III.1 Corporate Governance practices for Insurance companies

This policy paper is applicable to all licensed insurance companies operating in or from Aruba and is issued pursuant to section 10 of the State Ordinance on the Supervision of the Insurance Business (AB 2000 no. 82) (SOSIB).

1. Introduction
Insurance companies face special challenges, since they differ from other companies in that most of the funds they put at risk belong to third parties. Using third-party funds to generate income for the benefit of shareholders of a supervised institution demands that some limitation be placed by the supervisory authority on how prudently these funds can be put at risk.

It is essential that the management of the insurance company and its board of supervisory directors fully understand the nature of the business being undertaken by the company and the related risks, and are suitably qualified and competent to perform the necessary functions and oversight of the operation. In order to meet this goal, insurance supervisory authorities have developed a keen interest in determining that these institutions adopt sound corporate governance practices. These practices are presented below and the Centrale Bank van Aruba (the Bank) aims at promoting the adoption of sound corporate governance practices by insurance companies subject to its supervision.

2. Basic elements of sound corporate governance practices
Basic elements of sound corporate governance practices are:

- Establish clear strategic objectives and corporate values that are communicated throughout the organization.
- Set and enforce clear lines of responsibility and accountability throughout the organization.
- Ensure that board members and senior-management are qualified for their positions.
- Install adequate risk management policies.
- Implement comprehensive internal controls.
- Provide for full, accurate and timely financial disclosure.

In the following paragraphs these elements will be discussed more in length, especially in relation to the responsibilities of the Board.
3. **Responsibilities of the board and its members**
The Board has dual responsibilities. The Board has its responsibilities as a whole, while each Supervisory Director has responsibilities as an individual member of the Board. The responsibilities of the Board as a whole can be summarized as follows:
- Ensure competent management on an ongoing basis.
- Ensure appropriate plans and policies for the institution.
- Monitor operations to ensure compliance and adequate control.
- Oversee business performance.

3.1 **Board responsibilities**

A. **To ensure competent management on an ongoing basis**
Capable management is a critical element in the difference between success and failure of an institution. Integrity and suitability should be key considerations in the selection process of senior-management. Reference is made to paragraph 2 of the Directive on Sound Business Operations for further information on the integrity and suitability assessment conducted by the Bank. The appointment or dismissal of a member of senior-management should have the approval or at least the consent of the Board.

B. **To ensure appropriate plans and policies for the institution**

*Planning*
Rapid changes in the insurance industry call for clear strategies and business planning. Long-term strategic planning is done in strong cooperation with the Board and forms the broad policy framework, containing the institution’s philosophy and vision to the future.

*Policies*
All major activities must be covered by adequate policies and no such activity should be initiated before appropriate written policies and procedures are in place. Furthermore, policies should be communicated clearly through all levels, in order to promote consistency of interpretation throughout the organization as a whole. Reference is also made to paragraph 3 of the Directive on Sound Business Operations.

C. **To monitor operations to ensure compliance and adequate control**
The Board needs to ensure that senior-management has put adequate internal controls in place to ensure that the institution’s operations are properly controlled and that they comply with adopted policies, applicable laws and regulations.

D. **To oversee business performance**
The Board must receive timely all necessary information to evaluate management's performance (refer also to paragraph IV.3). The information provided should include at least:
- quarterly balance sheet and profit and loss account;
- analysis of actual versus budgeted income and costs (also per insurance branche);
- analysis of key ratio's and trends (including prudential ratio's);
• information on accounting, policy and compliance matters;
• information on important external developments;
• internal audit reports (including management's comments);
• reports from and correspondence with the external auditor (including the so-called management-letter);
• on-site examination letter and other relevant correspondence with the supervisor; and,
• changes in relevant laws and regulations;

3.2 Supervisory director’s individual responsibilities
A Supervisory Director should:

A. be aware of the institution’s operating environment
Each Supervisory Director should be generally informed of both the business environment and the legal and regulatory framework affecting the institution’s activities.

B. be diligent in performing its duties
Supervisory Directors must devote adequate time and attention necessary to fulfill their duties in a proper manner and should be knowledgeable enough to contribute in a meaningful sense to the activities of the Board.

C. exercise independent judgment
If a Supervisory Director disagrees with a Board decision, he or she should say so and formally register and explain his or her disagreement. Objective judgment, with due observance of the articles 9 and 10 of the Directive on Sound Business Operations, is critical to the Board’s effectiveness.

D. be loyal to the institution’s interests
Supervisors Directors are responsible for protecting the institution's interests. They must also ensure that neither they nor others abuse their position to benefit personally from the institution and avoid even the appearance of a conflict of interest. Reference is also made to articles 9 and 10 of the Directive on Sound Business Operations.

3.3 Required qualifications
Candidates for board positions in supervised insurance companies need at least some basic knowledge of either insurance or financial accounting. However, the Board as a whole must possess sufficient knowledge and experience in the insurance field.

3.4 Separate Board Committees
The Board can form, for example, the following separate committees, in order to perform certain tasks that require detailed review or in-depth consideration.
Audit Committee: This committee serves to monitor for compliance with Board’s policies, applicable laws and regulations, and to review financial and auditing matters.

Risk Management Committee: This committee ensures that acceptable risk limits and that appropriate risk-control techniques are in place to monitor and minimize losses to the institution.

Investment Committee: This committee ensures that the institution’s investment policies and assets/liabilities mix are adequate and that the institution’s investments comply with Board policies, general principles of asset and liability management, principles of risk management, and applicable laws and regulations.

Personnel development Committee: Matters usually dealt with by this committee include CEO compensation arrangements, remuneration, recruitment and termination policies, incentive schemes, and remuneration arrangements for Board members.

It should be stressed, however, that the Board as a whole remains fully responsible for a proper supervision of the institution. Therefore, these committees should report to the complete Board on all major issues discussed.

4. Risk Management
When evaluating the quality of risk management at insurance companies, the Bank considers primarily if the following conditions are met:

- active Board and senior-management oversight;
- adequate policies, procedures, and limits;
- adequate risk measurement, monitoring, and management information systems; and
- adequate and comprehensive internal controls.

4.1 Active Board and senior-management oversight
The Board should be consulted on the overall business strategy and on significant policy matters, including those related to the managing and taking of risks.

Senior-management is, however, primarily responsible for implementing strategies in a manner that limits risks associated with each strategy and that ensures compliance with laws and regulations on both a long-term and a day-to-day basis.
4.2 Adequate policies, procedures, and limits
The following guidelines are considered by the Bank in evaluating the adequacy of a supervised institution's policies, procedures, and limits:
- The institution's policies, procedures, and limits provide for adequate identification, measurement, monitoring, and control of the risks posed by its activities.
- The policies, procedures, and limits are consistent with the institution's stated goals and objectives and the overall financial strength of the institution.
- Policies clearly delineate accountability and lines of authority across the institution's activities.
- Policies provide for the review of new activities of the financial institution to ensure that the infrastructure necessary to identify, monitor, and control risks associated with an activity is in place before the activity is initiated.

4.3 Adequate risk measurement, monitoring, and management information systems
Effective risk monitoring requires institutions to identify and measure all material risk exposures. Consequently, risk monitoring activities must be supported by information systems that provide senior-managers and Board with timely reports on the financial condition, operating performance, and risk exposure of the financial institution, as well as with regular and sufficiently detailed reports for line managers in the day-to-day management of the institution's activities.

In assessing the adequacy of a supervised institution's measurement and monitoring of risk and its management reports and information systems, the Bank will consider whether the following conditions exist:
- The institution's risk monitoring practices and reports address all of its material risks.
- Key assumptions, data sources, and procedures used in measuring and monitoring risk are appropriate and adequately documented and tested for reliability on an ongoing basis.
- Reports and other forms of communication are consistent with the institution's activities, structured to monitor exposures and compliance with established limits, goals, or objectives, and as appropriate, compare actual versus expected performance.
- Reports to the Board and management are accurate and timely and contain sufficient information to identify any adverse trend and to evaluate adequately the level of risk faced by the institution.
4.4 Comprehensive internal controls
An institution’s internal control environment is critical to the safe and sound functioning of the institution and, in particular, to its risk management system. Establishing and maintaining an effective system of controls, including appropriate segregation of duties, is one of senior-management’s primary responsibilities.

When properly structured, a system of internal controls promotes effective operations and reliable financial and regulatory reporting. Moreover, the system safeguards assets and helps to ensure compliance with relevant laws, regulations, and institutional policies.

An internal auditor should test internal controls regularly. The results of audits or reviews should be adequately documented, as should management’s responses to them. In addition, communication channels should exist that allow negative or sensitive findings to be reported directly to the Board or to the relevant Committee of the Board.