Executive and Board Compensation Review Processes

Updated August, 2010



The Noridian Mutual Insurance Company (NMIC), d.b.a. Blue Cross Blue Shield of North Dakota (BCBSND) Board of Directors continuously reviews executive compensation levels and benefits, as well as the Board of Directors compensation levels, to ensure compensation is reasonable and fair.

Below is a summary of all actions by the Board of Directors since mid-2000.

Executive Compensation and PAR Timeline

Early to mid-2000s

Three organizations help NMIC design and develop PAR

Early to mid-2000s

- Board hires Hewitt Associates for annual evaluation of non-executive compensation levels against national and regional benchmarks in the health care industry.
- Board hires William H. Mercer Company for similar evaluation of executive compensation.
- Watson Wyatt Consulting was involved in developing PAR in the early 2000s and more recently provided an up-to-date analysis of NMIC's annual incentive levels.

2009

ND Department of Insurance conducts auditor's examination

Compensation, PAR, employee benefits and fringe benefits are cited as concerns.

NMIC responds with immediate changes and plans analysis

NMIC implements changes and promises to conduct further analyses in areas of concern.

NMIC seeks help from others to address executive compensation and PAR concerns NMIC relies on several sources to gauge how other entities approach executive compensation.

2009

- IRS Code section 4958 advises using an independent decision-making authority, combined with comparability data from industry surveys to ensure reasonable executive compensation levels.
 - Used in Vermont, Pennsylvania and Florida in response to insurance commissioners' inquiries.

NMIC conducts its own research on MN, ND executive compensation

Through IRS Form 990 filings, SEC filings and a survey of Agassiz Valley HR Association members, NMIC gathered data on executive pay in North Dakota and western Minnesota companies including Medica, Sanford and several other large health systems. Analysis confirms that NMIC's executive compensation is in line with like-size companies.

Executive Compensation and PAR Timeline Continued

2009 continued

NMIC engages consultant to review executive incentive program

In October 2009, the Board engaged Towers Watson (formerly Watson Wyatt) to help develop and implement a new program for executive incentive. Their analysis provides a formula to ensure future goals are set at appropriate levels and include targets that are meaningful to members and consider the financial stability of the company.

Towers Watson recommends NMIC:

- 1. Establish meaningful, member-focused measurement categories
- 2. Use historical data to set challenging goals
- 3. Apply threshold, target and maximum performance measures and corresponding probabilities for achievement
 - a. Threshold levels -80-90% chance of achievement
 - b. Target goals-50-60% chance of achievement
 - c. Maximum goals—10-15% chance of achievement, based on historical performance
- 4. The addition of another financial trigger to ensure the NMIC plan is stable before making PAR payments

Board freezes 2010 executive compensation at 2009 levels

NMIC reviews Board appointments

NMIC reviews its process to ensure it nominates and elects Member Directors in accordance with its bylaws and North Dakota law.

2010

Current year represents bridge between former practices and preparations for new framework

NMIC sets new goals within the Towers Watson framework

- 2010 Executive Incentive Plan goals presented to Board.
- Board approved goals on January 22; rolled out to all employees and executives on February 16, 2010.
- A five-year history for MTM, sales and external member services scores used to set goals within the new framework.
- 2011 goals will likely include a continuation of administrative efficiencies, combined with new member service measures and a cost trend goal.



Executive Compensation and PAR Timeline Continued



2010

2010 continued

NMIC prepares transition to Towers Watson framework

- A year to concentrate on establishing processes to complete transition
- In 2010, executives will be challenged to:
 - Establish benchmarks for the 2011 goals listed above
 - Create new measures in areas such as member satisfaction, where the current measures do not sufficiently measure a broader definition of satisfaction

2011

2011 goals will be set in the following areas:

- Operational efficiency/productivity improvements (e.g., administrative PMPM versus budget reflecting continuous improvement)
- Health care cost trend—a combination of cost (e.g., change in PMPM medical cost against an established inflation benchmark) and a measure of quality/access
- Customer Satisfaction—a comprehensive measure of customer and member satisfaction with the quality and value of NMIC services

2011 and beyond

NMIC continues to move benchmarks to North Dakota companies, gathers statistics on annual incentives among North Dakota competitors

The 2010 analysis serves as only the starting point for a robust process NMIC plans to develop and use from this point forward to ensure NMIC's positions are benchmarked against North Dakota companies.

Board of Directors Compensation and Elections

2005

2009

2010

2005

The compensation structure of the Board was evaluated to determine whether it fairly and reasonably compensates the directors for effective organizational oversight and pursuit of the organization's health care mission on behalf of constituents. Board compensation has remained frozen since 2005.

2009

Actions

- Completed extensive internal review of Board compensation levels
- Contracted with Mercer for an external review and recommendations that were presented August 2009
- Directed additional comparative research of North Dakota Board compensation to be incorporated into the McDermott survey
- Presented initial recommendations at the October 2009 Board of Directors meeting

2010

 Considered final recommendations at the April 23, 2010, Board of Directors meeting and voted to keep Board compensation frozen at 2005 levels. Specific information regarding the decision includes:

 The board compensation research concluded that Board compensation levels are below national board compensation levels and are the median of North Dakota company board compensation levels

Board of Directors Election Processes

In addition to nominations from the floor at the annual meeting, there are two ways to nominate candidates to run for those seats.*

Actions

- Names of candidates can be submitted to the Board's Governance and Nominating Committee. The
 committee will verify their qualifications, interview final candidates and place two successful candidate
 names for each seat on the ballot.
- A new option this year allows candidates to secure 250 signatures from voting BCBSND members.
 Once qualifications are verified and the candidate has been interviewed by the Board's Governance and Nominating Committee, the candidate will be placed on the ballot. This change is documented in Article III, Section 4 of the corporate bylaws.
- * The bylaws were changed to allow for nomination by petition as well as allowing opposing candidates to run against incumbents.



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Board of Directors Fact Sheet

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April 2010 —		8 Consumer Directors	cannot be providers of health care nor involved in health care or have financial interest in a health care provider
BSND's Board comprised of Directors	-	2 Provider Directors	must be physicians
	-	2 Provider Directors	must be hospital administrators
		1 Health Care Industry Directo	r must be a representative of the health care industry

BSND members elect directors

3SND's members vote for directors during the sember annual meeting. Eligible voters receive fication by mail at least 5 days before the ual member meeting. Notices also appear in local newspaper.

ibility requirements to vote:

lust be fully insured ith BCBSND group r individual ealth coverage

lust be a designated apresentative of a elf-funded plan. mployees within a elf-funded employer roup are not eligible a vote.

Four ways to vote:

- In person
- Online
- Mail hallot
- · Prox

no reviews the board?

3SND's Governance and Nominating Committee luates the performance of board members ually. The committee reviews the judgment, exity, age, skills, knowledge and experience orporate governance of each director.

ard candidates

ere are three ways individuals can be suggested as ential directors:

By members during BCBSND's call for potential candidates in May

By members attending BCBSND's annual meeting in December

By collecting 250 voting member signatures on an official BCBSND petition

Consumer Director eligibility guidelines

- Must have BCBSND health coverage
- · Cannot be a provider or an employee of a provider
- Cannot be a supplier of health care services

Directors commit to about 20 board and committee meeting days, and several telephonic meetings

Compensation

Board compensation is based on research conducted by the Blue Cross and Blue Shield Association (BCBSA) and the National Association of Corporate Directors. BCBSND compared director compensation amounts from local, regional and national like-sized health care companies.

Board downsized in 1998

The board was reduced from 21 members to 13 members.

Restructuring the BCBSND Board helped secure directors who were:

more qualified more experienced more committed more engaged in health care management

Did you know?

- Directors serve three-year terms
- Maximum service is four terms
- If completing a previous director's term, a director may serve up to 14 years

Election year 2010

Two Provider Directors and two Consumer Director positions will be elected in 2010. Of the two Provider Director positions, one current Provider Director is ineligible to serve another term.



NMIC aggressively reviewing every aspect of business

Beyond compensation, NMIC is committed to constant review of products and practices to offer the best health insurance value to members, as well as continuous review of administrative efficiencies.

Sherlock Company compares NMIC to other plans

In October 2009, NMIC commissioned the Sherlock Company to study 22 Blue plans and 16 independent/provider-sponsored (IPS) plans. Their findings include:

- 1. NMIC's per member per month (PMPM) administrative costs are \$9.66 lower than the Blue comparators and \$14.07 lower than the IPS firms.
- 2. When costs are expressed as premium and premium equivalents, NMIC's costs are also low.
- 3. In product comparison, in all but one product, NMIC's PMPM costs were lower than its peers.
- 4. NMIC's costs for the corporate executive/governance (executives not tied directly to a function plus Board of Director costs) were in line with Blue and IPS peer groups.
- 5. NMIC's premiums are lower than those of its peers in the Blue and IPS universe, regardless of product. (Comparisons data from fiscal year 2008.)

Praxis reveals NMIC economic impact

In a recent study, the Praxis Strategy Group estimated that NMIC brings nearly 2,000 jobs and \$110 million in earnings to the state's economy. As a large contributor to the state's economy, NMIC carefully balances its commitments to:

- Be an employer of choice in the state, providing good paying jobs in a positive work environment
- Provide our members good value in health insurance
- Remain a viable, independent health plan for the people of North Dakota

Conclusion

NMIC believes it has responded to all of the concerns from the targeted financial exam with:

- Necessary changes to both policy and philosophy
- Data to support a consistent compensation, PAR and fringe benefits framework
- Benefit changes including:
 - Increased employee contributions to health care premiums
 - Phaseout of retiree health contributions
 - Additional changes that bring benefits to median levels against North Dakota peers
 - Demonstration that executive compensation is in line with national, regional and now North Dakota benchmarks
 - Tougher PAR goals to ensure alignment with the needs of customers

This process is not complete, but NMIC is forging ahead. The management team is fully committed to these changes, to rebuilding trust and to restoring the reputation of this company as a low-cost, reputable provider of health insurance in North Dakota.