

BEFORE THE COMMISSIONER OF SECURITIES AND INSURANCE
OFFICE OF THE MONTANA STATE AUDITOR

In the matter of the adoption of NEW) NOTICE OF PUBLIC HEARING ON
RULES I through V relating to) PROPOSED ADOPTION
corporate governance annual)
disclosures)

TO: All Concerned Persons

1. On October 17, 2017, at 9:00 a.m., the Commissioner of Securities and Insurance, Montana State Auditor (CSI), will hold a public hearing in the basement conference room, at the Office of the Commissioner of Securities and Insurance, Montana State Auditor, 840 Helena Ave., Helena, Montana, to consider the proposed adoption of the above-stated rules.

2. The CSI will make reasonable accommodations for persons with disabilities who wish to participate in this rulemaking process or need an alternative accessible format of this notice. If you require an accommodation, contact the CSI no later than 5:00 p.m. on October 3, 2017, to advise us of the nature of the accommodation that you need. Please contact Ramona Bidon, CSI, 840 Helena Avenue, Helena, Montana, 59601; telephone (406) 444-2726; TDD (406) 444-3246; fax (406) 444-3499; or e-mail rbidon@mt.gov.

3. The rules as proposed to be adopted provide as follows:

NEW RULE I PURPOSE (1) The purpose of these rules is to set forth the procedures for filing and the required contents of the CGAD necessary to carry out the provisions of the Corporate Governance Disclosure Act, 33-2-2101 through 33-2-2109, MCA.

AUTH: 33-2-2105, MCA

IMP: 33-2-2101, 33-2-2102, 33-2-2103, 33-2-2104, 33-2-2105, 33-2-2106, 33-2-2107, 33-2-2108, 33-2-2109, MCA

NEW RULE II DEFINITIONS The following definitions apply to this subchapter:

(1) "CGAD" means the corporate governance annual disclosure required under Title 33, chapter 2, part 21, MCA.

(2) "Insurance group" means those insurers and affiliates included within an insurance holding company system as defined in 33-2-1101, MCA.

(3) "Senior management" means any corporate officer responsible for reporting information to the board of directors at regular intervals or providing this information to shareholders or regulators. "Senior management" includes the chief executive officer, chief financial officer, chief operations officer, chief procurement officer, chief legal officer, chief information officer, chief technology officer, chief revenue officer, chief visionary officer, or any other "C" level executive.

AUTH: 33-2-2105, MCA

IMP: 33-2-2101, 33-2-2102, 33-2-2103, 33-2-2104, 33-2-2105, 33-2-2106, 33-2-2107, 33-2-2108, 33-2-2109, MCA

NEW RULE III FILING PROCEDURES (1) An insurer, or the insurance group of which the insurer is a member, required to file a CGAD by Title 33, chapter 2, part 21, MCA, shall, no later than June 1 of each calendar year, submit to the commissioner a CGAD that contains the information described in [New Rule IV] for the prior calendar year.

(2) The CGAD must include a signature of the insurer's or insurance group's chief executive officer or corporate secretary attesting to the best of that individual's belief and knowledge that:

(a) the insurer or insurance group has implemented the corporate governance practices; and

(b) a copy of the CGAD has been provided to the insurer's or insurance group's board of directors or the appropriate committee of the board of directors.

(3) The insurer or insurance group shall have discretion regarding the appropriate format for providing the information required by this subchapter and is permitted to customize the CGAD to provide the most relevant information necessary to permit the commissioner to gain an understanding of the corporate governance structure, policies, and practices utilized by the insurer or insurance group.

(4) For purposes of completing the CGAD, the insurer or insurance group may choose to provide information on governance activities that occur at the ultimate controlling parent level, an intermediate holding company level, or the individual legal entity level, depending upon how the insurer or insurance group has structured its system of corporate governance.

(a) The insurer or insurance group is encouraged to make the CGAD disclosures at the level at which:

(i) the insurer's or insurance group's risk appetite is determined;

(ii) the earnings, capital, liquidity, operations, and reputation of the insurer are overseen collectively and at which the supervision of those factors are coordinated and exercised; or

(iii) legal liability for failure of general corporate governance duties would be placed.

(b) If the insurer or insurance group determines the level of reporting based on these criteria, it shall indicate which of the three criteria was used to determine the level of reporting and explain any subsequent changes in the level of reporting.

(5) As outlined in 33-2-2104, MCA, if the CGAD is completed at the insurance group level, and if the lead state has substantially adopted the requirements contained in the Corporate Governance Disclosure Act, then it must be filed with the lead state of the group as determined by the procedures outlined in the financial analysis handbook adopted in [New Rule V]. A copy of the CGAD must also be provided to the chief regulatory official of any state in which the insurance group has a domestic insurer upon request.

(6) An insurer or insurance group may comply with this section by referencing other existing documents, including the ORSA Summary Report, Holding Company Form B or F Filings, Securities and Exchange Commission (SEC) Proxy Statements, or foreign regulatory reporting requirements, if the documents provide information that is comparable to the information described in [New Rule IV]. The insurer or insurance group shall clearly reference the location of the relevant information within the CGAD and attach the referenced document if it is not already filed or available to the regulator.

(7) Each year following the initial filing of the CGAD, the insurer or insurance group shall file an amended version of the previously filed CGAD indicating any changes made since the filing. If no changes were made, the insurer or insurance group should state that in the filing.

AUTH: 33-2-2105, MCA

IMP: 33-2-2101, 33-2-2102, 33-2-2103, 33-2-2104, 33-2-2105, 33-2-2106, 33-2-2107, 33-2-2108, 33-2-2109, MCA

NEW RULE IV CONTENTS OF CORPORATE GOVERNANCE ANNUAL DISCLOSURE

(1) The insurer or insurance group shall be as descriptive as possible in completing the CGAD, and shall include any relevant attachments or example documents that are used in the governance process.

(2) The CGAD shall describe the insurer's or insurance group's corporate governance framework and structure. Its description shall include consideration of:

(a) the board of directors, including the rationale for the current board size and structure, the committees ultimately responsible for overseeing the insurer or insurance group, and the levels at which that oversight occurs, such as the ultimate control, intermediate holding company, or legal entity level; and

(b) the duties of the board and each of its significant committees and how they are governed, such as bylaws, charters, or informal mandates, as well as how the board's leadership is structured, including a discussion of the roles of chief executive officer and chairman of the board within the organization.

(3) The insurer or insurance group shall describe the policies and practices of the most senior governing entity and its significant committees, including a discussion of:

(a) how the qualifications, expertise, and experience of each board member meets the needs of the insurer or insurance group;

(b) how an appropriate amount of independence is maintained on the board and its significant committees;

(c) the number of meetings held by the board and its significant committees over the past year, and information on director attendance;

(d) how the insurer or insurance group identifies, nominates, and elects members to the board and its committees. The discussion should include:

(i) whether a nomination committee is in place to identify and select individuals for consideration;

(ii) whether term limits are placed on directors;

(iii) how the election and reelection processes function; and

(iv) whether a board diversity policy is in place and if so, how it functions.

(e) The processes in place for the board to evaluate its performance and the performance of its committees, as well as any recent measures taken to improve performance. The discussion should disclose any board or committee training programs.

(4) The insurer or insurance group shall describe the policies and practices for directing senior management, including a description of:

(a) any processes or practices, including suitability standards, to determine whether officers and key persons in control functions have the appropriate background, experience, and integrity to fulfill their prospective roles, including:

(i) identification of the specific positions for which suitability standards have been developed and a description of the standards employed; and

(ii) any changes in an officer's or key person's suitability as outlined by the insurer's or insurance group's standards and procedures to monitor and evaluate such changes.

(b) the insurer's or insurance group's code of business conduct and ethics, including consideration of:

(i) compliance with laws, rules, and regulations; and

(ii) proactive reporting of any illegal or unethical behavior.

(c) the insurer's or insurance group's processes for performance evaluation, compensation, and corrective action to ensure effective senior management throughout the organization, including a description of the general objectives of significant compensation programs and what the programs are designed to reward. The description shall include sufficient detail to allow the commissioner to understand how the organization ensures that compensation programs do not encourage or reward excessive risk taking. Elements to be discussed may include:

(i) the board's role in overseeing management compensation programs and practices;

(ii) the various elements of compensation awarded in the insurer's or insurance group's compensation programs and how the insurer or insurance group determines and calculates the amount of each element of compensation paid;

(iii) how compensation programs are related to both company and individual performance over time;

(iv) whether compensation programs include risk adjustments and how those adjustments are incorporated into the programs for employees at different levels;

(v) any clawback provisions built into the programs to recover awards or payments if the performance measures upon which they are based are restated or otherwise adjusted; and

(vi) any other factors relevant in understanding how the insurer or insurance group monitors its compensation policies to determine whether its risk management objectives are met by incentivizing its employees; and

(vii) the insurer's or insurance group's plans for chief executive officer and senior management succession.

(5) The insurer or insurance group shall describe the processes by which the board, its committees, and senior management ensure an appropriate amount of oversight to the critical risk areas impacting the insurer's business activities, including a discussion of:

- (a) how oversight and management responsibilities are delegated between the board, its committees, and senior management;
- (b) how the board is kept informed of the insurer's strategic plans, the associated risks, and steps that senior management is taking to monitor and manage those risks; and
- (c) how reporting responsibilities are organized for each critical risk area. The description must allow the commissioner to understand the frequency at which information on each critical risk area is reported to and reviewed by senior management and the board. This description may include, for example, the following critical risk areas of the insurer:
 - (i) risk management processes. An ORSA Summary Report filer may refer to its ORSA Summary Report pursuant to 33-2-1130 through 33-2-1138, MCA;
 - (ii) actuarial function;
 - (iii) investment decision-making processes;
 - (iv) reinsurance decision-making processes;
 - (v) business strategy and finance decision-making processes;
 - (vi) compliance function;
 - (vii) financial reporting and internal auditing; and
 - (viii) market conduct decision-making processes.

AUTH: 33-2-2105, MCA

IMP: 33-2-2101, 33-2-2102, 33-2-2103, 33-2-2104, 33-2-2105, 33-2-2106, 33-2-2107, 33-2-2108, 33-2-2109, MCA

NEW RULE V ADOPTION OF NAIC FINANCIAL ANALYSIS HANDBOOK

(1) For purposes of review of holding company systems and corporate governance disclosures, the commissioner adopts the financial analysis handbook, volumes one and two, most recently published on January 2, 2017 by the National Association of Insurance Commissioners. Copies of both volumes of the financial analysis handbook are available at: www.naic.org/prod_serv_publications.htm.

AUTH: 33-2-2105, 33-2-1117, MCA

IMP: 33-2-1111, 33-2-2101, 33-2-2104, MCA

REASON: The CSI proposes to adopt NEW RULES I through V in support of implementation of the Corporate Governance Annual Disclosure Act (Act). The Act was passed by the 2017 Legislature and signed by Governor Bullock on February 13, 2017. The Act is model legislation derived from the National Association of Insurance Commissioners (NAIC) Corporate Governance Annual Disclosure Model Act. The Act, and specifically 33-2-2106, MCA, requires that corporate governance annual disclosures be prepared consistent with rules promulgated for the purpose. The NAIC has developed the Corporate Governance Annual Disclosure Model Regulation for this purpose; New Rules I through IV are derived from this model regulation.

The disclosure requirements of the Act take effect in the calendar year 2018; adoption of these rules is necessary to provide insurers with guidance on what

actions are required to comply with the Act. New Rules I and II set forth the purpose of the rules and definitions used therein. New Rule III is necessary to provide insurers guidance regarding the procedure for filing the required disclosures. New Rule IV describes the contents of the corporate governance annual disclosure; this adoption is required under 33-2-2106(2), MCA. Finally, New Rule V adopts the most current version of the NAIC financial analysis handbook, as required by 33-2-1111 and 33-2-2104, MCA.

4. Concerned persons may submit their data, views, or arguments either orally or in writing at the hearing. Written data, views, or arguments may also be submitted to: Michael A. Kakuk, Attorney, Office of the Commissioner of Securities and Insurance, Montana State Auditor, 840 Helena Ave., Helena, Montana, 59601; telephone (406) 444-0385; fax (406) 444-3497; or e-mail mkakuk@mt.gov, and must be received no later than 5:00 p.m., October 25, 2017.

5. Michael A. Kakuk, Attorney, has been designated to preside over and conduct this hearing.

6. The CSI maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this agency. Persons who wish to have their name added to the list may sign up by clicking on the blue button on the CSI's website at: <http://csimt.gov/laws-rules/> to specify for which program the person wishes to receive notices. Notices will be sent by e-mail unless a mailing preference is noted in the request. Request may also be sent to the CSI in writing. Such written request may be mailed or delivered to the contact information in 2 above, or may be made by completing a request form at any rules hearing held by the CSI.

7. The bill sponsor contact requirements of 2-4-302, MCA apply and have been fulfilled. The primary bill sponsor was contacted by mail on July 28, 2017.

8. With regard to the requirements of 2-4-111, MCA, the department has determined that the adoption of the above-referenced rules will significantly and directly impact small businesses.

/s/ Michael A. Kakuk
Michael A. Kakuk
Rule Reviewer

/s/ Kris Hansen
Kris Hansen
Chief Legal Counsel

Certified to the Secretary of State September 11, 2017.