the corporation** all checks, drafts, notes, or other payment
- **Keep accurate books of account and other financial records**
- **Report on the condition of finances at each regular Board meeting**
Role of the Board Treasurer

• Review in light of increasing roles of CEO’s and CFO’s
• Transformation to chairman of the Audit Committee
• Primary Board contact for the outside auditor
Governance Issues

- Nomination and election of directors
- Director compensation
- Performance expectations
  - Board self-evaluation
  - Director education and development
  - CEO evaluation
  - Attorney evaluation
  - Auditor evaluation
Director Compensation

• Three components to determining director compensation
  – What are directors being paid to do?
  – How are directors being paid?
  – How much should directors be paid?

• AIE Board of Trustees
  – No compensation for service other than reimbursement for expenses incurred in conformance with Board policy
Director Compensation

NACD principles:

1. Director compensation should be determined by the Board and disclosed completely to the members

2. Director compensation should be aligned with the long-term interest of the members

3. Compensation should be used to motivate director behavior
Director Compensation

NACD principles:

4. Directors should be adequately compensated for their time and effort.

5. Director compensation should be approached on an overall basis, rather than as an array of separate elements.
Director Compensation

• Legal authority
  – State statutes
  – Cooperative bylaws
  – Board policy

• Methodology
  – Reliance on comparable data
    • Review prior to making determination
  – Concurrent documentation (minutes)
Performance Expectations

• Board self-evaluation
• Director education and development
• CEO evaluation
• Attorney evaluation