FINANCIAL SERVICES COMMISSION

GUIDELINE NO. 1

GUIDELINE ON CORPORATE GOVERNANCE

(This guideline is issued pursuant to section 53 of the Financial Services Commission Act, and comes into effect on March 1, 2013)

1.0 INTRODUCTION

1.1 The requirement to promote good corporate governance is receiving increased international attention. Given recent developments in the financial services sector in the region and beyond, the importance of good corporate governance is now unquestioned. The Financial Services Commission wishes to provide guidance to boards of directors and management of insurance companies and intermediaries about the Commission's expectations on corporate governance and related matters. This guidance includes specific recommendations contained with IAIS Core Principles of Supervision.

1.2 The Commission's approach to the supervision of insurance is becoming increasingly risk-based. This means that the Commission, to the extent possible, identifies, assesses, prioritizes, and minimizes the likelihood of events or circumstances occurring with might prevent the Commission from achieving its objectives. Further to this the Commission assesses the risks posed by an insurer by gaining an understanding of a licensed insurer's operations, the risks it faces and how it deals with these risks. The consideration of the governance and the decision-making and control processes of an insurer is a key component of this assessment process. This approach to supervision is in contrast to a transaction-oriented review.

1.3 In implementing this approach the Commission aims to use its resources to focus attention on insurers and activities where there is a greater likelihood of a risk crystallizing and its impact having repercussions for policyholders and the continued development of a viable, competitive and innovative Barbados insurance market. Additionally, the Commission aims to be proportionate in its approach to supervision and to consider the costs and benefits of its regulatory and supervisory processes.

1.4 Any guidance issued for corporate governance must be principle based, such that it can be adapted according to the nature of an insurer's customer and the characteristics of the risks assumed. It is the responsibility of the Board to determine which specific provisions of this guidance should be applied taking into account the size, nature, complexity and risk profile of the business of the insurer. When as part of its supervisory process, the Commission assesses the effectiveness of an insurer's corporate governance, the degree of applicability and weighting of individual elements in this guidance will depend on the size, nature, complexity and risk profile of each insurer.

1.5 Insurers must take immediate steps to ensure they are in compliance with the matters contained in the Guideline; the Commission encourages insurers to come into compliance as soon as possible.

2.0 BACKGROUND

2.1 Insurers must be prudently managed. The prime responsibility for the sound and prudent management of an insurer rests with the board of the insurer. Corporate governance refers to systems (such as structures, policies and processes) through which an entity is managed and controlled. What makes structures and policies work in practice are a knowledgeable and competent board, with a clear understanding of its role and strong commitment to, carrying it out.

2.2 Individual insurers will adopt different approaches to corporate governance, taking into account the nature, scope, complexity, and risk profile of its organization. The supervisory process will take this into consideration in the evaluation of individual insurers.

2.3 This guideline provides information to boards of directors and management of insurers about the expectations of the Commission on corporate governance and related matters, and the factors that the Commission will take into account in assessing the quality of governance of each insurer.

2.4 The Commission recognizes the need for clarity as to the scope and implementation of the provisions of the guideline if the regulatory system is to command the confidence of insurers and policyholders. It seeks, therefore, to ensure that those operating in Barbados have a good understanding of the nature of the requirements and of the Commission's approach in implementing the guideline.

2.5 This Guideline is not intended to be exhaustive. The Commission will do its best through this and other guidelines to set out its understanding of the legal provisions affecting corporate governance, and to provide additional information about the Commission's regulatory approach and expectations regarding these matters. The relevant legislation is comprised of the Financial Services Commission Act, the Insurance Act Cap 310, and the Exempt Insurance Act Cap 308B.

3.0 APPLICATION

3.1 High standards of corporate governance are important for all registered insurers. In managing its affairs, an insurer should have regard to such principles of good corporate governance, as it reasonably considers applicable to it. It is the responsibility of the Board to determine which specific provisions of this Guidance should be applied taking into account the size, nature, complexity and risk profile of the business of the licensed insurer.

3.2 As part of its supervisory process, the Commission will look for indications that, overall, processes or procedures for effective corporate governance are in place, that they are appropriate to the individual insurer, and that they are operating effectively. The Commission will formulate its overall judgment on the effectiveness of an insurer's corporate governance based on a variety of indicators. The degree of applicability and weighting of individual elements in this guidance will depend on the nature, scope complexity and risk profile of each insurer.

3.3 All registered insurers and intermediaries are expected to comply with the standards in this Guidance.

3.4 The Commission expects registered insurers to be aware of other emerging and in-force standards that are applicable to their organizations (which may depend, for example, on whether the institution is a publicly-traded entity) and to consider and, where appropriate, incorporate these into the institution's governance practices. The Commission also recognizes that these other standards may overlap or exceed some of the expectations for corporate governance described in this and other guidance issued by the Commission, and that developments in these other standards may have an implication for insurers with respect to time and effort involved in meeting these other standards.

3.5 Where other standards for corporate governance are consistent with the Commission's expectations for corporate governance as described in this and other guidance, and where the Commission can rely on an insurer's compliance with these other standards, it is not the intention of the Commission to require a company to undergo additional costs in order to comply with both the Commission's guidance as well as the other standards.

4.0 DEFINITIONS

4.1 **Board** – The term board refers to either the entire board of directors of the licensee or, where applicable, to a committee of the board that has been delegated a particular element of board oversight.

4.2 **Management** comprises either persons employed by a licensee who exercise senior management responsibilities. Senior management responsibilities mean having primary responsibility for one or more of the following:

- High-level decision-making;
- Implementing strategies and policies approved by the board;
- Developing processes that identify, manage and monitor risks incurred by the insurer;
- Monitoring the appropriateness, adequacy and effectiveness of the risk management and internal control system.

5.0 EFFECTIVE CORPORATE GOVERNANCE

5.1 The board is ultimately accountable and responsible for the performance and conduct of the insurer. It should have a balance of appropriately skilled, experienced and qualified individuals who can apply informed and independent judgment to the governance of the licensed entity. It should ensure that the insurer is effectively directed and managed, and its business is conducted in a sound and prudent manner with integrity, due care and professional skills appropriate to the nature and scale of its activities. In seeking to ensure that the objectives of this Guidance are met, the insurer must exercise its judgement in determining an effective approach to corporate governance, taking into account the nature, scope, complexity, and risk profile of its organization, and also having regard to the cost effectiveness of the rules and procedures.

5.2 Corporate governance encompasses the means by which directors and management of an insurer are held accountable for their actions and for the establishment and implementation of oversight functions and processes. The value of good corporate governance lies in its contribution to both the prosperity and accountability of the insurer. There is no one standard model of corporate governance. A corporate governance framework specifies the distribution of rights and responsibilities among different participants in management of the company and sets out the rules and procedures [practices] for making decisions, and for the management and control of the insurer's business and affairs. Corporate governance includes corporate discipline, transparency, independence, accountability, and responsibility. Corporate governance also includes compliance with legal and regulatory requirements.

5.3 Risk management and internal controls systems are integral parts of a corporate governance framework. Risk management and internal control systems and practices may also differ depending on the size and complexity of the insurer, and the nature of the insurer's risk exposures. The Commission has issued guideline No. 2 outlining its expectations of licensees for Risk Management and Internal Control systems.

5.4 Best practices for governance practices are continuously evolving. The Commission expects the board to be aware of emerging best practices that are applicable to their institution, and will look for indications that these have been considered and, where appropriate, incorporated into the institution's governance practices.

6.0 EFFECTIVE BOARD PERFORMANCE

6.1 Corporate governance is often referred to as a system of "checks and balances". This recognises that an insurer has to be flexible and responsive to developments affecting its operations in making timely decisions, while at the same time being transparent and having appropriate systems, controls and limits to ensure that powers are not unduly concentrated and are used in the best interest of the insurer as a whole and its stakeholders.

6.2 The Board should adopt a process for setting and overseeing the implementation of the insurer's overall business objectives and risk strategies, taking into account the long term financial safety and soundness of the insurer as a whole, and the legitimate interests of its stakeholders, including fair treatment of customers. These objectives and strategies should be adequately documented and properly communicated to its Senior Management, Key Persons in Control Functions and all other relevant staff of the insurer.

Structure of the Board

6.3 In addition to complying with the Companies Act of the laws in Barbados, the board of an insurer shall comprise a suitable number of directors that enables it to carry out its functions effectively and efficiently, taking into account the activities and business volume of the licensee. The Commission expects that all directors will be fit and proper to hold the post. Collectively board members should have the appropriate breadth of experience, ability and integrity to conduct the business of the insurer, taking account of potential conflicts of interest.

6.4 To enable the board to make sound decisions in the best interests of the insurer, independent and objective opinions are essential. While certain governance structures, including those described in this guideline, can encourage independence, the Commission does not view any one structure as guaranteeing independence. What matters is that a particular structure and the board's behaviour are effective, taking into account the ownership structure and particular circumstances of the financial institution.

6.5 The Board may consider the establishment of an Audit Committee. Without prejudice to the relevant provisions of the Companies Act, the audit committee can review –

(a) Returns that the registered insurer is required to file with the Commission;
(b) Reports made by the auditor under the Companies Act and the Insurance Act.
(c) Such other reports, transactions or matters as may be prescribed.

<u>Oversight Responsibilities of the Board</u>

6.6 The following is a list of basic oversight responsibilities that the board should consider when establishing and assessing the effectiveness of an insurer's corporate governance framework. The degree of applicability of these oversight responsibilities will depend on the nature, scope, complexity and risk profile of each insurer:

6.6.1 Clearly setting out its responsibilities toward, and commitment to the principles of good corporate governance principles in respect of the licensed entity;

6.6.2 Satisfying it that the insurer is organized in a way that promotes the effective and prudent management of the institution and the board's oversight of that management;

6.6.3 Approving and reviewing the broad business strategies and significant policies of the insurer, including the means of attaining them, and procedures for monitoring and evaluating the progress toward them. Adherence to the policies and strategies are reviewed regularly, and at least annually;

6.6.4 As appropriate, having in place and monitoring independent risk management functions that identifies and monitors the material risks related to the type of business undertaken. As appropriate, the board of directors establishes and monitors audit functions, actuarial functions, strong internal controls and applicable checks and balances;

6.6.5 Where applicable, clearly distinguishing between the responsibilities, decision-making, interaction and cooperation of the board, chairman, chief executive and management;

6.6.6 Requiring a clear division of responsibilities to ensure a balance of power and authority, so that no one individual has unfettered powers of decision;

6.6.7 Appointing and dismissing management. The board must ensure that management are fit and proper, and compensated in a manner that is consistent with appropriate incentives;

6.6.8 Having access to accurate, relevant and timely information. Where stakeholders participate in the corporate governance process, they should have access to relevant information;

6.6.9 Where the insurer writes domestic business, providing oversight of the market conduct activities of the insurer, including setting out policies that address conflicts of interest, fair treatment of customers and information sharing with stakeholders, and reviewing these policies regularly;

6.6.10 Where appropriate, establishing standards of business conduct and ethical behaviour for directors, management and other personnel. These include policies on private transactions, self-dealing, preferential treatment of favoured internal and external entities, covering trading losses, and other inordinate trade practices of a non-arm's length nature. This includes ensuring that the insurer has an on-going, appropriate and effective process of ensuring adherence to those standards; and

6.6.11 Collectively ensuring that the insurer complies with all relevant laws, regulations, guidance notes, industry standards and any established codes of conduct. As applicable, this may include identifying an officer or officers with responsibility for ensuring compliance with relevant legislation and required standards of business conduct, and who reports to the board of directors at regular intervals.

Responsibilities of Management

6.7 Senior Management is responsible for:

6.7.1 Overseeing the operations of the insurer and providing direction to it on a day-to-day basis, subject to the objectives and policies set out by the board of directors and in compliance with applicable laws and regulations.

6.7.2 Providing the board of directors with recommendations, for its review and approval, on objectives, strategy, business plans and major policies that govern the operation of the insurer.

6.7.3 Facilitating the board's oversight role, by providing accurate, relevant and timely information to the board, enabling the board to review business objectives, strategy and policies, to hold management accountable for its performance, and to determine whether the insurer is operating in an appropriate control environment. Management also facilitates effective oversight through fostering candid and robust board discussions.

6.7.4 Ensuring that the independent oversight functions, such as internal audit, actuarial, compliance and risk management, have the resources and support to do their work and the capacity to offer objective opinions and advice to the board and to management.

7.0 RELATIONSHIP BETWEEN THE BOARD AND THE COMMISSION

7.1 A licensee and its board and management are expected to deal with the Commission in an open and cooperative manner. There is a need for candour and cooperation in a licensee's relationship with the Commission. Insurers are required to advise the Commission promptly of any matter that might reasonably be expected to affect their authorisation to carry on business in Barbados or might materially affect the interests of the policyholders.

7.2 Where an insurer conducts insurance business outside Barbados, it should notify the Commission in writing if its right to conduct that business ceases, or if the insurer's right to conduct insurance business has been limited or otherwise adversely affected under a law of the jurisdiction in which the business is being conducted. Notification must be provided with 14 days of the event occurring.

8.0 ASSESSMENT OF CORPORATE GOVERNANCE

8.1 The Commission will formulate its overall judgment on board effectiveness and quality of governance of an insurer based on a variety of indicators, the most important of which are findings from off-site monitoring and on-site examinations. As part of its supervisory process, the Commission will look for indications that, overall, processes or procedures are in place, that they are appropriate to the individual institution, and that they are operating effectively.

8.2 When assessing the board's effectiveness in guiding the insurer and overseeing its activities effectively, the Commission may consider whether the board members and management have the level of competence for their roles, and whether they have the appropriate ability and integrity to conduct insurance business, taking account of potential conflicts of interests. Additionally, the Commission will consider the collective breadth of experience and the calibre of the board through appropriate fit and proper reviews where necessary. Appropriate ability can generally be judged from the level of a person's professional or formal qualifications or relevant experience within the insurance and financial or other related businesses. The knowledge and experience required depends upon the position and responsibility of the functionary within the insurer.

8.3 The Commission's approach to the supervision of insurance focuses on understanding the quality and reliability of an insurer's governance programs, risk management processes and controls, internal controls; and independent and effective oversight (e.g. via audit and compliance) of business and operational activities and methodologies. Through the on-site visits, this approach aims at raising the level of dialogue between the Commission and the insurer, and enhancing the Commission's understanding of the insurer's governance umbrella, respective roles and accountability, and the "tone at the top". We do not believe that transitional arrangements will be required on an industry-wide basis as the expected impact from the guideline on the operations of the company should be minimal.