DeNederlandscheBank
EUROSYSTEEM

Q&A on supervisory board independence – Insurers

An insurer qualifying as a public limited company or a European company is required, under Section 3:19(1) of the Dutch Financial Supervision Act (*Wet op het financieel toezicht – Wft*), to establish a supervisory board of at least three members.[1] In this Q&A, DNB will elaborate on the legal basis for supervisory board independence, and set out its views on different types of independence and ways for insurers to ensure supervisory board independence.[2]

Question:

What are the requirements that govern supervisory board independence?

Answer:

Good and balanced institutional governance contributes to a robust and ethical financial sector. A discerning and independent supervisory board exercising its supervisory and advisory roles is instrumental in a financial services provider's governance structure. At insurers, supervisory board independence revolves around three types of independence: independence of mind, independence in appearance and formal independence.

Legal basis

In Section 3:17, the *Wft* stipulates that insurers are to structure their governance processes such that sound and ethical operational management is guaranteed.[3] By exercising internal supervision of the policies pursued by management and the general course of business at an institution, a supervisory board contributes greatly to sound and ethical operational management. A supervisory board will also offer advice to management. In performing their duties, supervisory directors are required to act in the best interest of the company and its business (Sections 140/250/53a in

---

[1] An insurer qualifying as a mutual insurance association is not required to establish a supervisory board under Section 3:19 of the *Wft*. That said, mutual insurance association societies governed by the statutory two-tier regime *are* required to establish a supervisory board under the Dutch Civil Code (*Burgerlijk Wetboek – BW*). If an insurer is not required to establish a supervisory board, either under Section 3:19 of the *Wft* or under the statutory two-tier regime, it may still need to do so for the purposes of ensuring that it has a balanced organisational structure as per Sections 17 and 26.2 of the Dutch Decree on Prudential Rules for Financial Undertakings (*Besluit prudentiële regels Wft – Bpr*).
[2] In this Q&A, the term 'supervisory board' is used to refer to the highest internal supervisory body. This Q&A also applies to non-executive directors on a one-tier board.
[3] Under Section 26.2 of the *Bpr*, insurers other than limited-risk insurers are also required to have in place an adequate, transparent organisational structure. Under Section 17 of the *Bpr*, limited-risk insurers should have in place a clear, balanced and adequate organisational structure.

conjunction with Section 47, Book 2 of the Dutch Civil Code (*Burgerlijk Wetboek – BW*)).

Pursuant to Section 3:8 of the *Wft*, the members of an insurer's supervisory board must be fit to fulfil their supervisory role. To ensure this, DNB will perform fitness assessments based on the Policy Rule on Fitness. Part of the fitness assessment is a review of whether the person in question is capable of making their own sound, objective and independent decisions and judgements.

Types of independence

In assessing the independence of a supervisory board, DNB will consider the following three types of independence.

1: Independence of mind

All supervisory board members should be independent of mind. Acting with independence of mind is particularly important in discussions and in the decision-making process in the supervisory board. All supervisory directors should engage actively in their duties and be capable of making sound, objective and independent decisions and judgements when fulfilling their duties and responsibilities. Supervisory board members must have the courage, conviction and strength to effectively assess and challenge the management body's policies and proposed decisions without being led by group thinking.

They cannot have any conflicts of interest that would impede their ability to perform their duties independently and objectively.

2: Independence in appearance

Supervisory board members should prevent and/or manage conflicts of interest or the semblance of such conflicts. The supervisory board must have a policy in place to address and manage actual and potential conflicts of interest or the semblance of such conflicts. Dutch law stipulates that, if a supervisory director has a direct or indirect personal interest that is contrary to that of the institution, they will not take part in the supervisory board's deliberations and decision-making.

3: Formal independence

To effectively ensure sound and ethical operational management and a balanced or adequate organisational structure, a supervisory board should, in principle, have a sufficient number of formally independent members.

When does a supervisory director qualify as formally independent?

Although the EBA/ESMA Guidelines on the assessment of the suitability of members of the management body and key function holders (hereinafter: "the EBA/ESMA Guidelines") do not apply to insurers, they do provide useful guidance for assessing

DeNederlandscheBank
EUROSYSTEEM

whether a supervisory board member can be considered as formally independent. For this reason, DNB will take the EBA/ESMA Guidelines as a starting point when assessing whether an insurer's supervisory directors qualify as formally independent (notably Paragraphs 89-91). An insurer may decide not to follow the EBA/ESMA Guidelines, explaining its reasons, if it can demonstrate why it believes a supervisory director should nevertheless be considered as formally independent.

What is a 'sufficient number' of formally independent supervisory directors?

There is no strict definition of the term 'sufficient number' that applies across the board, given that its interpretation depends on the circumstances of a case. That is why, with this Q&A, DNB seeks to provide insight into the circumstances it will consider when determining what constitutes a 'sufficient number' of formally independent supervisory board members in a specific case.

In assessing how many formally independent supervisory board members are required in a specific case to effectively ensure sound and ethical operational management and a balanced or adequate organisational structure, DNB will consider all relevant circumstances of a case, including the nature, scale, risks and complexity of the insurer's operations. In some instances, it may be enough for insurers to have fewer than 50% formally independent supervisory board members for the purposes of ensuring sound and ethical operational management and a balanced or adequate organisational structure, while other insurers may be required to have at least 50% formally independent members on their supervisory board.

Furthermore, listed insurers are subject to the Dutch Corporate Governance Code (CGC), which stipulates in a best practice provision that a majority of their supervisory board members should be formally independent. The CGC is a form of self-regulation based on the comply-or-explain principle.

When will an insurer have to have at least 50% formally independent supervisory directors?

Circumstances may dictate that an insurer should have at least 50% formally independent supervisory board members to ensure sound and ethical operational management and a balanced or adequate organisational structure. To DNB, such circumstances would include situations in which the interests of the insurer in question are, or are likely to become, incompatible with, or contradictory or subordinate to, the interests of shareholders or other stakeholders. In all these circumstances, it is particularly important that the supervisory board can exercise countervailing power. A number of examples of such circumstances have been provided below:

a) **Group structure with entities providing different services**: providing different services and/or not holding the same type of licence (e.g. insurance/banking groups) may lead to situations where the interests of the insurer and the parent institution are opposed or where the interests of the insurer are, or are likely to become, subordinate to other interests within the group.

b) **Presence of director-majority shareholder or dominant shareholder**: structures with a director-majority shareholder/dominant shareholders (e.g. because of a majority interest or substantial minority interest, specific special voting rights or a particular investment strategy (e.g. short or medium-term profit maximisation)) come with a risk of the decision-making process being dominated by the majority shareholder or shareholders, as a result of which their part interest will take precedence over other part interests in the insurer or the insurer's own interest.

c) **Parent institution outside EEA:** if the parent institution is not located in the EEA, the risk of a conflict of interest between the parent institution and the insurer and/or of incompatibility of a parent institution's decision with the interests that are sought to be protected by European and/or Dutch law is greater than if the parent institution were located in the EEA, except where parent companies are subject to supervision that is equivalent to insurance group supervision under the Solvency II Directive.

When will one formally independent supervisory director be considered sufficient?

There may be circumstances in which an insurer may suffice, in principle, with having at least one formally independent supervisory board member to ensure sound and ethical operational management and a balanced or adequate organisational structure. In DNB's view, this would apply, for instance, to captives:

Captive: in the Solvency II Directive, a captive insurer/reinsurer is defined (in brief) as an insurance/reinsurance undertaking, owned by a parent institution for the purpose of providing insurance/reinsurance cover exclusively for the risks of the undertaking or undertakings to which it belongs or of an undertaking or undertakings of the group of which it is a member. The proportional approach for captives will imply, in principle, that at least one formally independent supervisory director will suffice, given that a captive provides insurance/reinsurance cover exclusively for the risks of the undertaking or undertakings to which it belongs or of an undertaking or undertakings of the group of which it is a member.[4] In DNB's opinion, this poses a limited risk of conflicts of interest between the captive and the parent institution. Whether or not a conflict of interest exists is subject to review on a case-by-case basis.

---

[4] For the sake of completeness, DNB would note that, based on Article 109 of the Capital Requirements Directive (CRD), captives in a CRD group are also governed by such provisions as those of Article 91 of the CRD. For this reason, DNB will apply the relevant EBA Guidelines to these captives (Guideline 9, independence of mind and independent members).

DISCLAIMER

Q&As provide further insight into DNB's policy practice by setting out its interpretation of statutory supervisory rules. Institutions are free to opt for alternative ways in which to meet the statutory and regulatory requirements provided that they apply the comply-or-explain principle. To learn more about the status of DNB's policy statements, go to the Explanatory guide to DNB's policy statements on Open Book on Supervision.