

RLI CORP
Form DEF 14A
March 26, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934 (Amendment No.)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

RLI CORP.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
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 - (2) Aggregate number of securities to which transaction applies:
 - (3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):
 - (4) Proposed maximum aggregate value of transaction:
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**RLI CORP.
9025 North Lindbergh Drive
Peoria, Illinois 61615**

March 26, 2004

Dear Shareholder:

Please consider this letter your personal invitation to attend the 2004 RLI Corp. Annual Shareholders Meeting. It will be held at 9025 North Lindbergh Drive, Peoria, Illinois, 61615, the Company's principal office, on May 6, 2004, at 2:00 P.M. CDT.

Business scheduled to be considered at the meeting includes the election of Class II directors and approval of the RLI Corp. Nonemployee Directors' Stock Plan. In addition, we will review significant events of 2003 and their impact on you and your Company. Directors, officers and representatives of KPMG LLP will be available before and after the meeting to talk with you and answer any questions you may have.

Your vote is important to us, no matter how many shares you own. Shareholders will have a choice of voting over the Internet, by telephone or by using a traditional proxy card. Check the proxy card forwarded by your bank, broker, other holder of record or our proxy administrators to see the options available to you. If you do attend the Annual Meeting and desire to vote in person, you may do so even though you have previously voted your proxy.

Thank you for your interest in your Company as well as your confidence and support in our future.

Sincerely,

Gerald D. Stephens, CPCU
Chairman of the Board

**RLI CORP.
9025 North Lindbergh Drive
Peoria, Illinois 61615**

Notice of Annual Meeting of Shareholders

May 6, 2004

To the Shareholders of RLI Corp.:

NOTICE IS HEREBY GIVEN that the Annual Meeting of the Shareholders of RLI Corp. (Company) will be held at 9025 North Lindbergh Drive, Peoria, Illinois, 61615, on Thursday, May 6, 2004, at 2:00 P.M. Central Daylight Time to:

1. Elect four (4) directors for a three-year term expiring in 2007 or until their successors are elected and qualified;
2. Consider and act upon a proposal to approve the RLI Corp. Nonemployee Directors Stock Plan; and
3. Transact such other business as may properly be brought before the meeting.

Only holders of Common Stock of the Company, of record at the close of business on March 8, 2004, are entitled to notice of and to vote at the Annual Meeting. This Proxy Statement and the enclosed Proxy are first being mailed or electronically delivered to shareholders entitled to notice of and to vote at the Annual Meeting on or about March 26, 2004.

By Order of the Board of Directors

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Camille J. Hensey
Vice President and Corporate Secretary

Peoria, Illinois
March 26, 2004

It is important, regardless of the number of shares you hold, that you personally be present or be represented by proxy at the Annual Meeting. Even if you expect to attend, it is important that you complete the enclosed proxy card, and sign, date and return it as promptly as possible in the envelope enclosed for that purpose. You may also vote your shares by telephone or on the Internet by following the instructions on your proxy card. You have the right to revoke your proxy at any time prior to its use by filing a written notice of revocation with the Corporate Secretary of the Company prior to the convening of the Annual Meeting, or by presenting another proxy card with a later date. If you attend the Annual Meeting and desire to vote in person, your proxy may be withdrawn upon request.

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RLI Corp.
9025 North Lindbergh Drive
Peoria, Illinois 61615

Proxy Statement

Annual Meeting of Shareholders
to be held
May 6, 2004

General Information

This Proxy Statement is furnished to the shareholders of RLI Corp. (Company) in connection with the solicitation, by the Board of Directors of the Company (Board or Board of Directors), of proxies to be used at the Annual Meeting of Shareholders to be held at 2:00 P.M. Central Daylight Time on Thursday, May 6, 2004, at 9025 North Lindbergh Drive, Peoria, Illinois, 61615, and at any adjournments of the Annual Meeting.

Proxy Solicitation. The Company will bear the cost of solicitation of proxies. In addition to the use of the mail, proxies may be solicited in person or by telephone, facsimile or other electronic means, by directors, officers or employees of the Company. No additional compensation will be paid to such persons for their services. In accordance with the regulations of the Securities and Exchange Commission (SEC) and the New York Stock Exchange (NYSE), the Company will reimburse banks, brokerage firms, investment advisors and other custodians, nominees, fiduciaries and service bureaus for their reasonable out-of-pocket expenses for forwarding soliciting material to beneficial owners of the Company s Common Stock and obtaining their proxies or voting instructions.

Voting. As many shareholders cannot attend the Annual Meeting in person, it is necessary that a large number be represented by proxy. Even if you expect to attend, it is important that you complete the enclosed proxy card, and sign, date and return it as promptly as possible in the envelope enclosed for that purpose. You may also vote your shares by telephone or on the Internet by following the instructions on your proxy card.

Each proxy will be voted in accordance with the shareholder s specifications. If there are no such specifications, it will be voted as recommended by the Board of Directors. All proxies delivered pursuant to this solicitation are revocable at any time at the option of the shareholder either by giving written notice to the Corporate Secretary at 9025 North Lindbergh Drive, Peoria, Illinois, 61615, or by timely delivery of a properly executed proxy, including an Internet or telephone vote, bearing a later date, or by voting in person at the Annual Meeting. All shares represented by valid, unrevoked proxies will be voted at the Annual Meeting.

Assuming the presence of a quorum, the election of directors requires the affirmative vote of a plurality of the votes cast by the holders of the outstanding shares of Common Stock. With respect to the election of directors, shareholders may vote in favor of all nominees, or withhold their votes as to all nominees,

or withhold their votes as to specific nominees. Brokers who hold shares for the accounts of their clients may vote such shares either as directed by their clients or at their own discretion if permitted by the NYSE or other organization of which they are members. Members of the NYSE are permitted to vote their clients' proxies at their own discretion as to the election of directors if the clients have not furnished voting instructions within 10 days of the meeting. If an executed proxy is returned by a broker holding shares in street name that indicates the broker does not have discretionary authority as to certain shares to vote on one or more matters (a "broker non-vote"), such shares will be considered present at the Annual Meeting for purposes of determining a quorum but will not be considered to be represented at the Annual Meeting for purposes of calculating the vote with respect to Proposal One. With respect to Proposal Two, broker non-votes will not be considered present at the Annual Meeting.

Mailing. This Proxy Statement and enclosed Proxy are first being mailed or electronically delivered to shareholders entitled to notice of and to vote at the Annual Meeting on or about March 26, 2004.

Voting Via Telephone or the Internet. Shareholders can save the Company expense by voting their shares over the telephone, toll-free from the United States or Canada, or by voting through the Internet. The voting procedures are designed to authenticate each shareholder by use of a control number, to allow shareholders to vote their shares, and to confirm that their instructions have been properly recorded. Specific instructions to be followed by any shareholder interested in voting by telephone or the Internet are set forth on the proxy card. The method of voting will not limit a shareholder's right to attend the Annual Meeting.

Electronic Access to Proxy Materials and Annual Report. This notice of Annual Meeting and Proxy Statement and the 2003 Annual Report are available on the Company's Internet site under Investors at www.rlicorp.com. Shareholders can elect to view future proxy statements and annual reports over the Internet instead of receiving paper copies in the mail. You can choose this option and save the Company the cost of producing and mailing these documents by following the instructions provided if you vote over the Internet or by telephone. Should you choose to view future proxy statements and annual reports over the Internet, you will receive an e-mail next year with voting instructions and the Internet address of those materials.

Shareholder Proposals. To be included in the Board of Directors' Proxy Statement for the 2005 Annual Meeting of Shareholders, a shareholder proposal must be received by the Company on or before November 26, 2004. Proposals should be

directed to the attention of the Corporate Secretary at 9025 North Lindbergh Drive, Peoria, Illinois, 61615. If a shareholder raises a matter at the 2005 Annual Meeting of Shareholders, the Company may exercise discretionary authority (vote the shares in the discretion of the persons appointed in the Proxy Card) unless the shareholder notifies the Company of the matter before February 10, 2005.

Shareholders Entitled to Vote. At the close of business on March 8, 2004, the record date for the determination of shareholders entitled to vote at the Annual Meeting, the Company had 25,182,820 shares of Common Stock outstanding and entitled to vote. Common share ownership entitles the holder to one vote per share upon each matter to be voted at the Annual Meeting.

Share Ownership of Certain Beneficial Owners

Principal Shareholders. The only persons or entities known to the Company who beneficially own more than five percent of the Company's Common Stock as of December 31, 2003, are as follows:

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class %
Franklin Resources, Inc. 777 Mariners Island Boulevard 6 th Floor San Mateo, California 94404(1)	1,574,287	6.3%
Gerald D. Stephens 493 East High Point Drive Peoria, Illinois 61614(2)	1,601,276	6.3%
State Street Bank and Trust Company 225 Franklin Street Boston, Massachusetts 02110(3)	2,503,447	9.9%

(1) The information shown is based solely on a Schedule 13G dated February 12, 2004, filed by Franklin Resources, Inc., (Franklin), Charles B. Johnson, Rupert H. Johnson, Jr., and Franklin Advisory Services, LLC, which filing indicates that one or more open- or closed-end investment companies or other managed accounts that are advised by direct and indirect investment advisory subsidiaries of Franklin have sole voting and sole dispositive power with respect to 1,567,236 shares. Messrs. Johnson and Johnson are the principal shareholders of Franklin.

(2) Includes 23 shares allocated to Mr. Stephens under the ESOP (as defined below), over which Mr. Stephens has sole voting power and no investment power; 112,196 shares allocated to Mr. Stephens under the RLI Corp. Key Employee Excess Benefit Plan (Key Plan), over which Mr. Stephens has no voting or investment power; 32,183 shares held in custodian accounts for the benefit of Mr. Stephens grandchildren, over which Mr. Stephens has sole voting and investment power; 3,658 shares in the H. O. Stephens Trust for the benefit of Mr. Stephens mother, over which Mr. Stephens, as trustee, has sole voting and investment power; 38,212 shares owned by the Gerald D. and Helen M. Stephens Foundation, over which Mr. Stephens, as President, has sole voting and investment power; 371,992 exercisable stock options; and 10,387 shares held by a bank, as trustee, under an irrevocable trust established by the Company pursuant to the RLI Corp. Executive Deferred Compensation Agreement (Deferred Agreement). Excludes 70,356 shares owned by Mr. Stephens spouse, over which Mr. Stephens has no voting or investment power, as to which Mr. Stephens disclaims beneficial ownership.

(3) The information shown is based solely on a Schedule 13G dated February 6, 2004, filed by State Street Bank and Trust Company (State Street), which filing indicates, as of December 31, 2003, State Street, as trustee, held 2,184,088 shares on behalf of participants in the Company s Employee Stock Ownership Plan (ESOP). State Street further disclosed sole voting power with respect to 293,771 shares, shared voting power with respect to 2,184,088 shares, sole dispositive power with respect to 318,359 shares and shared dispositive power with respect to 2,185,088 shares. Each ESOP participant or beneficiary may direct State Street as to the manner in which the shares allocated to each participant under the ESOP are to be voted. State Street has sole voting power with respect to all unallocated shares and sole investment power as to all allocated and unallocated shares, except as to those shares that are the subject of a participant s diversification election. With respect to allocated shares for which no votes are received, State Street will vote such shares in proportion to the votes cast on behalf of allocated shares for which votes are received.

Directors and Officers. The following information is furnished as to the beneficial ownership of the shares of the Company s Common Stock by each current director, nominee for director and named executive officer, and the directors and executive officers of the Company as a group, as of December 31, 2003:

Name of Individual or Number of Persons in Group	Amount and Nature of Beneficial Ownership (1)	Percent of Class
John T. Baily(2)(3)	1,309	*
Richard H. Blum(2)(11)	12,430	*
Joseph E. Dondanville(4)(10)(12)(13)	143,492	*
Camille J. Hensey(10)(12)(13)	45,914	*
William R. Keane(5)(11)	83,570	*
Gerald I. Lenrow(2)(6)(11)	50,758	*
Charles M. Linke(2)	2,073	*
F. Lynn McPheeters(2)(11)	14,419	*
Jonathan E. Michael(7)(10)(12)(13)	337,117	1.3%
Mary Beth Nebel(8)(10)(12)(13)	53,579	*
Edwin S. Overman(2)(11)	85,655	*
Gerald D. Stephens(9)(10)(12)(13)	1,601,276	6.3%
Michael J. Stone(10)(12)(13)	148,306	*
Edward F. Sutkowski(2)(11)	253,181	1.0%
Robert O. Viets(2)(11)(14)	65,072	*
Directors and executive officers as a group (16 persons)(10)(12)(13)	2,899,059	11.1%

*Less than 1% of Class.

(1) Unless otherwise noted, each person has sole voting power and sole investment power with respect to the shares reported.

(2) Includes shares held by a bank trustee under an irrevocable trust established by the Company pursuant to the RLI Corp. Director Deferred Compensation Plan (Deferred Plan) for the benefit of the following: Mr. Baily 309 shares; Mr. Blum

4,166 shares; Mr. Lenrow 32,753 shares; Mr. Linke 573 shares; Mr. McPheeters 5,337 shares; Dr. Overman 66,755 shares; Mr. Sutkowski 69,671 shares; and Mr. Viets 27,161 shares. Each participating director has no voting or investment power with respect to such shares and disclaims beneficial ownership of such shares for purposes of Section 13(d) of the Securities Exchange Act of 1934.

- (3) Includes 1,000 shares held by Mr. Baily's spouse as to which Mr. Baily claims beneficial interest.

- (4) Includes 600 shares held by Mr. Dondanville's spouse in a custodian account for the benefit of their children, as to which Mr. Dondanville disclaims any beneficial interest.

- (5) Includes 28,486 shares owned by Mr. Keane as trustee under the Evelyn C. Keane Revocable Trust Agreement, as to which Mr. Keane claims beneficial interest.

- (6) Includes 905 shares held by Mr. Lenrow's spouse in a custodian account for the benefit of their minor daughter, as to which Mr. Lenrow disclaims any beneficial interest.

- (7) Includes 29,870 shares allocated under the Key Plan, over which Mr. Michael has no voting or investment power.

- (8) Includes 1,240 shares held by Ms. Nebel in a custodian account for the benefit of her minor son, as to which Ms. Nebel claims beneficial interest.

- (9) Includes 112,196 shares allocated to Mr. Stephens under the Key Plan, over which Mr. Stephens has no voting or investment power; 32,183 shares held in custodian accounts for the benefit of Mr. Stephens grandchildren, over which Mr. Stephens has sole voting and investment power; 3,658 shares in the H. O. Stephens Trust for the benefit of Mr. Stephens' mother, over which Mr. Stephens, as trustee, has sole voting and investment power; and 38,212 shares owned by the Gerald D. and Helen M. Stephens Foundation, over which Mr. Stephens, as President, has sole voting and investment power. Excludes 70,356 shares owned by Mr. Stephens' spouse, over which Mr. Stephens has no voting or investment power, as to which Mr. Stephens disclaims beneficial interest.

- (10) Includes shares allocated to the named persons under the ESOP with respect to which such persons have sole voting power and no investment power, except when any such person may diversify up to a percentage, not to exceed 50%, of such person's ESOP benefit. As of December 31, 2003, the following shares were allocated under the ESOP:

Mr. Dondanville 45,491 shares; Ms. Hensey 13,579 shares; Mr. Michael 75,521 shares; Ms. Nebel 25,427 shares; Mr. Stephens 23 shares; and Mr. Stone 10,233 shares.

(11) Includes shares that may be acquired by the named persons within 60 days of December 31, 2003, under the Directors Stock Option Plan for Outside Directors (Director Plan), upon the exercise of outstanding stock options as follows: Mr. Blum 8,264 shares; Mr. Keane 18,900 shares; Mr. Lenrow 17,100 shares; Mr. McPheeters 9,082 shares; Dr. Overman 18,900 shares; Mr. Sutkowski 15,150 shares; and Mr. Viets 18,900 shares.

(12) Includes shares that may be acquired by the named persons within 60 days of December 31, 2003, under the Incentive Stock Option Plan (ISOP), upon the exercise of outstanding stock options as follows: Mr. Dondanville 78,002 shares; Ms. Hensey 16,991 shares; Mr. Michael 194,430 shares; Ms. Nebel 20,695; Mr. Stephens 371,992 shares; and Mr. Stone 114,850 shares.

(13) Includes shares allocated to the named persons which shares are held by a bank trustee under an irrevocable trust established by the Company pursuant to the Deferred Agreement for the benefit of the following: Mr. Dondanville 7,295 shares; Ms. Hensey 430 shares; Mr. Michael 13,358 shares; Ms. Nebel 3,593 shares; Mr. Stephens 10,387 shares; and Mr. Stone 15,153 shares. Each participant has no voting or investment power with respect to such shares and disclaims beneficial ownership of such shares for purposes of Section 13(d) of the Securities Exchange Act of 1934.

(14) Includes 13,400 shares held by Mr. Viets spouse as trustee of the Robert O. Viets Florida Intangible Trust, as to which Mr. Viets claims beneficial interest.

The information with respect to beneficial ownership of Common Stock of the Company is based on information furnished to the Company by each individual included in the table.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended (1934 Act), requires the Company s directors, executive officers and beneficial owners of more than 10% of the Common Stock of the Company to file with the SEC certain reports regarding their ownership of Common Stock or any changes in such ownership. In addition, officers, directors and greater than 10% shareholders are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms that they file.

Based solely on its review of the copies of such reports received by it, and/or written representations from certain reporting persons that no Form 5s were required for such persons, the Company believes that, during the year ended December 31, 2003, and except as set forth below, the reporting persons have complied with all filing requirements of Section 16(a) of the 1934 Act. There was a late filing of one Form 4 on behalf of Ms. Mary Beth Nebel, an executive officer of the Company, reporting one transaction. This was an inadvertent omission, and the Form 4 was promptly filed upon discovery of the oversight.

**Proposal One:
Election of Directors**

Nominees. At the Annual Meeting, four (4) directors are to be elected, each to hold office for a three-year term or until a successor is elected and qualified. Messrs. Richard H. Blum, F. Lynn McPheeters, Gerald D. Stephens, and Robert O. Viets are Class II directors who were elected by the shareholders in 2001 for three-year terms expiring in 2004.

Voting of Proxies. Unless otherwise instructed, the shares represented by a proxy will be voted for the election of the four nominees named above. The affirmative vote of a plurality of the shares present in person or represented by proxy at the Annual Meeting and entitled to vote is required for the election of directors. Votes will be tabulated by an Inspector of Election appointed at the Annual Meeting. Shares may be voted for, or withheld from, each nominee. Shares that are withheld and broker non-votes have no effect on determinations of plurality except to the extent that they affect the total votes received by any particular nominee. There is no cumulative voting for the directors under the Company's Articles of Incorporation.

Substitute Nominees. The Board of Directors has no reason to believe that any nominee will be unable to serve if elected. In the event that any nominee shall become unavailable for election, the shares represented by a proxy will be voted for the election of a substitute nominee selected by the persons appointed as proxies unless the Board of Directors should determine to reduce the number of directors pursuant to the Company's By-Laws.

Director and Nominee Information. The following includes certain information with respect to the current directors and nominees to the Board of Directors furnished to the Company by such individuals:

NAME	AGE	DIRECTOR SINCE	PRINCIPAL OCCUPATION
Richard H. Blum (term expiring in 2004) PICTURE	65	2000	Chairman of AXIS Specialty U.S.Holdings, Inc., Holdings, Inc., having joined them on February 1, 2002. Was Senior Advisor to Marsh & McLennan Companies, Inc., (MMC) a professional services firm in risk and insurance services, investment management and consulting businesses from 1999 to January 31, 2002. Former director of MMC from 1986 to 1999 and served as Vice Chairman of J&H Marsh & McLennan from 1997 to 1999, and previously as Chairman and CEO of Guy Carpenter & Company, Inc., having joined that firm in 1958.
F. Lynn McPheeters (term expiring in 2004) PICTURE	61	2000	Vice President and Chief Financial Officer of Caterpillar Inc., manufacturer of construction, mining and related equipment. Mr. McPheeters joined Caterpillar Inc. in 1964 and held various finance positions until his promotion to Vice President and CFO in 1998.
Gerald D. Stephens (term expiring in 2004) PICTURE	71	1965	Elected Chairman of the Board of the Company January 1, 2001. Mr. Stephens founded the Company in 1965 and served as Chief Executive Officer until his election as Chairman of the Board.
Robert O. Viets (term expiring in 2004) PICTURE	60	1993	Since 1999, President of ROV Consultants, LLC. Former President, CEO and Director from 1988 until 1999 of CILCORP Inc., a holding company in Peoria, Illinois, whose principal subsidiary was Central Illinois Light Company.

Certain information concerning the remaining directors, whose terms expire either in 2005 or 2006, is set forth as follows based upon information furnished to the Company by such individuals:

John T. Baily(1) (term expiring in 2005) PICTURE	60	2003	Appointed to the Board on August 28, 2003. Was National Insurance Industry Chairman and Board Member of the international accounting firm of Coopers & Lybrand LLP (now PricewaterhouseCoopers LLP) retiring in 1999 after 23 years as a partner. Served as President of Swiss Re Capital Partners from 1999 through 2002.
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William R. Keane (term expiring in 2005) PICTURE	87	1966	Former Vice President, Contacts, Inc. (contact lens dispenser) in Chicago, Illinois, until his retirement in 1983.
Gerald I. Lenrow (term expiring in 2005) PICTURE	76	1993	Since 1999, in private law practice providing consultation services to certain members of the insurance industry. Consultant to General Reinsurance Corp. until December 31, 1998. Former partner in the international accounting firm of Coopers & Lybrand LLP until 1990, following which he served as its consultant until 1996.
Charles M. Linke (term expiring in 2006) PICTURE	66	2003	Professor Emeritus of Finance at the University of Illinois (Urbana-Champaign) since 1998. Professor Linke has held various positions with the University of Illinois since 1966. CEO of Economics Et Cetera, Inc. (formerly Linke & Associates, Inc.), a consulting firm specializing in financial economics since 1981.
Jonathan E. Michael (term expiring in 2006) PICTURE	50	1997	President & Chief Executive Officer of the Company since 2001. Elected Chairman of the Board & Chief Executive Officer of the Company's principal insurance subsidiaries January 1, 2002. Mr. Michael joined the Company in 1982, and held various managerial and executive officer positions until his promotion to President & Chief Executive Officer.
Edwin S. Overman (term expiring in 2005) PICTURE	81	1987	President Emeritus of the Insurance Institute of America and the American Institute for Chartered Property/Casualty Underwriters, national educational organizations in Malvern, Pennsylvania, since his retirement as President, CEO of the Institutes in 1987.

Edward F. Sutkowski (term expiring in 2006) PICTURE	65	1975	Since 1965, President of the law firm of Sutkowski & Rhoads Ltd., a regional firm specializing in tax, fiduciary litigation, pension and ERISA law.
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(1) Mr. Baily serves as a Director of Endurance Specialty Holdings, Ltd., Erie Indemnity Company and its subsidiary, Erie Family Life Insurance Company, and NYMAGIC, Inc., all publicly traded companies.

Proposal Two:

Approval of the RLI Corp. Nonemployee Directors Stock Plan

Time commitments for service as a director of public companies have increased in recent years. These increasing demands on directors' time have greatly increased the competition for potential directors who possess the talents, skills, judgment, personal attributes and other characteristics of an outstanding director. This competition is especially keen for independent directors who are not associated with a company that requests their services as a director.

The Board of Directors has adopted the RLI Corp. Nonemployee Directors Stock Plan (Stock Plan) to provide compensation to each director of the Company who is not an employee of the Company or its subsidiaries, in the form of a stock grant at the time of such director's election or appointment to the Board of Directors, and future stock grants based on continued service as a director. The Board of Directors believes that the Stock Plan will enhance the Company's ability to attract and retain well-qualified individuals, enhance the long-term commitment of nonemployee directors to the Company, and further align their interests with the interests of the shareholders.

Summary of the Stock Plan

The following is a summary of the Stock Plan adopted by the Board of Directors on March 8, 2004, subject to shareholder approval of the Stock Plan. This summary is qualified in its entirety by reference to the complete Stock Plan attached as Exhibit A. Effective May 7, 2004, no future options will be granted under the Director Plan, if the Stock Plan is approved by the Shareholders.

Purpose. The Stock Plan is intended to advance the interests of the Company and its shareholders by attracting, retaining, compensating and motivating the performance of nonemployee directors of the Company and to encourage and enable nonemployee directors to acquire and retain a proprietary interest in the Company by ownership of its stock.

Eligibility. Only the Company's nonemployee directors are eligible to participate in the Stock Plan. Nine nonemployee directors currently serve on the Board (all directors except Messrs. Stephens and Michael).

Administration. The Stock Plan is administered by the Nominating/Corporate Governance Committee (Committee) comprised of directors Messrs. Baily, Blum, McPheeters and Sutkowski.

Shares Subject to the Stock Plan. Subject to shareholder approval of the Stock Plan, an aggregate of 200,000 shares of Common Stock of the Company will be reserved for directors' stock grants, subject to adjustments for such matters as stock splits and stock dividends. Shares of Common Stock issued and sold under the Stock Plan may be either authorized but unissued shares or shares held in the Company's treasury, which includes shares repurchased in the open market.

Stock Grants. From time to time, the Committee will recommend for approval by the Board the dollar amount of the fee to be paid under the Stock Plan to each new nonemployee director who joins the Board (New Director Fee). Currently, the New Director Fee is \$30,000. Commencing with the 2004 Annual Meeting, each new nonemployee director who joins the Board will receive a stock grant having a fair market value equal to the New Director Fee, such that the number of shares of Common Stock subject to the stock grant will be equal to the number determined by dividing the New Director Fee by the fair market value of a share of Common Stock on the date of grant. The stock grant will be made as of the date of the nonemployee director's election to the Board.

The Committee will recommend for approval by the Board the dollar amount of the fee to be paid under the Stock Plan to each nonemployee director for service during each fiscal year (Annual Fee). Currently the Annual Fee is \$30,000. For each fiscal quarter ending during the fiscal year, the Company will issue to each nonemployee director a stock grant having a fair market value equal to one-fourth of the Annual Fee (Quarterly Fee), such that the number of shares of Common Stock subject to such stock grant will be equal to the number determined by dividing the Quarterly Fee by the fair market value of a share of Common Stock on the date of grant. Stock grants issued as payment of the Quarterly Fee will be made on the tenth calendar day prior to the end of each fiscal quarter, provided that if such grant date falls on a weekend or a holiday, the grant date will be the immediately preceding business day. If a nonemployee director is elected or terminated (other than removal for cause) during the fiscal quarter, the nonemployee director will receive a stock grant equal to the Quarterly Fee times a fraction, the numerator of which is the number of days during such quarter that the

nonemployee director serves as a director and the denominator of which is 90.

The Annual Fee for the 2004 fiscal year, as recommended by the Committee and approved by the Board, will be made in two grants, each of which will be one-half of the Annual Fee, on the issuance dates (as determined above) for the quarters ending September 30, 2004 and December 31, 2004.

Fair market value means the average of the highest and lowest sale prices of a share of Common Stock on the NYSE on the date as of which fair market value is to be determined.

In addition to the automatic grants provided for above, the Committee may recommend for Board approval discretionary stock grants to any nonemployee director. The Committee will select the nonemployee directors who will receive any discretionary stock grants and determine the number of shares subject to any such stock grant.

Each stock grant will be issued in the name of each nonemployee director. Upon the issuance of a stock grant, the nonemployee director will be entitled to vote the shares of Common Stock and to receive any dividends paid thereon.

Effective Date, Termination and Amendment. The Stock Plan will become effective on the date of its approval by the shareholders of the Company. The Stock Plan will terminate on the date of the Annual Meeting in 2014, provided that the Board may at any time terminate the Stock Plan earlier. Notwithstanding the foregoing, no termination of the Stock Plan will in any manner affect any previously issued stock grant without the consent of the nonemployee director who received the stock grant. The Board may at any time and from time to time and in any respect, amend or modify the Stock Plan; provided, however, that shareholder approval will be required to the extent necessary to comply with the rules of the NYSE. No amendment or modification of the Stock Plan will in any manner affect any previously issued stock grant without the consent of the nonemployee director who received the stock grant.

Shareholder Vote

The listing requirements of the NYSE require that the shareholders of the Company approve the Stock Plan. The affirmative vote of the holders of at least a majority of the shares of Common Stock of the Company present and entitled to vote at the Annual Meeting is required for adoption of this proposal. With respect to the approval of the Stock Plan, broker non-votes will not be considered present at the Annual Meeting.

The Board of Directors recommends the shareholders vote For the proposed RLI Corp. Nonemployee Directors Stock Plan.

Corporate Governance and Board Matters

Corporate Governance Principles. The Company is committed to having sound corporate governance principles that are designed to ensure that the Board exercises reasonable business judgment in discharging its obligations to the Company and its shareholders. Corporate governance practices also help to ensure that full and transparent disclosures are made to the Company's shareholders and the SEC.

The Company's published Corporate Governance Guidelines, which are publicly available on the Company's Internet site under Investors at www.rlicorp.com, outline the directors' responsibilities, which include attendance at shareholder, Board and committee meetings. Each member of the Board attended the 2003 Annual Meeting of Shareholders and was available to respond to appropriate questions from the shareholders.

The Board is required under the NYSE rules to affirmatively determine the independence of each independent director and to disclose such determination in the proxy statement for each Annual Meeting of Shareholders of the Company. The Board has established guidelines to assist it in making this determination, which incorporate all of the NYSE independence standards. Only independent directors serve on the Company's Audit Committee, Executive Resources Committee and Nominating/Corporate Governance Committee.

The Company has developed an orientation process that encourages new directors to attend a director seminar in their first year as a director. Each year, certain of the incumbent directors are requested to attend an accredited director seminar selected by the Company.

Director Independence Standards. It is the policy of the Board of Directors of the Company that a majority of its members be independent. To be considered independent under the NYSE Listing Standards, the Board must affirmatively determine that a director or director nominee (collectively referred to as "director") has no material relationship with the Company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the Company). The Board examines the independence of each of its members once per year, and again if a member's outside affiliations change substantially

during the year. With the exception of the Chairman of the Board and the President & CEO, the Board has affirmatively determined that each director is independent within the meaning of the NYSE Listing Standards and the Company's Director Independence Standards.

The Board has established the following categorical standards to assist it in determining director independence:

- (a) A director will not be independent if, within the preceding three years:
- (i) the director was an employee, or an immediate family member of the director was an executive officer, of the Company;
 - (ii) the director received, or an immediate family member of the director received, more than \$100,000 per year in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service);
 - (iii) the director was affiliated with or employed by, or an immediate family member of the director was affiliated with or employed in a professional capacity by, the Company's present or former internal or external auditor;
 - (iv) the director was employed, or an immediate family member of the director was employed, as an executive officer of another company where any of the Company's present executive officers serve on that company's compensation committee; or
 - (v) the director was an executive officer or an employee, or an immediate family member of the director was an executive officer, of a company that makes payments to, or receives payments from, the Company for property or services in an amount which, in any single fiscal year, exceeded the greater of \$1 million, or 2% of such other company's consolidated gross revenues.
- (b) The following commercial and charitable relationships will not be considered to be material relationships that would impair a director's independence: (i) if a director, or an immediate family member of the director, is an executive officer, director, employee or holder of an equity interest of a company that makes payments to, or receives payments from, the Company for property or services in an amount which, in the last fiscal year, do not exceed the greater of \$1 million, or 2% of such other

company's consolidated gross revenues; (ii) if a director, or an immediate family member of the director, is an executive officer, director, employee or holder of an equity interest of a company that is indebted to the Company, or to which the Company is indebted, and the total amount of either company's indebtedness to the other does not exceed the greater of \$1 million, or 2% of such other company's total consolidated assets; (iii) if a director, or an immediate family member of the director, is an executive officer, director, employee or holder of an equity interest of a company in which the Company owns an equity interest, and the amount of the Company's equity interest in such other company does not exceed the greater of \$1 million, or 2% of such other company's total shareholders equity; (iv) if a director, or an immediate family member of the director, is an executive officer, director, employee or holder of an equity interest of a company that owns an equity interest in the Company; and (v) if a director, or an immediate family member of the director, serves as an officer, director or trustee of a charitable organization, and the charitable contributions from the Company to such charitable organization in the last fiscal year do not exceed the greater of \$1 million or 2% of such charitable organization's consolidated gross revenues. (The Company's automatic matching of employee charitable contributions will not be included in the amount of the Company's contributions for this purpose.)

(c) For relationships not covered by the standards in subsection (b) above, the determination of whether the relationship is material or not, and therefore whether the director would be independent or not, shall be made by the directors who satisfy the independence standards set forth in subsections (a) and (b) above. The Company is required to explain in its proxy statement the basis for any Board determination that a relationship was immaterial, despite the fact that it did not meet the categorical standards of immateriality set forth in subsection (b) above.

Board Independence Status

Director	Independent	Non-Management	Management
John T. Baily	X		
Richard H. Blum	X		