Welcome Remarks by the Executive Director of the Centrale Bank van Curacao en Sint Maarten (CBCS) at the first training organized by the CBCS in conjunction with the NAIC and IAIS on Financial Analysis and Risk Focused Examinations

Opening remarks by

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Ladies and gentlemen, good morning,

Welcome to this training organized by our Bank on Financial Analysis and Risk-Focused Examinations. We extend a special welcome to our foreign guests and to Mrs. Julie McPeak, Tennessee Commissioner of Insurance.

I am very pleased to address you on the occasion of the first training organized by our Bank in conjunction with the National Association of Insurance Commissioners (NAIC) and the International Association of Insurance Supervisors (IAIS). The Bank has been a member of the IAIS for over a decade now. Our aim has always been to comply with the guidelines of this organization whose primary goal is to set standards for the regulation and supervision of the insurance industry at the international level. We have committed ourselves to this endeavor, and we periodically assess our supervisory framework against the IAIS Insurance Core Principles (ICPs).

In November of 2011, our Bank signed an MOU with the National Association of Insurance Commissioners. This MOU has proven to be another milestone in our efforts to enhance and strengthen our relationship and commitment towards information sharing and cooperation with foreign supervisors. I must say that the signing of this MOU has so far been very beneficial to our Bank. In the past couple of months, our staff has been able to make use of the NAIC's on-line training resources at minimum cost, and we have received information from NAIC staff on several topics of interest to us. In addition, NAIC readily accepted our request to provide local training to our insurance staff on their supervisory methodology.

With the increasing integration of financial sectors, the globalization in the insurance sector, and the lessons learned from the financial crisis, it has become a must to ensure that supervisors in all jurisdictions are well-equipped to address their largely preventive role.

In principle, it is each jurisdiction's role and responsibility to provide its supervisors with the necessary expertise and know-how to carry out their role of insurance supervision. However, this task is easier said than done, particularly for emerging supervisory authorities, who cannot easily find the supervisory experience and skills they need in their own jurisdiction.

Allow me to elaborate a bit on the reason why we as supervisors of this industry need to continue educating ourselves the area of insurance.

Insurance companies have, as their prime business, the accepting of risks on behalf of others. They accept different types of risk with the expectation of generating an adequate return on capital from the premiums charged. Therefore, the management of the risk assumed is fundamentally important to the success of the operation.

Intuitively, an insurance company should be able to manage exposures of both liabilities and assets so that it allocates its established 'risk tolerance' between underwriting activities and investment strategy to maximize its expected overall return on capital. The 'risk tolerance' level of an individual company is clearly a matter for its Board of Directors to establish, subject to minimum regulatory standards. I define risk tolerance as management's willingness to live with unstable results to boost expected profitability.

Having said that, it goes without saying that as the supervisor of the financial sector, we must be aware of the risks within the institutions that we supervise. Prudential supervisors must have oversight programs and should be able to implement these to avert financial meltdowns within their financial sector.

In my opinion, supervisors should be able to:

- Read the warning signs.
- Make adequate use of the regulatory powers at their disposal to stop the buildup of risks in their system.

- Up to a certain extent, control the risk appetite of the supervisory board and management of a regulated entity.
- Require disclosure of information by institutions because such disclosure offers the best means of consumer protection.

The clue in all that I just said is good supervision. But how do we define good supervision? As with everything, we know that our supervisory framework can always use further improvement. With this in mind, our Bank made the decision a few years ago to adopt a risk-based supervisory approach.

In our approach, we will pay considerable attention to the institutions' corporate governance framework, risk statements, and the risk management strategies adopted by the entities. The effectiveness of these processes will be assessed off-site and during on-site examinations.

Our goal with this new framework is to take a very active, 'hands-on' approach to supervision. All of our supervisory activities and interventions will be guided by an overarching risk-based framework. In my view, supervision is more than enforcement of prudential rules like solvency, capital adequacy, and so forth. I tend to define supervision as the oversight of the effectiveness of an entity's risk management. Hence, supervision should not be constrained by the rules but should extend beyond the rules to ensure effective management of risk by the regulated entities.

It goes without saying that a financial institution can never have enough capital or liquidity if material flaws exist in its risk management practices. Only by understanding the risks that financial institutions take on can prudential supervisors begin to take action to protect the interests of those whose interests we are bound by law to protect. In my opinion, that is where risk-based supervision comes in. Risk-based supervision is about the efficient allocation of limited supervisory resources to their most effective use, or simply said: Pick important problems and fix them!

Understanding and responding to the risks faced by regulated financial institutions is precisely what a prudential supervisor's mission should be. To carry out this mission, I believe that the supervisor should have a structured process to:

- Identify risks;
- Assess their significance;
- Develop a remediation strategy; and
- Prioritize the allocation of resources.

The effectiveness of any risk-based approach depends a lot on the supervisor's ability to see the risks within the regulated entities. Coming to grips with matters of risk management and corporate governance requires a certain approach from supervisors that includes the following:

- An understanding of the institution's business model and appetite for risk for each of its main business lines;
- Frequent interaction with supervised institutions at supervisory board and management level (firms need to know that the supervisor is looking over their shoulder!);
- Capacity to assess the effectiveness of risk management and control functions, including how the entity is governed and its prevailing risk culture; and
- Capacity and willingness to act when deficiencies are identified.

To date, the Bank has had good experiences during our meetings with the supervised institutions. In these meetings, which are held on a regular basis, the Bank discusses the business strategy, perceived strengths and weaknesses, and regulatory points of concern, among other things, with the managing and supervisory boards of the supervised institutions. These discussions provide the Bank with valuable information on where to focus our supervisory efforts.

Having said that, I do admit that none of what I have recommended is easy to implement. As noted earlier, risk-based supervision requires a hands-on, active approach to prudential supervision. It requires experienced supervisors with deep industry knowledge. And, even after all that, there is no guarantee that supervisors will always make the right calls on risk.

Despite that caveat, I believe that supervisors need to continue investing in the training and upgrading of one of their most valuable resources, --their staff--. And our Bank is committed to do so. In the coming days one of our staff members will tell you more about how far our Bank has come in developing and implementing its risk-based supervision methodology.

We see this training as an opportunity to prepare our staff for this new approach to supervision and to assure a smooth implementation over time.

Having observed the different topics on the agenda for this training, I would suggest that those unable to attend the training are going to miss a big opportunity to participate in vital discussions about issues that are most valuable for all of us as supervisors of an ever-evolving financial industry.

Apart from the very interesting topics, I am sure that the coming sessions will result in the sharing of valuable supervisory experiences that will greatly contribute to further fortification of the supervisory framework of each participating jurisdiction.

Organizations like the IAIS and the NAIC have proven valuable sources of expertise and know-how. I believe that the IAIS's contribution in the form of partial funding of this training underscores its role in supporting the education and training of its members. Of equal importance is the time donated by NAIC staff to assist us with the set-up and presentation of this training. I therefore extend a word of thanks to both organizations for their valuable contribution to this training programme. Please allow me also to thank our staff for the preparatory work done for this training. Last, I extend a word of thanks to you for participating in this training. To a great extent, the success of this training depends on your active participation.

Allow me to wish you all fruitful training sessions and a pleasant stay on our island.

Thank you.