

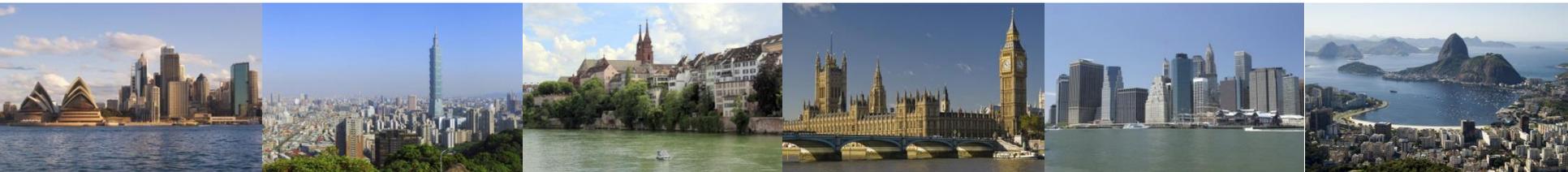


# IAIS

INTERNATIONAL ASSOCIATION OF  
INSURANCE SUPERVISORS

# ICP 7 Corporate Governance

Yoshi Kawai, Secretary General  
ASSAL, April 2015



# Corporate Governance

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Refers to systems (such as strategies, policies, processes and controls) through which an entity is managed and controlled

# Why is Governance important?

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*General Motors*

HBOS

HP

**LIBOR**

**ENRON**

BCCI

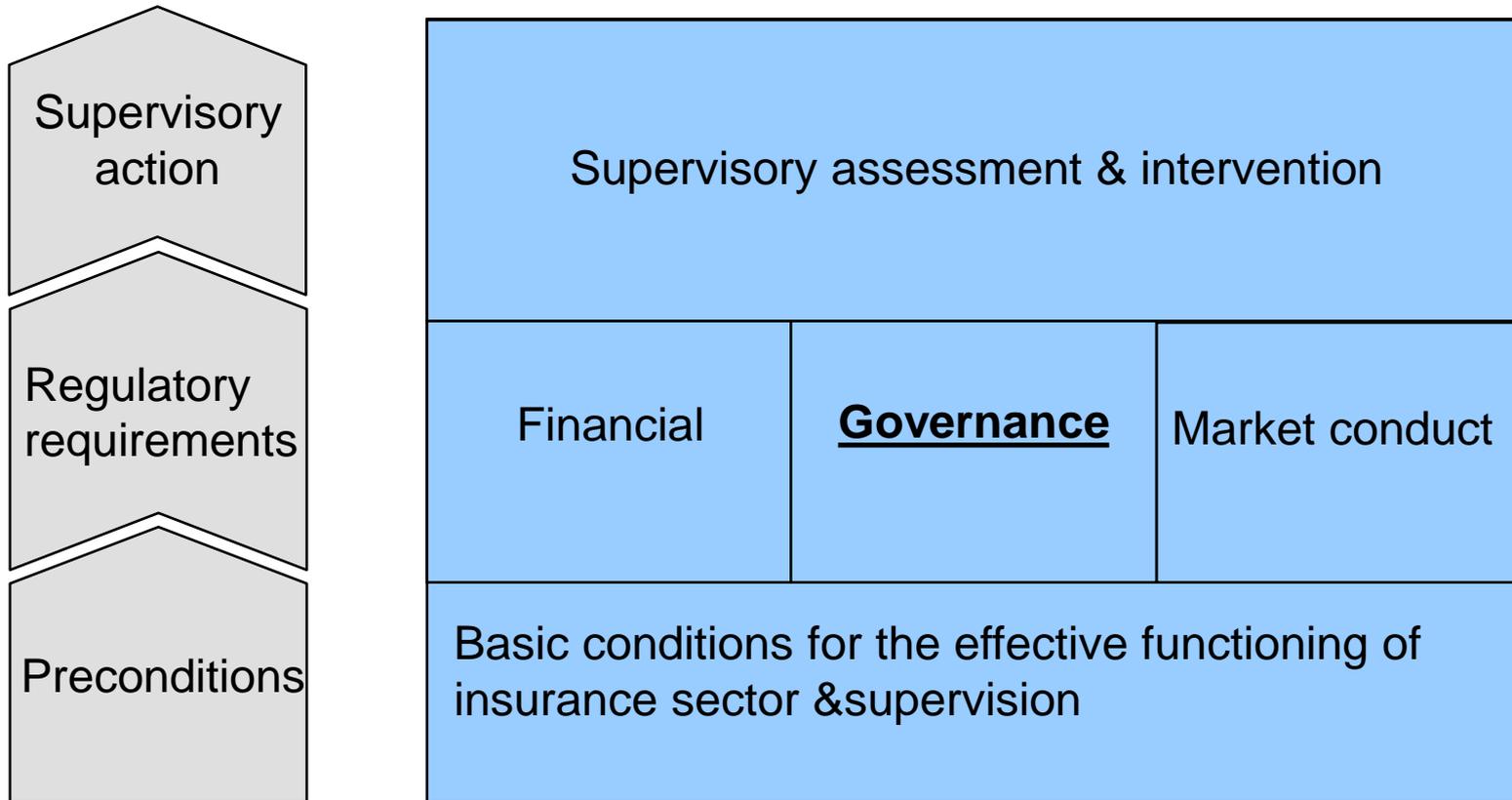
**Worldcom**

*Parmalat*

Olympus

‘Capital opens the door – without it you can’t start the business. But to be successful you need governance and risk management’

# IAIS Framework for Insurance Supervision



# Corporate Governance

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## Lessons learned from the Financial Crisis:

- People matter more than structures
- Focus on adverse incentives
- Importance of independent control functions

## Relevant Insurance Core Principles:

- ICP 5 Suitability of Persons
  - People matter more than structures
- ICP 7 Corporate Governance
  - Important system of check and balances
- ICP 8 Risk Management and Internal Controls
  - Importance of independent control functions

# Corporate Governance

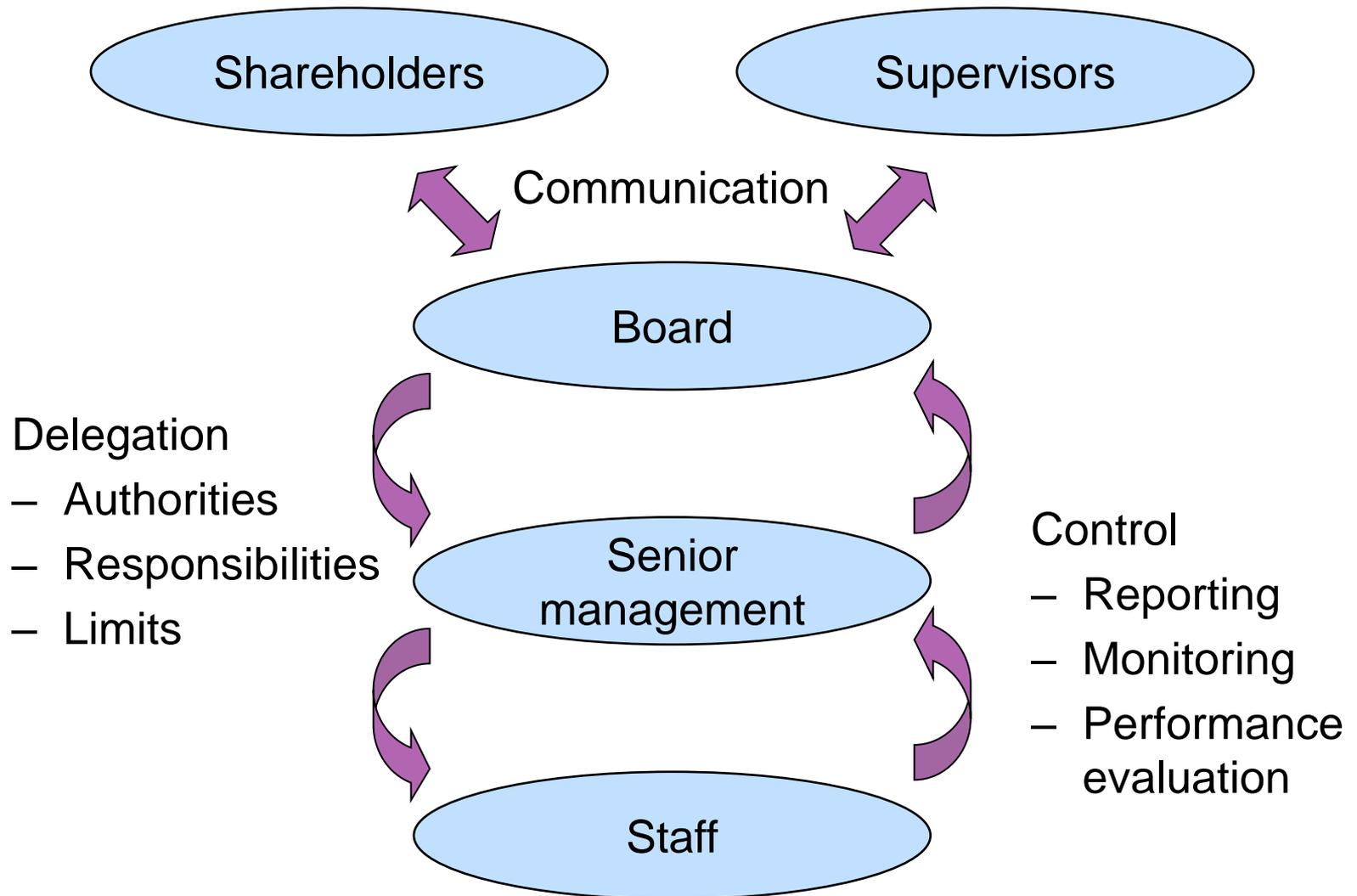
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## **ICP 7:**

The supervisor requires insurers to establish and implement a corporate governance framework which provides for sound and prudent management and oversight of the insurer's business and adequately recognises and protects the interests of policyholders.

# The corporate governance framework

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# Responsibilities of the Board

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- Setting objectives and strategies of the insurer (standard 7.1)
- Allocation of oversight and management responsibilities (st 7.2)
- Risk management & internal control systems & functions (st 7.5)
- Remuneration policy and practices (st 7.6)
- Reliable and transparent financial reporting (st 7.7)
- Transparency & communications (st 7.8)
- Duties of senior management (st 7.9)

# Board composition and structure

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- Structure and governance of the Board (Standard 7.3)
- Duties of individual Board members (7.4)

## Board Composition:

- Sufficient number of members
- Collectively & individually maintain necessary skills, knowledge, competency & understanding of business
- But not so large to maintain efficiency

# Suitability of Board members and management

## **ICP 5:**

“The supervisor requires Board Members, Senior Management, Key Persons in Control Functions and Significant Owners of an insurer to be and remain suitable to fulfil their respective roles”.

- Fit and Proper criteria
- Knowledge/experience (proper understanding of the business)
- Senior Management attitude and behaviour
- Financial soundness of significant owners

# The Board

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*The Board shall ensure that Senior Management:*

- carries out the day-to-day operations effectively and in accordance with the insurer's strategies, policies and procedures
- promotes a culture of sound risk management, compliance and fair treatment of customers
- provides the Board adequate and timely information
- provides to the relevant stakeholders and the supervisor the information required

# Behavioral Factors

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- Avoid commercial conflict of interest
  - Disclosure of potential conflict of interest
  - Requirement for arm's length transaction
  - Prior approval of transaction by board or shareholders
  - Decline to vote or take any decisions in related matters
- Separation of functions
  - Oversight responsibility (non-executive)
  - Day-to-day management (executive)
- Independence & objectivity
  - Especially sensitive in remuneration & audit areas

# IMF on Culture

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## Corporate culture:

*‘It is impossible to design an incentive structure that leads a bank manager to make the “right” decision every time... In cases in which incentive rules are insufficient, corporate culture will guide decisions and complement a bank’s ability to manage risk.*

*Corporate culture thus provides a set of unwritten, but widely accepted, rules that determine acceptable behavior— which in some corporate cultures may include disregarding written rules.’*

# Remuneration

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- Performance evaluation & remuneration affects behaviour
  - Promote business objectives & risk strategies if appropriately set
  - Ethics is important
- Remuneration policy should
  - Not encourage excessive or inappropriate risk taking
  - Be consistent with identified risk appetite & long term interests of insurer
- Should at least cover individuals who may have material impact on risk exposures & results

# Remuneration

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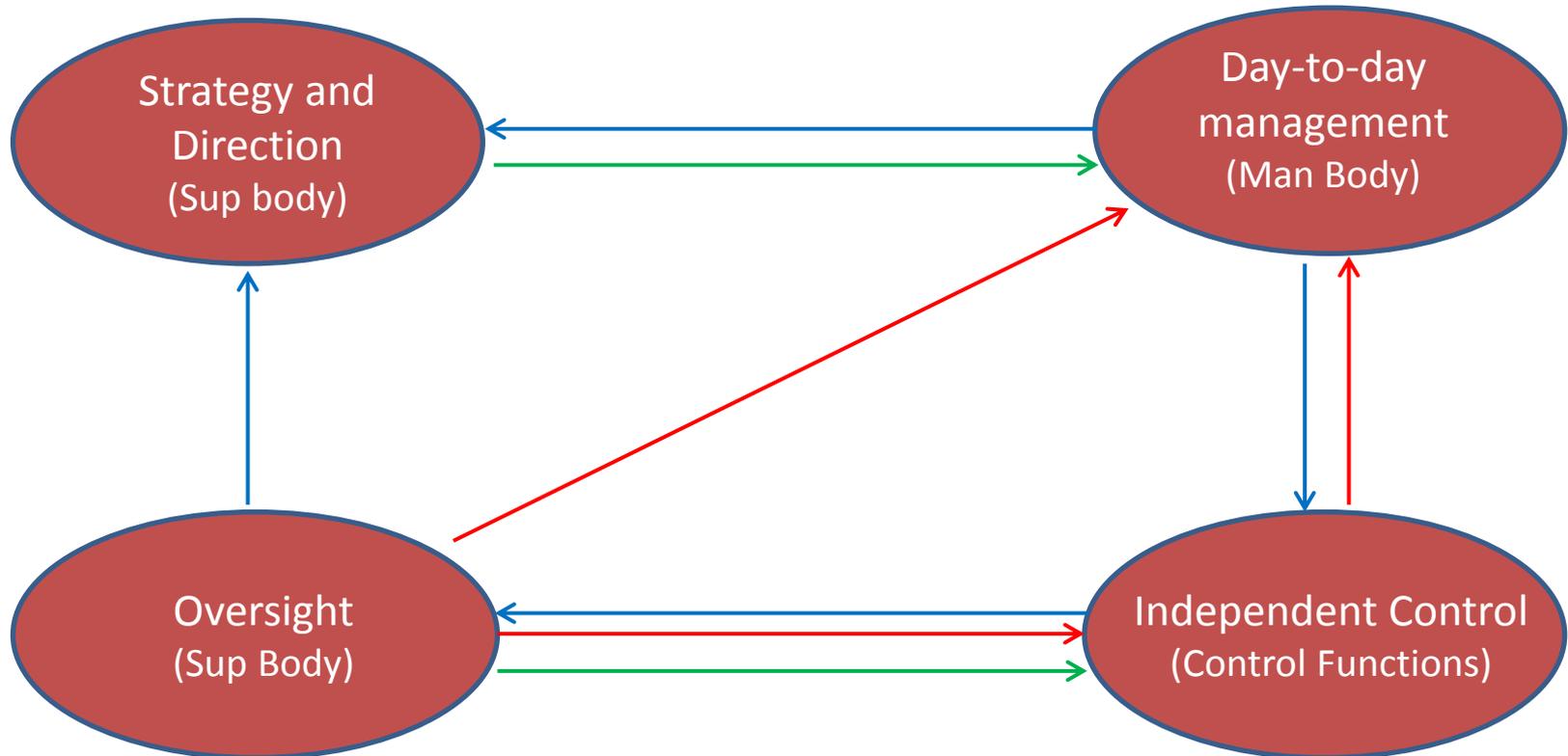
The Board shall have oversight of remuneration policies and practices (incentives for compensation and risk taking)

STAR TRIBUNE  
S&P



# Corporate Governance: division of roles

BLUE = input ; GREEN = direction ; RED = oversight / control



# Effectiveness of governance framework

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- Not the governance, but the behaviour of the board members determines the success of an organisation.
- Governance alone is not sufficient to correct incentives and motives of directors.
- Extreme financial incentives and personal characteristics of CEO's have a negative impact on the success of a company.
- Two crucial behavioural elements to enforce the effectiveness of Boards are modestness and truthfulness.

# Supervisory Review:

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- The Supervisor must have the power to require the insurer to demonstrate the adequacy and effectiveness of its corporate governance framework (Standard 7.10) and the power to impose corrective measures (ICP11)
- New challenges for Supervisors to supervise the governance culture within insurers

# Conclusions – review of ICP 7

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ICP 7 is currently under review based on:

- Self Assessment and Peer Review
- FSB principles and guidelines on risk culture and risk appetite frameworks
- Revised Basel Committee principles and guidelines
  - Consultation in June-August 2015

# ANNEX ICP 7 STANDARDS

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# ICP 7 Standards

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## **Objectives and Strategies of the Insurer**

7.1 The supervisor requires the insurer's Board to set and oversee the implementation of the insurer's business objectives and strategies for achieving those objectives, including its risk strategy and risk appetite, in line with the insurer's long term interests and viability.

## **Appropriate Allocation of Oversight and Management Responsibilities**

7.2 The supervisor requires the insurer's Board to:

- ensure that the roles and responsibilities allocated to the Board, Senior management and Key Persons in Control functions are clearly defined so as to promote an appropriate separation of the oversight function from the management responsibilities; and
- provide adequate oversight of the Senior Management.

# ICP 7 Standards

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## **Structure and Governance of the Board**

**7.3** The supervisor requires the insurer's Board to have, on an on-going basis:

- an appropriate number and mix of individuals to ensure that there is an overall adequate level of knowledge, skills and expertise at the Board level commensurate with the governance structure and the nature, scale and complexity of the insurer's business;
- appropriate internal governance practices and procedures to support the work of the Board in a manner that promotes the efficient, objective and independent judgment and decision making by the Board; and
- adequate powers and resources to be able to discharge its duties fully and effectively.

# ICP 7 Standards

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## **Duties of Individual Board Members**

7.4 The supervisor requires the individual members of the Board to:

- act in good faith, honestly and reasonably;
- exercise due care and diligence;
- act in the best interests of the insurer and policyholders, putting those interests of the insurer and policyholders ahead of his/her own interests;
- exercise independent judgment and objectivity in his/her decision making, taking due account of the interests of the insurer and policyholders; and
- not use his/her position to gain undue personal advantage or cause any detriment to the insurer.

## **Risk Management and Internal Control Systems and Functions**

7.5 The supervisor requires the insurer's Board to provide oversight in respect of the design and implementation of sound Risk management and internal control systems and functions.

# ICP 7 Standards

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## Remuneration Policy and Practices

7.6 The supervisor requires the insurer's Board to:

- adopt and oversee the effective implementation of a remuneration policy, which does not induce excessive or inappropriate risk taking, is in line with the identified Risk appetite and long term interests of the insurer, and has proper regard to the interests of its stakeholders; and
- ensure that such a remuneration policy, at a minimum, covers those individuals who are members of the Board, Senior Management, Key Persons in Control functions and other employees whose actions may have a material impact on the risk exposure of the insurer (major risk-taking staff).

# ICP 7 Standards

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## **Reliable and Transparent Financial Reporting**

7.7 The supervisor requires the insurer's Board to ensure there is a reliable financial reporting process for both public and supervisory purposes which is supported by clearly defined roles and responsibilities of the Board, Senior management and the external auditor.

## **Transparency and Communications**

7.8 The supervisor requires the insurer's Board to have systems and controls to ensure the promotion of appropriate, timely and effective communications with the supervisor and relevant stakeholders on the governance of the insurer.

# ICP 7 Standards

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## **Duties of the Senior Management**

7.9 The supervisor requires the insurer's Board to have appropriate policies and procedures to ensure that Senior Management:

- carries out the day-to-day operations of the insurer effectively and in accordance with the insurer's strategies, policies and procedures;
- promotes a culture of sound risk management, compliance and fair treatment of customers;
- provides the Board adequate and timely information to enable the Board to carry out its duties and functions including the monitoring and review of the performance and risk exposures of the insurer, and the performance of Senior Management; and
- provides to the relevant stakeholders and the supervisor the information required to satisfy the legal and other obligations applicable to the insurer or Senior Management.

## **Supervisory Review**

7.10 The supervisor has the power to require the insurer to demonstrate the adequacy and effectiveness of its Corporate governance framework.