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General concepts

A **corporation** is a legal personality, usually used to conduct business. Corporations exist as a product of corporate law, and their rules balance the interests of the shareholders that invest their capital and the employees who contribute their labor. People work together in corporations to produce. In modern times, corporations have become an increasingly dominant part of economic life. People rely on corporations for employment, for their goods and services, for the value of the pensions, for economic growth and social development.

The defining feature of a corporation is its legal independence from the people who create it. If a corporation fails, shareholders will lose their money, and employees will lose their jobs, but neither will be liable for debts that remain owing to the corporation's creditors. This rule is called limited liability. (Caveat: assessable mutual insurance corporations may assess their policyholders if assets do not cover liabilities.)
Despite not being persons, corporations are recognized by the law to have rights and responsibilities like actual people. Just as they are "born" into existence through its members obtaining a certificate of incorporation, they can "die" when they lose money into insolvency.

A **not-for-profit corporation** is an incorporated organization created by statute, that is not intended to provide a profit to the owners or members. It differs from a for-profit corporation substantially as this is organized to provide profits to its owners or members. A non-profit corporation is always organized as a non-stock corporation. (Caveat: mutual insurance corporations may issue dividends to their policyholders.)

The **Articles of Incorporation** are the primary rules governing the management of a corporation in the United States, and are filed with a state or other regulatory agency.

Articles of Incorporation vary widely from corporation to corporation, and from jurisdiction to jurisdiction, but generally do not go into great detail about a corporation's operations, which are spelled out in more detail in a company's bylaws.

A **bylaw** is a rule governing the internal management of an organization, such as a business corporation. Bylaws cannot countermand governmental law.

In a business situation, bylaws are drafted by a corporation's founders or directors under the authority of its Articles of Incorporation. Bylaws vary widely from organization to organization, but generally cover topics such as how directors are elected, how meetings of directors (and in the case of a business, shareholders) are conducted, and what officers the organization will have and a description of their duties.

A **board of directors** is a body of elected or appointed persons who jointly oversee the activities of a company or organization. The body sometimes has a different name, such as board of trustees, board of governors, board of managers, or executive board. It is often simply referred to as "the board."

In an organization with voting members, e.g. a professional society, the board acts on behalf of, and is subordinate to, the organization's full assembly, which usually chooses the members of the board. In a stock corporation, the board is elected by the stockholders and is the highest authority in the management of the corporation. In a nonstock corporation with no general voting membership, e.g. a university, the board is the supreme governing body of the institution. In a nonstock corporation with members, the members typically have voting rights on certain issues reserved to the members.

Typical duties of boards of directors include:

- Governing the organization by establishing broad policies and objectives
- Selecting, appointing, supporting and reviewing the performance of the chief executive
- Insuring the availability of adequate financial resources
- Approving annual budgets
- Accounting to the stakeholders for the organization's performance

The legal responsibilities of boards and board members vary with the nature of the organization, and with the jurisdiction within which it operates.

**Wisconsin law**

In general, Wisconsin’s statutes regarding non-stock corporations are consistent with the general concepts set forth above. Chapter 181 of the Wisconsin Statutes governs nonstock corporations in general. It contains the following definitions:

181.0103 (1) "Articles of incorporation" includes amended and restated articles of incorporation and articles of domestication.

181.0103 (2) "Board" means the group of persons vested with the management of the affairs of the corporation, irrespective of the name by which such group is designated.

181.0103 (3) "Bylaws" means the code of rules, other than the articles of incorporation, adopted under this chapter for the regulation or management of the affairs of a corporation, by whatever name designated.

181.0103 (5) "Corporation" or "domestic corporation" means, except as used in subs. (13) and (18), a nonstock corporation, including a nonprofit corporation, that is subject to the provisions of this chapter, except a foreign corporation.

181.0103 (9) "Director" means an individual, designated in the articles of incorporation or bylaws or elected by the incorporators, and the individuals' successors, and an individual elected or appointed by any other name or title to act as a member of the board.

181.0103 (15) "Member" means a person who has membership rights in a corporation in accordance with the provisions of its articles of incorporation or bylaws.

181.0103 (16) "Membership" means the rights and obligations that a member has under a corporation's articles of incorporation and bylaws and this chapter.
"Nonprofit corporation" means a corporation that does not make distributions, except as authorized under s. 181.1302 (1), (2) and (3).

"Nonstock corporation" means a corporation without capital stock.

Transit Mutual is a corporation. As such, it is subject to many of the provisions of Chapter 181. However, it is not subject to all of the provisions of that Chapter. And, it is subject to other statutory provisions that govern its formation and operation. Those provisions are unique to mutual insurance corporations and are set forth in Chapter 611 of the Wisconsin Statutes. In order to determine which portions of the law relating to nonstock corporations in general apply to Transit Mutual, it is necessary to look to Chapter 611.

Some of the primary differences between Transit Mutual as a mutual insurance corporation and nonstock corporations in general, include:

- The Commissioner of Insurance determines whether a certificate of incorporation will be issued. Sec. 611.13(3)
- The Commissioner of Insurance issues a certificate of authority that specifies any limits placed on the insurance business that may be carried on by the corporation and may specify limits on the corporation’s methods of operation. Sec. 611.20(2)(b)
- Policyholders have voting rights (as opposed to members in other nonstock corporations). The policyholders have the right to vote on conversion, voluntary dissolution, amendment of the articles of incorporation and election of directors. The articles of incorporation may give the policyholders additional voting rights. Sec. 611.42(2)
- Directors or officers may be removed by the Commissioner of Insurance if, after a hearing, the Commissioner finds that the director or officer "has a conflict of interest, is incompetent, untrustworthy" or has willfully violated insurance statutes, rules or orders and the conflict, incompetence, or violation "endangers the interests of insureds or the public." Sec. 611.54(3)

It is clear that the statutes provide for much more extensive regulation of mutual insurance corporations than other corporations. The Commissioner of Insurance has extensive authority regarding insurance corporations, which is not typical of general business corporations.

**Board of Directors**

Under Wisconsin law, the board of directors of a mutual insurance corporation is generally elected by the policyholders. Sec. 61153(2). Directors of a mutual insurance corporation "may be removed from office for cause by an affirmative vote of a majority of the full board at a meeting of the board called for that purpose." Sec. 611.53(3)
The board is given a broad grant of power:

>[A]ll corporate powers shall be exercised by or under the authority of, and the affairs of the corporation managed under the direction of, its board. Sec. 181.0801(2)

The board “shall manage the business and affairs of the [mutual insurance] corporation and may not delegate its power or responsibility to do so,” except to the extent authorized by statute. Sec. 611.51(6). One of the statutes allowing delegation of authority allows appointment of officers, including a president, a secretary, a treasurer “and such other offices as are appointed by the board.” Sec. 181.0840(1). The statutes also provide:

Each officer or agent has the authority and shall perform the duties set forth in the bylaws or, to the extent consistent with the bylaws, the duties and authority prescribed in a resolution of the board or by direction of an officer authorized by the board to prescribe the duties and authority of other officers. Sec. 181.0841

The board may also establish committees. If the articles of incorporation or bylaws allow, the board may designate one or more committees, each consisting of at least three directors. The designation must be made by resolution adopted by a majority of the full board. Committees serve at the pleasure of the board. Sec. 611.56(1). The statutes allow board committees to include one or more nonvoting members who are not directors; however, all voting members of committees must be directors. Sec. 611.56(1)

When the board is not in session, committees may exercise the powers of the board in management of the business and affairs of the corporation to the extent authorized in the resolution forming the committee or in the articles of incorporation or bylaws. Sec. 611.56(3). However, committees may not act in respect to the following:

(a) Compensation or indemnification of any person who is a director, principal officer or one of the 3 most highly paid employees, and any benefits or payments requiring shareholder or policyholder approval;

(b) Approval of any contract required to be approved by the board under s. 611.60 or 611.61, or of any other transaction in which a director has a material interest adverse to the corporation;

(c) Amendment of the articles or bylaws;

(d) Merger under s. 611.72 or 611.73, stock exchanges under s. 611.71, conversion under s. 611.75 or 611.76, voluntary dissolution under s. 611.74 or transfer of business or assets under s. 611.78;
(e) Any other decision requiring shareholder or policyholder approval;

(f) Amendment or repeal of any action previously taken by the full board which by its terms is not subject to amendment or repeal by a committee;

(g) Dividends or other distributions to shareholders or policyholders, other than in the routine implementation of policy determinations of the full board;

(h) Selection of principal officers; and

(i) Filling of vacancies on the board or any committee created under sub. (1) except that the articles or bylaws may provide for temporary appointments to fill vacancies on the board or any committee, the appointments to last no longer than the end of the next board meeting.

Fiduciary duty

Directors owe a fiduciary duty to the corporation. One definition of “fiduciary duty” states:

Directors owe duties of “care” and “loyalty” to the corporation and its shareholders. These duties require the board of directors to act in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner he or she reasonably believes to be in the best interest of the corporation and its shareholders. (*Fiduciary Duties of Directors*, by Kumi Yamamoto)

There are two statutes that provide some guidance on how a director may fulfill the duties owed to the corporation:

181.0850 Reliance by directors or officers. Unless the director or officer has knowledge that makes reliance unwarranted, a director or officer, in discharging his or her duties to the corporation, may rely on information, opinions, reports or statements, any of which may be written or oral, formal or informal, including financial statements and other financial data, if prepared or presented by any of the following:

(1) Officers and employees. An officer or employee of the corporation whom the director or officer believes in good faith to be reliable and competent in the matters presented.

(2) Professionals and experts. Legal counsel, certified public accountants licensed or certified under ch. 442, or other persons as to matters the director or
officer believes in good faith are within the person's professional or expert competence.

(3) Committees. In the case of reliance by a director, a committee of the board of directors of which the director is not a member, if the director believes in good faith that the committee merits confidence.

181.0853 Consideration of interests in addition to members' interests. In discharging his or her duties to the corporation and in determining what he or she believes to be in the best interests of the corporation, a director or officer may, in addition to considering the effects of any action on members, consider the following:

(1) Employees, suppliers and customers. The effects of the action on employees, suppliers and customers of the corporation.

(2) Communities. The effects of the action on communities in which the corporation operates.

(3) Other. Any other factors that the director or officer considers pertinent.

Conflict of interest

Wisconsin statutes demonstrate the relationship between duty to the corporation and conflict of interest. Directors are indemnified for damages arising from a breach, or failure to perform, any duty resulting solely from his/her status as a director (or officer) unless the breach or failure to perform constituted “a willful failure to deal fairly with the corporation or its members [policyholders] in connection with a matter in which the director or official has a material conflict of interest.” Sec. 181.0855(1). The statute deals with the concepts of the duty to deal fairly with the corporation and also conflict of interest.

The following are statutes that relate specifically to conflict of interest issues regarding insurance corporations:

611.57 Interlocking directorates and other relationships. No person may simultaneously be a director or officer in one insurance corporation and a director, officer, employee or agent for another insurer, if the effect is to lessen competition substantially or if the 2 insurers have materially adverse interests.

611.60 Transactions in which directors and others are interested.

(1) Voidable transactions. Any material transaction between an insurance corporation and one or more of its directors or officers, or between an insurance
corporation and any other person in which one or more of its directors or officers or any person controlling the corporation has a material interest, is voidable by the corporation unless:

(a) The transaction at the time it is entered into is reasonable and fair to the interests of the corporation; and

(b) The transaction has, with full knowledge of its terms and of the interests involved, been approved in advance by the board or by the shareholders; and

(c) The transaction has been reported to the commissioner immediately after such approval.

(2) Quorum and voting. Directors, whose interest or status make the transaction subject to this section, may be counted in determining a quorum for a board meeting approving a transaction under sub. (1) (b), but may not vote. Approval requires an affirmative vote of a majority of those present.

(3) Restricted transactions. The commissioner may by rule require that for any classes of transactions subject to sub. (1) which by their nature tend to be unreasonable or unfair to the interests of the corporation the report under sub. (1) (c) shall be submitted to the commissioner in advance of the proposed effective date. Such a transaction shall not be carried out even though approved under sub. (1) (b), until the commissioner approves the transaction, or does not disapprove it for failure to comply with sub. (1) (a) within 30 days after receiving the report under sub. (1) (c).

(4) Excepted transactions. This section does not apply to transactions subject to s. 611.61 [transactions with affiliates], nor to transactions made between an insurance corporation and its wholly owned subsidiary, nor to policies of insurance, other than reinsurance, issued in the normal course of business. Nothing in this section deprives any person of any rights accruing under a policy of insurance written at usual terms, other than reinsurance. The commissioner may by rule exempt other classes of transactions from the reporting requirement of sub. (1) (c), to the extent that the purposes of this section can be achieved without the report.
611.63 Executive compensation.

(5) Prohibited criteria. No arrangement for compensation or other employment benefits for any director, officer or employee with decision-making power may be made if it would:

(a) Measure the compensation or other benefits in whole or in part by any criteria that would create a financial inducement for him or her to act contrary to the best interests of the corporation; or

(b) Have a tendency to make the corporation depend for continuance or soundness of operation upon continuation in his or her position of any director, officer or employee.

Duty, conflict and Transit Mutual

How does a Transit Mutual director fulfill his/her duty to the corporation and avoid conflict of interest situations – when each director is employed by one of Transit Mutual’s policyholders and owes certain duties to his/her employer? In other words, how does a Transit Mutual director wear both hats?

There’s no single rule that fits all situations. Consider whether you can act in the best interest of Transit Mutual without breaching a duty owed to your employer. If in doubt, seek guidance from the Executive Committee, Board or Executive Director. If the answer is that you cannot act in the best interests of Transit Mutual without breaching a duty to your employer, abstaining and/or recusing yourself from the discussion would generally be appropriate.