

SUBSTITUTE FOR
HOUSE BILL NO. 5243

A bill to amend 1956 PA 218, entitled
"The insurance code of 1956,"
by amending sections 1001 and 1027 (MCL 500.1001 and 500.1027),
section 1001 as amended by 2016 PA 276 and section 1027 as added by
2008 PA 342, and by adding section 1028.

THE PEOPLE OF THE STATE OF MICHIGAN ENACT:

1 Sec. 1001. As used in this chapter:

2 (a) "Audited financial report" means the report required in
3 section 1005 and furnished ~~pursuant to~~ **under** section 1007.

4 (b) "Audit committee" means a committee or equivalent body
5 established by the board of directors of an entity to oversee the
6 accounting and financial reporting processes **of an insurer or group**
7 **of insurers, the internal audit function of an insurer or group of**



1 **insurers, if applicable, and the external** audits of the financial
2 statements of an insurer or group of insurers. The audit committee
3 of an entity that controls a group of insurers may be the audit
4 committee for 1 or more of these controlled insurers solely for the
5 purposes of compliance with this chapter at the election of the
6 controlling person as permitted in section ~~1027(6)~~. **1027(7)**. If an
7 audit committee is not designated by an insurer, the insurer's
8 entire board of directors will constitute the audit committee.

9 (c) "Group of insurers" means those licensed insurers included
10 in the reporting requirements of chapter 13, or a set of insurers
11 as identified by management, for the purpose of assessing the
12 effectiveness of internal control over financial reporting.

13 (d) "Indemnification agreement" means an agreement of
14 indemnity or a release from liability as to which the intent or
15 effect is to shift or limit in any manner the potential liability
16 of the person or firm for failure to adhere to applicable auditing
17 or professional standards, whether or not resulting in part from
18 knowing of other misrepresentations made by the insurer or its
19 representatives.

20 (e) "Independent board member" has the same meaning as
21 described in section ~~1027(4)~~. **1027(5)**.

22 (f) "Independent public accountant" means an independent
23 certified public accountant or accounting firm in good standing
24 with the American Institute of Certified Public Accountants and in
25 good standing in all states in which the accountant or accounting
26 firm is licensed to practice. For Canadian and British companies,
27 "independent public accountant" means a Canadian-chartered or
28 British-chartered accountant.

29 (g) "Insurer" means that term as defined in section 106 and

1 includes a nonprofit dental care corporation operating under 1963
2 PA 125, MCL 550.351 to 550.373.

3 **(h) "Internal audit function" means a person or persons that**
4 **provide independent, objective, and reasonable assurance designed**
5 **to add value and improve an organization's operations and**
6 **accomplish its objectives by bringing a systematic, disciplined**
7 **approach to evaluate and improve the effectiveness of risk**
8 **management, control, and governance processes.**

9 **(i) ~~(h)~~**"Internal control over financial reporting" means a
10 process effected by an entity's board of directors, management, and
11 other personnel designed to provide reasonable assurance regarding
12 the reliability of the financial statements filed with the
13 director, and includes the following:

14 **(i)** Policies and procedures pertaining to the maintenance of
15 records that, in reasonable detail, accurately and fairly reflect
16 the transactions and dispositions of assets.

17 **(ii)** Policies and procedures providing reasonable assurance
18 that transactions are recorded as necessary to permit preparation
19 of the financial statements filed with the director and that
20 receipts and expenditures are being made only in accordance with
21 authorizations of management and directors.

22 **(iii)** Policies and procedures providing reasonable assurance
23 regarding prevention or timely detection of unauthorized
24 acquisition, use, or disposition of assets that could have a
25 material effect on the financial statements filed with the
26 director.

27 **(j) ~~(i)~~**"SEC" means the United States Securities and Exchange
28 Commission.

29 **(k) ~~(j)~~**"Section 404" means section 404 of the Sarbanes-Oxley



1 act of 2002, 15 USC 7262, and the SEC's rules and regulations
2 promulgated under that section.

3 (l) ~~(k)~~—"Section 404 report" means management's report on
4 "internal control over financial reporting" as defined by the SEC
5 and the related attestation report of the independent certified
6 public accountant.

7 (m) ~~(l)~~—"SOX compliant entity" means an entity that either is
8 required to be compliant with, or voluntarily is compliant with,
9 all of the following provisions of the Sarbanes-Oxley act of 2002
10 and the regulations promulgated under that act:

11 (i) The preapproval requirements of section 201, section 10A(i)
12 of the securities exchange act of 1934, 15 USC 78j-1.

13 (ii) The audit committee independence requirements of section
14 301, section 10A(m) (3) of the securities exchange act of 1934, 15
15 USC 78j-1.

16 (iii) The internal control over financial reporting requirements
17 of section 404, 15 USC 7262, as prescribed by item 308 of SEC
18 regulation S-K, 17 CFR 229.308.

19 Sec. 1027. (1) This section applies to a domestic insurer that
20 is not a SOX compliant entity. A domestic insurer that is a direct
21 or indirect subsidiary of a SOX compliant entity is considered to
22 be a SOX compliant entity for purposes of this section.

23 (2) The audit committee ~~shall be~~ **is** directly responsible for
24 the appointment, compensation, and oversight of the work of any
25 accountant, including resolution of disagreements between
26 management and the accountant regarding financial reporting, for
27 the purpose of preparing or issuing the audited financial report or
28 related work ~~pursuant to~~ **under** this chapter. Each accountant shall
29 report directly to the audit committee.



1 (3) The audit committee of an insurer or group of insurers is
 2 responsible for overseeing the insurer's internal audit function
 3 and granting the person and persons performing the function
 4 suitable authority and resources to fulfill their responsibilities
 5 if required under section 1028.

6 (4) ~~(3)~~—Each member of the audit committee ~~shall~~**must** be a
 7 member of the board of directors of the insurer or a member of the
 8 board of directors of an entity elected ~~pursuant to~~**under**
 9 subsection ~~(6)~~**(7)**.

10 (5) ~~(4)~~—To be considered independent for purposes of this
 11 section, a member of the audit committee ~~shall~~**must** not, other than
 12 in his or her capacity as a member of the audit committee, the
 13 board of directors, or any other board committee, accept any
 14 consulting, advisory, or other compensatory fee from the entity
 15 audited or be an affiliated person of the entity or subsidiary
 16 audited, unless the individual serves on the board to meet another
 17 statutory requirement related to the composition of the board.
 18 However, ~~in no case can~~ the independent audit committee member **must**
 19 **not** be an officer or employee of the insurer or 1 of its
 20 affiliates.

21 (6) ~~(5)~~—If a member of the audit committee ceases to be
 22 independent for reasons outside the member's reasonable control,
 23 that person, with notice by the responsible entity to the state,
 24 may remain an audit committee member of the responsible entity
 25 until the earlier of the next annual meeting of the responsible
 26 entity or 1 year from the occurrence of the event that caused the
 27 member to be no longer independent.

28 (7) ~~(6)~~—To exercise the election of the controlling person to
 29 designate the audit committee for purposes of this section, the



1 ultimate controlling person shall provide written notice to the
2 ~~commissioner~~ **director**. Notification ~~shall~~ **must** be made timely
3 ~~prior to~~ **before** the issuance of the statutory audit report and
4 include a description of the basis for the election. The election
5 can be changed through notice to the ~~commissioner~~ **director** by the
6 insurer, which ~~shall~~ **must** include a description of the basis for
7 the change. The election ~~shall~~ **must** remain in effect until
8 rescinded.

9 **(8)** ~~(7)~~—The audit committee shall require the accountant that
10 performs for an insurer any audit required by this chapter to
11 timely report to the audit committee in accordance with the
12 requirements of SAS 61, communication with audit committees, or a
13 substantially similar replacement publication as required by the
14 ~~commissioner~~ **director**, including all of the following:

15 (a) All significant accounting policies and material permitted
16 practices.

17 (b) All material alternative treatments of financial
18 information within statutory accounting principles that have been
19 discussed with management officials of the insurer, ramifications
20 of the use of the alternative disclosures and treatments, and the
21 treatment preferred by the accountant.

22 (c) Other material written communications between the
23 accountant and the management of the insurer, such as any
24 management letter or schedule of unadjusted differences.

25 **(9)** ~~(8)~~—If an insurer is a member of an insurance holding
26 company system, the reports required by subsection ~~(7)~~ **(8)** may be
27 provided to the audit committee on an aggregate basis for insurers
28 in the holding company system, provided that any substantial
29 differences among insurers in the system are identified to the



1 audit committee.

2 (10) ~~(9)~~ All insurers are encouraged to structure their audit
 3 committees with at least a supermajority of independent committee
 4 members. An insurer with \$300,000,000.01 or less of direct written
 5 and assumed premiums in the prior calendar year is not required to
 6 have independent audit committee members. An insurer with over
 7 ~~\$300,000,000.00~~ **\$300,000,000.01** but **less than** \$500,000,000.00 ~~or~~
 8 ~~less~~ of direct written and assumed premiums in the prior calendar
 9 year ~~shall~~ **must** have 50% or more of its audit committee members be
 10 independent. An insurer with over \$500,000,000.00 of direct written
 11 and assumed premiums in the prior calendar year ~~shall~~ **must** have 75%
 12 or more of its audit committee members be independent. ~~As used in~~
 13 ~~this section, "direct written and assumed premiums" is the combined~~
 14 ~~total of direct premiums and assumed premiums from nonaffiliates~~
 15 ~~for the reporting entities.~~

16 (11) ~~(10)~~ The ~~commissioner~~ **director** may require an entity's
 17 board to enact improvements to the independence of the audit
 18 committee membership if the insurer is in a risk-based capital
 19 action level event, meets 1 or more of the standards listed in
 20 chapter 4 of an insurer considered to be in hazardous financial
 21 condition, or otherwise exhibits signs of a troubled insurer.

22 (12) ~~(11)~~ An insurer with direct written and assumed premium,
 23 excluding premiums reinsured with the ~~federal crop insurance~~
 24 ~~corporation~~ **Federal Crop Insurance Corporation** and ~~federal flood~~
 25 ~~program~~, **National Flood Insurance Program**, of less than
 26 \$500,000,000.00 may apply to the ~~commissioner~~ **director** for a waiver
 27 from this section based ~~upon~~ **on** hardship. The insurer shall file,
 28 with its annual statement filing, the approval for relief from this
 29 section granted by the commissioner with the states that it is



1 licensed in or doing business in and with the ~~national association~~
 2 ~~of insurance commissioners.~~ **National Association of Insurance**
 3 **Commissioners.** If the nondomestic state accepts electronic filing
 4 with the ~~national association of insurance commissioners,~~ **National**
 5 **Association of Insurance Commissioners,** the insurer shall file the
 6 approval in an electronic format acceptable to the ~~national~~
 7 ~~association of insurance commissioners.~~ **National Association of**
 8 **Insurance Commissioners.**

9 (13) ~~(12)~~ This section takes effect January 1, 2010. An
 10 insurer or group of insurers that is not required to have
 11 independent audit committee members or only 50% independent audit
 12 committee members because the total written and assumed premium is
 13 below the required threshold in subsection ~~(9)~~ **(10)** and
 14 subsequently becomes subject to 1 of the independence requirements
 15 due to changes in premium, whether through business combination or
 16 not, ~~shall have~~ **has** 1 year after the year the threshold is exceeded
 17 to comply with the independence requirements of subsection
 18 ~~(9)~~ **(10)**.

19 (14) As used in this section, "direct written and assumed
 20 premiums" is the combined total of direct premiums and assumed
 21 premiums from nonaffiliates for the reporting entities.

22 Sec. 1028. (1) An insurer is exempt from the requirements of
 23 this section if the insurer has annual direct written and
 24 unaffiliated assumed premium, including international direct and
 25 assumed premium but excluding premiums reinsured with the Federal
 26 Crop Insurance Corporation and National Flood Insurance Program
 27 less than \$500,000,000.00 and if the insurer is a member of a group
 28 of insurers that has annual direct written and unaffiliated assumed
 29 premium including international direct and assumed premium, but



1 excluding premiums reinsured with the Federal Crop Insurance
2 Corporation and National Flood Insurance Program less than
3 \$1,000,000,000.00.

4 (2) An insurer or group of insurers not exempt under
5 subsection (1) shall establish an internal audit function providing
6 independent, objective, and reasonable assurance to the audit
7 committee and management regarding the insurer's governance, risk
8 management, and internal controls. This assurance must be provided
9 by performing general and specific audits, reviews and tests, and
10 by employing other techniques considered necessary to protect
11 assets, evaluate control effectiveness and efficiency, and evaluate
12 compliance with policies and regulations.

13 (3) General and specific audits performed under this section
14 are not considered an insurance compliance self-evaluative audit
15 under section 221. Documents prepared or produced as a result of or
16 in connection with audits performed under this section must be
17 disclosed to the director on written request. Except as otherwise
18 provided in this subsection, the director shall withhold from
19 public inspection all information and documents submitted to the
20 department under this section and these items are confidential, are
21 not subject to subpoena, are not subject to disclosure under the
22 freedom of information act, 1976 PA 442, MCL 15.231 to 15.246, and
23 must not be divulged to any person. However, the director may
24 divulge the information and documents described in this subsection
25 to a relevant state or federal agency, or to the National
26 Association of Insurance Commissioners, if the director receives
27 assurances that the information and documents will be kept
28 confidential. The director shall not use the information and
29 documents submitted under this section to form the sole basis for



1 an examination under section 222.

2 (4) To ensure that internal auditors remain objective, the
3 internal audit function must be organizationally independent.
4 Specifically, the internal audit function must not defer ultimate
5 judgment on audit matters to others, and must appoint an individual
6 to head the internal audit function who will have direct and
7 unrestricted access to the board of directors. Organizational
8 independence does not preclude dual-reporting relationships.

9 (5) The head of internal audit function shall report to the
10 audit committee regularly, but no less than annually, on the
11 periodic audit plan, factors that may adversely impact the internal
12 audit function's independence or effectiveness, material findings
13 from completed audits, and the appropriateness of corrective
14 actions implemented by management as a result of audit findings.

15 (6) If an insurer is a member of an insurance holding company
16 system or included in a group of insurers, the insurer may satisfy
17 the internal audit function requirements set forth in this section
18 at the ultimate controlling parent level, an intermediate holding
19 company level, or the individual legal entity level.

20 (7) An insurer that meets the premium thresholds under this
21 section must have an internal audit function and must have the
22 function in place by no later than January 1, 2021. If an insurer
23 or group of insurers that is exempt no longer qualifies for the
24 exemption, it has 1 year after the year the threshold is exceeded
25 to comply with the requirement.

