



Little Switzerland, North Carolina
(Or it looks like this anyway)

***Captive Insurance Corporate Secretary and Corporate
Governance Newsletter***

Volume One, No. 1
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Compliments of John J. O'Brien JD, CLU, CPCU

Dear Friend:

This letter is to introduce you to the first issue of the Captive Insurance Corporate Secretary and Corporate Governance Newsletter.

As of April 1, 2007, I have established my own legal, consultant and expert witness practice. While operating Charleston Captive Management and since then while working for CCM's successor Wilmington Trust, I became interested in ethics and corporate governance. These areas had always intrigued me even when engaged in the private practice of law before forming a captive management company. Recently I was given the opportunity to instruct for the ICCIE ethics course and this multiplied this interest especially as it relates to corporate governance of captive insurance companies and in particular the roles that service providers such as auditors, attorneys and captive managers play in the corporate governance of these alternative risk vehicles. To me this area is

undergoing transition and I felt that there might be a need for a newsletter like this. Once my interest is pique, I'm always prepared to research and write and share with others in the hope that I'll find an appreciative audience and in some way be contributing to the overall good of our industry and to your work in it.

And of course, I hope that this newsletter could lead to the opportunity to develop relationships as corporate attorney, secretary or even as a board of directors member to round out the consulting and expert service work I am now enjoying. Some of you had the opportunity to be invited to the wonderful "insurance leadership conferences" that Russell Miller organized years back in San Francisco and know of the valuable written material we received there as well as the contacts we all made there. Russell Miller did much to bring insurance professionals together with flattering invitations to us as insurance industry leaders to attend the conferences he organized. Always, somewhere in Russell's material one could find a very direct reminder in small type- "We want your business." He pursued that business in such a high fashion through valuable publications and meaningful conferences that he brought lasting value to anyone who had the opportunity to participate. Many of us benefited in our own businesses through the efforts of Russell Miller as he grew his business although many of us like me never had the opportunity to hire Russell Miller or his "well thought of" company.

This newsletter is offered in the Russell Miller style and in tribute to him. I want your business but even without it, I hope at least that you will find value in this newsletter and that the information provided will benefit you and your clients and make a contribution to our industry as the ethical and corporate governance climate in it undergoes change. If I can merit your approval, then this newsletter will be a success.

In this issue I am featuring two check lists – one is suggested for a corporate secretary to follow in the organizational board of directors meeting of a risk retention group or captive (this is taken from a paper I have prepared, namely, Risk Retention and Purchasing Groups in a Nutshell) and the other is an audit

committee checklist where I opine that the items set forth there are also a good checklist for board of directors of captives and risk retention groups even when an audit committee is not required. In future newsletters, I hope to be able to provide information to you in five areas:

- 1. Newly proposed or passed legislation or regulations that deal with ethics and corporate governance.*
- 2. New case law that is directed towards ethics as well as corporate governance.*
- 3. Some guidelines and personal comments from me that might be helpful to you and your clients.*
- 4. References to recent publications and law review articles dealing with ethics and corporate governance – perhaps even, if I dare, a book review.*
- 5. Comments I may have heard from readers since the last issue or answers to questions that have been proposed to me.*

You are on the list to receive this because I know you or know of you and thought you might find the information provided helpful. Feel free to cut and paste anything and share with your clients or others. If you know others who might find this material useful, simply let me know their email address sent to lionsthree @ aol.com and I'll be glad to add their names to the distribution lists. Of course if you would like to be removed from the list, please let me also know that.

Thanks for your attention and I hope you find the newsletter worthwhile.

Sincerely yours,

John

P.S. My practice is conducted out of Charleston, South Carolina as well as Little Switzerland, South Carolina (when I head for the hills). The mountain range pictured above represents the Blue Ridge Mountains where this first newsletter was compiled. The next newsletter will originate from the lowcountry.

**Risk Retention Group Board of Directors
Organizational Meeting Checklist
Organizational Steps and Management after Formation and Licensing**

The domiciliary state will issue a license to the risk retention group if the regulators are happy with the application material submitted by the group. Sometimes, this license is written subject to certain conditions. One constant condition is that no business can be written until the risk retention group is capitalized.

It is necessary that the risk retention group has an organizational meeting of the shareholders and board of directors. The requirements for these meetings vary as to where the meetings should be held and who should attend. There usually is a requirement that the risk retention group has at least one director who is a resident of the domicile. This role is typically played by the captive manager. The captive manager after stewardship of the application for license through his state's insurance department now becomes the bedrock for future compliance and regulatory reporting of the risk retention group. My experience has been that sometimes attorneys are reluctant, for reasons related to their malpractice coverage I believe, to serve on the board of directors for risk retention groups and captives that they have been appointed attorney for. From my perspective, there are good reasons to have the local attorney serve as the resident director of the captive and risk retention group as well as corporate secretary. This presents an ideal arrangement for the corporate attorney to be in a position that he can ensure that all safeguards that are required to attain maximum corporate compliance and corporate minutes record keeping are in place. The captive manager on the other hand typically comes to the resident director job from a financial background and might not have the same level of training in corporate governance as the captives or risk retention group's attorney does.

Actions that are taken at the organization meetings of the board of directors include:

1. Ratification of the actions of the incorporators.
2. Designation of financial institution for holding capital and investments.
3. Appointment of officers.
4. Issuance of share certificates.
5. Acceptance of corporate governance policy.
6. Appointment of committees.
7. Acceptance of the form of stock certificate.
8. Adoption of a conflict of interest policy with parties signing it and disclosing any potential conflicts of interest.
9. Adoption of check writing policies.
10. Appointment of auditor or approval of fee if shareholders appoint.
11. Appointment of attorney.
12. Adoption of investment policy.
13. Appointment of captive manager.
14. Acceptance of the form of insurance policy.
15. Signing of any other service provider contracts.
16. Opening bank and investment accounts.
17. Reviewing and accepting reinsurance treatise.
18. Accepting corporate seal.
19. Accepting form of subscription agreement.
20. Adoption of a code of ethics and mission statement.

This meeting customarily takes place in the offices of the captive manager in the domiciliary state. There usually is a requirement that the meeting take place in that state as well as for subsequent shareholders and board of directors meeting. It is strongly recommended that the organizational and operational functions of the risk retention group be carried out under the oversight and tutelage of a qualified captive manager and your captive attorney. Granted it is not rocket science but a risk retention group is in reality an insurance company and insurance is only considered “simple” by those who are trained and nurtured in the field. To all others, it is rocket science.

Although the regulation of traditional captives by a state might be limited, regulation of risk retention groups tends to be a bit more stringent. The risk retention group will be subject to an organizational examination sometime during the first ninety days of its existence. In addition the risk retention group is subject to the same requirements of the domiciliary state

that apply to any captive including providing a copy of the annual statement certified by an independent public accountant and an annual actuarial opinion on the adequacy of loss reserves.

Risk retention groups are required to apply for an NAIC company number or code. The form is available at www.naic.org. A certified copy of the state license must be provided in order to obtain the company code. Subsequently, the risk retention group must also file annual and quarterly financial statements with the NAIC and are subject to accreditation standards. Risk retention groups must also file quarterly statements with the states where they are registered and with the domiciliary state. The National Association of Insurance Commissioners establishes the format for the annual and quarterly statements. For property and casualty companies, the annual statement has a yellow cover and is popularly known in the industry as the "Yellow Peril."

The owners of successful risk retention groups embrace the oversight by the domiciliary state. Attitude as in most endeavors is important in the operation of a risk retention group. Attention to detail and establishment of corporate governance standards will go a long way to ensure the success of a risk retention group. The federal preemption of separate state regulation is a valuable commodity. It will enable a group after it receives a license to have almost instant access to market and be free from the red tape of individual state regulation. It is a privilege that is best employed in a reasonable fashion with careful attention to the filing requirements, fee requirements and tax requirements of each state. This corporate good behavior is a small price to pay for the rights granted by the Liability Risk Retention Act.

Board of Directors and Audit Committee Check List

Corporate Governance Suggested Check List for Captives and Risk Retention Groups

The purpose of this check list is to provide some informal guidance for corporate governance for board of director members who serve on audit committees of captives and risk retention groups. Audit committees have been recommended for public companies since 1939 and pursuant to Sarbanes-Oxley since 2002, the operation and membership of audit committees of the board's of public companies is carefully governed as the exclusive overseer of the retention and performance of the external auditor. It is suggested that with

changes in corporate governance taking place in the regulation of risk retention groups and other discussions taking place amongst regulators concerning the independent status of captive managers who serve as board members of captives they manage, that perhaps an audit committee of the board of these non-public groups is a good idea and certainly would stand the group in good stead in the eyes of the regulators. There is talk that the NAIC will soon adopt a corporate governance model regulation that will have many of the same characteristics of SOX. With or without an audit committee, this check list I believe could be useful to the board of a captive or risk retention group. Many of the following suggestions are contained in the Corporate Director's "Guidebook" published by the American Bar Association and others are ones that I particularly like but that are not be found in other material.

The List

1. Select members of Audit Committee (carefully) – under SOX, each member must be independent and at least one member must be a financial expert. Look for members who are qualified; who possesses the qualities of personal integrity and reputation; who exercise common-sense business judgment, and, who are vigilant.
2. The Board and the Audit Committee should define their Core Values and communicate those Core Values. These values should include unquestionable ethics and integrity.
3. Adopt a formal written audit committee charter covering:
 - a. the scope of responsibilities
 - b. how the committee will carry out these responsibilities
 - c. the outside auditor's accountability to the audit committee
 - d. the audit committee's responsibility to insure the independence of the outside auditor
4. Select and retain the corporation's external auditor and determine for each fiscal year whether to continue or terminate that relationship.
5. Review and approve annually the external auditor's compensation and the proposed terms of engagement, including the scope and plan of the annual audit.

6. Approve, prior to each engagement, any further audit-related or non-audit services to be provided by the audit firm, based on the committee's judgment as to whether the firm is an appropriate choice to provide such services and whether the engagement, or the aggregate of such engagements, would interfere with the firm's independence. Publicly traded companies under SOX might be prohibited from approving any non-audit services to be performed by the outside auditor.
7. Establish procedures to receive and respond to complaints or concerns regarding the corporation's accounting, internal controls or auditing matters, including procedures for the confidential and anonymous submission by employees of any such complaints or concerns.
8. Serve as a channel of communication between the external auditor and the board and between the senior internal auditing executive, if any, and the board.
9. Discuss the corporation's procedures for issuing earnings reports to shareholders, regulators, rating agencies or the financial press.
10. Review the corporation's financial statements and management certifications with management and the external auditor and discuss with them the quality of management's accounting judgments in preparing the financial statements.
11. Review and act upon any communications received from the external auditor.
12. Consider, in consultation with the external auditor, the adequacy of the corporation's internal financial controls, which among other things, must be designed to provide reasonable assurance that the corporation's books and records are accurate, that its assets are safeguarded and that the reported financial statements prepared by management are accurate.
13. Meet periodically with management to review the corporation's major risk exposures and consider with management, risk management programs, including the reduction of present and future litigation risks, and procedures and policies addressing legal compliance.
14. Review annually, all fronting and reinsurance arrangements to assure that adequate coverage is being provided and that all contracts are in compliance and accurately reflect exposures and responsibilities i.e. no side agreements.
15. Approve any related party transactions between the corporations and its officers or directors, or their family members or enterprises they control.
16. Establish or review policies and guidelines for expense reimbursements, perquisites and other benefits provided to senior executives.
17. Do an annual self evaluation.

This Issue's Ethics and Corporate Governance Quote:

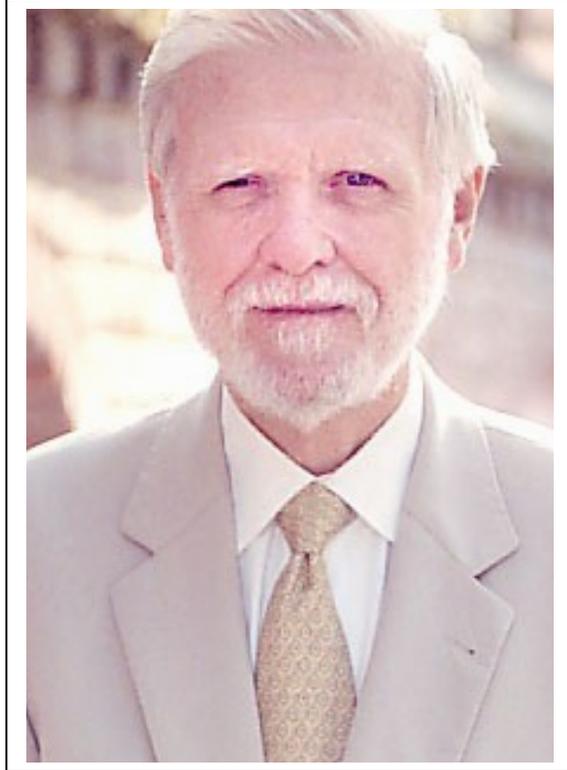
"I am only one. But still I am one I cannot do everything, But still I can do something
And because I cannot do everything I will not refuse to do something that I can do."

Edward Everett Hale

Hope you have found the information contained in this first newsletter of value.

Next Newsletter:

THE ROLE OF THE CAPTIVE MANAGER IN CORPORATE GOVERNANCE



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