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NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Governance Resource

November 2007

Mutual Insurance Company Proxy Practice

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What is a proxy?

In a mutual insurance company, policyholders possess certain rights regarding governance of the organization. These are often called participation rights, and one element of these rights is the right to attend policyholder meetings and vote on company matters. As a practical matter, it has been the experience of a number of companies that, in spite of the right to participate, policyholders choose not to attend such meetings. This lack of participation can result in less than a sufficient number of policyholders attending who are able to provide a quorum to transact business.

In order to have enough policies represented at a meeting to properly conduct business, or to simply give policyholders a convenient means of participating in company governance, a company may solicit proxies from its policyholders.[1] A proxy is an instrument that authorizes a person to vote on behalf of another at a duly called meeting of policyholders. The ability to vote by proxy must be authorized or allowed under the governing documents of the company, such as the articles or bylaws.

For mutual insurance companies, proxies are most often solicited for an annual meeting at which directors are elected, or for special meetings that may be called to address more unusual corporate matters, such as mergers. The authority conferred by a proxy will be consistent with the terms of the proxy itself, and, unless restricted, will generally apply to all matters properly before the meeting and for which appropriate notice has been given.

Proxies are generally obtained on the part of and in the name of management or perhaps an officer of the boards in order to authorize voting on the policyholder's behalf. The proxy may describe how the proxy will be voted, or it may allow the policyholder to select among several options regarding how they wish their vote to be cast, (e.g. vote for or against a matter, to withhold their vote, or to abstain from voting).

Companies obtain or solicit proxies in a number of ways. Some companies obtain proxies at the time an insurance policy application is submitted. These proxies typically will authorize voting on the policyholder's behalf at all policyholder meetings that are held during the time the policyholder is insured by the company. Other companies chose to obtain proxies once each year, and still other companies obtain their proxies prior to each meeting. State law may impact how often proxies are solicited since some states set specific time limits during which a proxy remains effective.[2]

Proxy practice and reform

Proxy practice for a company consists of the frequency, use, and terms of proxies obtained from policyholders. This includes, among other things, how many proxies are solicited, how often a proxy solicitation takes place, how many times a solicitation is required to obtain the needed amount of proxies, the power conferred by the proxy, the revocability of the proxy, and access by persons other than management to the proxy process. Proxy practice is influenced not only by the governing documents of the organization but by state law applicable to corporate governance matters.

Proxy issues are very prominent in current debates about improving corporate governance – notably so for public companies that have considerable numbers of shareholders. These issues can impact the practice of proxy solicitation directly. Current issues include:

- Access by persons other than management to a company's proxy process in order to place proposals or director nominees before a company's shareholders (or, in the case of mutual companies, its policyholders).
- Whether to require directors to be elected by a majority vote in favor of the director – which effectively requires votes in favor to exceed votes that are either against or withheld. This requirement considerably expands the importance and impact of proxies on director elections.
- The ability to obtain proxies by fax or Internet – a growing development impacting governance participation by shareholders or policyholders.

Private company proxy practice

Private companies like mutual insurance companies are not directly affected by public company governance reforms. However, public company governance reform typically influences private company governance through the courts or, within highly regulated industries like insurance, through regulatory authorities.

This report presents and discusses the findings of a survey conducted by NAMIC to determine the state of proxy practices by mutual insurance companies.[3] As a result of this survey and report, mutual companies may become increasingly aware of the use of proxies to assist in governance and of proxy practices that they might wish to consider in their own companies. It may also help companies anticipate any public company proxy reform that may influence private mutual insurance companies

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Frequency of proxy solicitations

The most common method for a mutual insurance company to obtain a proxy is to solicit one when needed, namely for each annual or special policyholders meeting. Twenty percent of responding companies use this method of proxy solicitation. Less common is the practice of obtaining an annual proxy that applies to all meetings held during the year. Nearly 17 percent of responding companies use this method. On average, companies solicit proxies 60 days before the meeting, but actual time frames ranged from 14 days to nearly one year. One year time frames typically occur if the proxy is obtained on the date of policy renewal or at the time of billing.

Of all responding companies that solicit proxies from policyholders, securing an *omnibus* proxy, a single proxy to cover all meetings occurring while the person is a policyholder, is the least common method used. Only 14 percent of responding companies solicit such a proxy. For companies that obtain an omnibus proxy, the most frequent means of obtaining that proxy is through part of the application process for an insurance policy (36 percent). The Appendix to this report contains an example of the language used on an application for an omnibus proxy. Another sizeable percentage of companies – 27 percent - obtain an omnibus proxy at the time the policy is issued to the policyholder.

A sizeable percentage of responding companies do not use proxies at all. This is generally because proxies are not allowed under their articles or bylaws or because state law does not allow them to solicit proxies. One

responding company reported that while it solicits an omnibus proxy, under state law the proxy is only valid for a period of five years, at which time another omnibus proxy is requested.

Policyholders who are solicited

Sixty-four percent (64%) of responding companies that solicit proxies annually or for each policyholder meeting do so from all policyholders. The alternative practice – to solicit only a percentage of policyholders – is used by the remaining companies to obtain a sufficient number of proxies to constitute a quorum to conduct policyholder business.

For those companies that solicit only a percentage of their policyholders, 25 percent of the companies select the policyholders to be solicited on a random selection basis, and 17 percent select policyholders on the basis of their renewal date. In the remaining number of companies, a variety of other election methods are used, – many are specific to the history, tradition, or circumstances of the individual company.

Eighty percent of the time, companies that solicit only a percentage of their policyholders do not find it necessary to conduct follow-up solicitations in order to obtain sufficient proxies to hold a meeting. Of those that do find follow-up soliticiations necessary, only 5 percent of companies have had to conduct such a follow up frequently. This would indicate that mutual policyholders are generally responsive to proxy solicitations, or that companies are doing a satisfactory job of identifying the right percentage of policyholders to initially solicit in order to obtain a sufficient response.

Revocation

Seventy percent of the companies that solicit proxies on a per meeting basis report that the proxy obtained from their policyholders is revocable. That figure is higher – 80 percent - for those companies that solicit proxies on an annual basis. The difference might possibly be explained by the fact that the proxy obtained on a per meeting basis is intended to last for a shorter time than for those solicited on an annual basis. That shorter time frame would make it difficult for companies to respond to revocations that might occur before the meeting and still to assure a sufficient number of proxies for a quorum.

Of course, state law impacts the revocability of a proxy, irrespective of whether the proxy itself addresses the issue. For instance, simply authorizing a subsequent proxy will revoke an earlier one, and showing up at the policyholder meeting will revoke a previously authorized proxy.

Voting instructions

Generally speaking, responding companies were more inclined to allow a policyholder to *withhold* their vote for a director nominee by proxy – 76 percent – than to allow a policyholder to vote *against* a director by proxy – 47percent. This has an interesting relevance with regards to any current governance reform proposals requiring a majority vote to elect a director. In director elections requiring a majority vote, a withheld vote would count against a director and make election more difficult. Only 35 percent of responding companies allow policyholders to choose to *abstain* from voting by proxy.

Proxy information

Public company governance reform has focused significant attention on the *kind* of information that is provided with proxy solicitations. For mutual insurance companies, the kind of information supplied most often is financial information, (51 percent of companies) and biographical information concerning director nominees, (48 percent of companies).

The *form* of information that is most often provided to policyholders with a proxy solicitation is the company's annual report – 69 percent.

One of the more vigorous recent governance reform efforts has focused on requiring more detailed information about the compensation of executive management. With respect to this issue, there is an important distinction to note between mutual company policyholders and public company shareholders. Public company shareholders have a financial investment in the company as owner. As a result, the compensation of management, especially as it relates to performance of that investment, is

a significant and understandable interest. Mutual company policyholders do not have a financial investment interest in the company.

The absence of an investment interest could account for the lack of mutual insurance company proxy information regarding executive compensation. Our survey indicates that only 10 percent of mutual insurance companies provide policyholders any information regarding the compensation of executive officers or the compensation of directors.

Director Nominations

Another area of considerable activism regarding public company proxy practice is the level of access by shareholders to the company's proxy process. Typically in public companies, access to the proxy process has been very limited or non-existent. Governance reform advocates argue that this places shareholders, who are the true owners of the company, at a significant disadvantage in nominating their own director candidates or presenting their own proposals, especially as these may conflict with those of management. This drive to provide greater access for shareholders to nominate directors or include their own proposals in proxy materials reflects their direct and substantial investment interest in the company. Where that interest does not exist, the ability to include director nominees or proposals from individuals other than those of management in proxy materials seems a less direct interest.

Interestingly, it is clear that the overwhelming majority of mutual insurance companies responding to the survey – 80 percent – allow policyholders to submit nominations for directors before a meeting. Only a slightly smaller percentage of companies – 70 percent - actually require that these nominations occur within a set time before a policyholder's meeting. However, a significant number of survey respondents – 74.6 percent – do not include information about such nominees in the proxy solicitation materials sent to policyholders. A similar percentage of companies do not allow policyholders the ability to vote for such nominees by proxy – 78.4 percent.

Policyholder Proposals

One-third of the companies surveyed require that policyholders submit in advance any proposals they wish to raise at a policyholders meeting. In slightly more than half of these companies, any such policyholder proposal will be described in the materials that accompany a proxy solicitation. However, in most cases, the proxy solicited does not include the ability to indicate how the policyholder wishes the proxy to be voted regarding such a proposal.

Digital/electronic proxy process

All of the companies responding to the NAMIC survey solicit proxies through the mail. Less than 5 percent of responding companies report that they send, or offer to send, proxy materials by fax or through the Internet.

Interestingly, companies are more willing to *accept* proxies by fax, phone or the Internet. Our survey indicates that 25 percent of responding companies offer to receive proxies by fax, and that 8 percent of the companies offer to receive proxies through the Internet.

Of the proxies received by some means other than the mail, slightly more than 40 percent are received by fax and the remainder are received either by phone or the Internet.

Endnotes

1. A company's articles and bylaws may not allow policyholders the opportunity to vote by proxy. The following is an example of a bylaw provision of a NAMIC member that prohibits proxies:

> "Each member or policyholder shall have one vote at all meetings, regardless of the number of policies held or the number of names upon the policies, and there shall be no vote cast by proxy; provided however, that in the event of joint tenancies, either party may vote, upon designation by the other."

2. State or provincial law does indeed control whether a proxy may be obtained, or if allowed, the type, duration, or other attributes of a policyholder proxy.

One responding company reported that their state of domicile, South Carolina, limited the effectiveness of proxies to one year. Another reported that the Insurance Act of Ontario did not permit voting by proxy, but that federally licensed Canadian companies were permitted to use proxies.

3. The proxy survey was conducted in November 2006 and distributed to all of NAMIC's 900+ member companies, and 143 responses were obtained from NAMIC members.

Appendix

Proxy as Part of an Application

I appoint the members of the Board of Governors, and each of them, agents and attorneys with powers of substitution in each of them, my lawful proxy to vote and act for me and in my name at all annual, regular, and special meetings of the _____ Company.

This proxy is solicited on behalf of the management of the _____ Company and will empower the holders to vote on the Subscriber's behalf for the election of members of the Board of Governors and such other business as may properly come before any annual, regular, or special meeting of Subscribers.

This proxy, unless revoked or replaced by substitution, shall remain in force for five years from the date stated below.

You may revoke this proxy by giving the Company written notice of your revocation at least 10 days before the date of any annual, regular, or special meeting at which such proxy is to be exercised. If you attend a meeting, you may revoke this proxy if you choose to vote in person.

The signing of this proxy is not a condition of completion of this application and your signature, or your failure or refusal to sign, will not be considered in connection with the underwriting of your application.

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