FOCUS!

The new supervisory approach of De Nederlandsche Bank

De Nederlandsche Bank
Eurosysteem

FOCUS!

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Summary

As of 2012, De Nederlandsche Bank (DNB) employs a new supervisory approach known as FOCUS!. This brochure describes the most salient features of this new approach. How does it work, and how will it contribute to effective supervision?

FOCUS! is the culmination of a reform programme designed to make supervision more effective and more vigorous. DNB has recently been working to instil a culture of more intrusive and conclusive supervision. To achieve this, the organisational structure has also been modified. The 2011 publication *'From Analysis to Action – Progress Report on the Action Plan for a change in the conduct of supervision (Van analyse naar actie – Uitvoering Plan van aanpak cultuurverandering toezicht DNB)* set out the measures taken. One of those measures, a renewed methodology for risk analysis and mitigation, took more time to develop and is summarized in this brochure.

FOCUS! builds upon the risk methodology used by DNB in recent years, known as FIRM, but includes a number of important improvements. One of these concerns the classification of supervised institutions into five categories, each with its own risk analysis; the greater the impact of problems at a given institution on DNB's supervisory objectives, the more intensive the risk analysis. The analysis, judgement and mitigation of risks is based on insights derived from the entire spectrum, from macro-level to micro-level relationships. The method draws on macroeconomic and sectoral developments, as well as specific themes, and uses these as a basis from which to zoom in on individual risks. As part of this process, the business model and strategy and the conduct and culture of supervised institutions are explicitly assessed. This encourages supervision to focus more closely on potential sources of later problems. This focus is anchored in newly developed risk registers and assessment frameworks. Where necessary, analysis is followed by targeted action. Based on their risk profile, institutions are assigned to different supervision regimes determining the further mitigation of risks. Supervisory interventions will seek to achieve clearly defined effects without delay, with targeted attention for measuring and evaluating the effects of any action taken. Urgent problems are escalated to specialist teams. The quality assurance of the supervisory activities has been stepped up, with an important role being assigned to the new Risk Management of Supervision Processes department. Together with the various changes initiated in the supervisory framework, this renewed approach will help ensure the stability of the financial sector.

1 Introduction

DNB has introduced a new supervisory approach known as FOCUS!. Its introduction is the culmination of a reform programme that was initiated in 2010. At that time, the lessons drawn from the credit crisis were set out in *DNB Supervisory Strategy 2010-2014* and in the *Action Plan for a change in the conduct of supervision*. These lessons are reflected in an across-the-board revamping of the supervisory approach. DNB has learned from other supervisory authorities in the Netherlands and elsewhere. Best practices from the various supervisory divisions have been identified and anchored across the full spectrum of DNB's supervision.

This brochure describes the key points of the renewed approach. How does it work, and how will it contribute to effective supervision? The brochure aims to provide transparency for supervised institutions and other stakeholders. Society is increasingly demanding accountability, as also observed in the report on DNB's supervision of banks as drawn up by the Netherlands Court of Audit. This concerns above all a need for insight into the results of DNB's supervision. DNB strives to meet these demands. Accountability also means showing how DNB fulfils its mandate, which is exactly the purpose of this brochure. Raising the awareness of the supervisory approach among supervised institutions will also increase the support for supervision and foster compliant behaviour. The annual brochure *DNB Supervisory Themes* and the online *Open Book on Supervision*, which provides information on the application of supervisory laws and regulations, also contribute to this aim, and can encourage other stakeholders of financial institutions (such as members of the Supervisory Board, external auditors and shareholders) to act as 'co-supervisors'. This will boost the effectiveness of DNB's supervision.

2 Priorities in improving DNB's supervision

A good deal has been said and written about DNB's supervision in the wake of the credit crisis. We have drawn lessons from the crisis ourselves, and others have scrutinised our supervision as well. All this has been translated by DNB into a set of principles for more effective supervision:

- Looking beyond individual institutions;
- More attention for the qualitative and strategic elements in supervision;
- More intrusive and conclusive conduct of supervision;
- Better internal and external assessment and accountability.

The supervisory approach puts these principles into practice both in the risk analysis – the identification and assessment of risks to which financial institutions are exposed and the measures taken to control them – and in risk mitigation – the supervisory activities aimed at reducing problems and risks.

Looking beyond individual institutions

The credit crisis made clear that risks often go beyond individual institutions. Major risks regularly occur at several institutions simultaneously. In addition, financial institutions are closely intertwined, both with each other and with the real economy. Adequate supervision therefore demands a supra-institutional approach. This means strong coherence between macroprudential insights and developments and microprudential supervision of individual institutions. It also implies more attention for sectoral analyses, more mutual comparisons of similar institutions (benchmarking) and a focus on supervisory themes.

More attention for the qualitative and strategic elements in supervision

In the past, supervision was not only heavily focused on individual institutions, but also (too) strongly on quantitative criteria such as solvency and liquidity. While these criteria are still very important, effective supervision also demands attention for strategic and qualitative aspects. This entails a focus on two sources that are anchored more deeply within organisations: the business model and strategy of institutions, and their conduct and culture. Gaining an insight into these potential sources of later problems enables risks to be identified and addressed before they manifest themselves in the form of solvency and liquidity problems.

More intrusive and conclusive conduct of supervision
Not only the conduct and culture at supervised institutions has attracted attention, but also the supervisory culture at DNB. In August 2010, DNB outlined the measures intended to make its supervision more intrusive, more sceptical and above all more conclusive (see box for a summary). Virtually all the measures were implemented in 2011, although the renewed methodology for risk analysis and mitigation, which is described in this brochure, needed more time.

Better internal and external assessment and accountability (learning organisation)
Finally, good supervision constantly renews itself and is open to internal and external assessment and criticism. This demands transparency about the supervisory activities and (as far as possible) their impact on the behaviour of institutions, on

Action plan for a change in the conduct of supervision – summary

Organisation
- New Intervention & Enforcement department
- New Risk Management of Supervisory Processes department
- Expert Centre for Conduct & Culture
- New cross-sectoral supervisory division

Staff
- Modification of job profiles
- Intensification of training programme
- Fine-tuning of staff rotation policy
- Project aimed at raising awareness and developing required supervisory behaviour
- Changes to recruitment and selection

Accountability and transparency
- IMF Financial Sector Assessment Program (FSAP)
- Periodical analysis by Netherlands Court of Audit
- Raising the profile of supervision within DNB's operating model
- New mandate for the Supervisory Board
- Peer reviews by European supervisors

New focus in supervision
- Looking beyond individual institutions
- Financial risk departments
- Macroprudential orientation
- Business models and strategy
- Conduct, culture and governance

their solidity and integrity and on financial stability. This transparency has its limits. DNB is, for example, bound by a code of secrecy which imposes limits on the information that can be made public. Furthermore, it is often difficult to attribute behavioural changes at institutions unambiguously to supervisory activities. Despite these limitations, DNB is committed to enhance transparency about the achievements and effects of its supervision, and is open to external assessments (such as the 2011 examination under the Financial Sector Assessment Program conducted by the IMF).

3 Core elements of the supervisory approach

3.1 Objective and principles of DNB's supervision

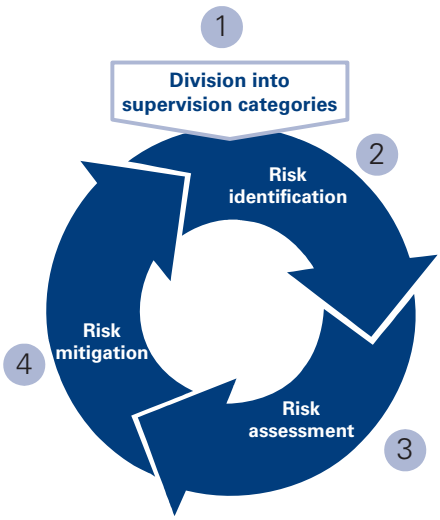
Supervisory legislation and regulations provide the formal basis for supervision of financial institutions in the Netherlands. In line with these, DNB exercises supervision to ensure strong and sound financial institutions that meet their obligations and to safeguard financial stability. DNB also ensures that the provisions of the Articles and Rules of pension funds and pension plans placed with insurance companies meet the relevant pensions legislation and regulations; this is known as material supervision. Strong and sound financial institutions must hold sufficient capital to absorb any losses and have sufficient liquidity to meet their obligations on time. Moreover, operational integrity and effective risk management are essential, and the institutions must be led by fit and proper management and boards. Financial stability means that risks are properly managed and shocks are adequately absorbed, so that they do not become a threat to the financial system (consisting of financial markets, financial institutions and the financial infrastructure) or the real economy. The objective of supervision is, as far as reasonably possible, to minimise the risk of defaults and instability. In the first instance, supervision is preventive. Intervention follows if necessary.

3.2 The supervisory approach in broad outline

Broadly, the supervisory approach operates as follows:

1. Prior to the cycle of risk analysis and risk mitigation, all institutions – individually or as a group – are divided into five categories, each with its own risk analysis intensity.
2. The risk analysis begins with an assessment of the 'risk drivers': developments in the external environment, business model & strategy, conduct, culture & governance and infrastructure & IT. This assessment helps prioritising risks from the entire gamut of prudential risks (such as market risk and interest rate risk) and integrity risk.
3. The relevant prudential and integrity risks are assessed, followed by an analysis of the capital and liquidity of the institution. The results of all the assessments

The supervision cycle



are summarised in a risk profile for the institution. Based on this profile, the institution is assigned to the appropriate supervision regime. In combination with the supervision category in which the institution has been placed, this supervision regime dictates the approach to risk mitigation.

4 Risk mitigation focuses on establishing the desired effect, without delay. The new Intervention and Enforcement department plays a key role in this.

To ensure that DNB has an adequate picture of the supervised institutions, the risk assessments are updated on a regular basis.

3.3 Supervision categories

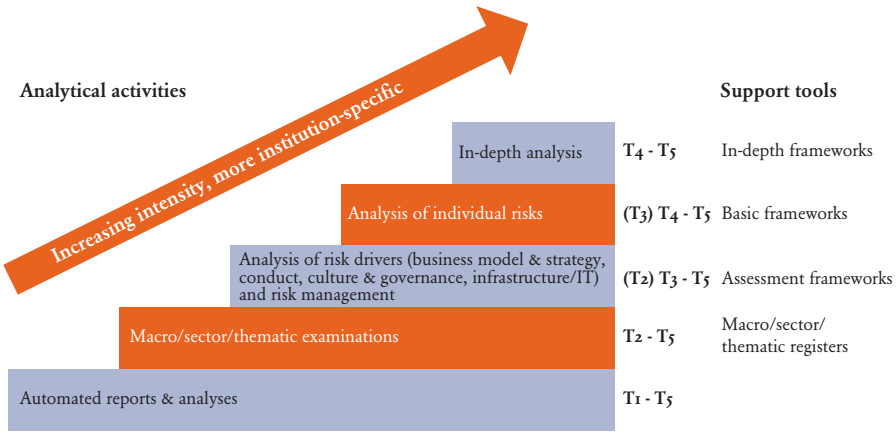
Since supervisory capacity and expertise are scarce, choices have to be made. This is done among other things by placing supervised institutions in one of five supervision categories (T1 to T5) before risk analysis takes place. The higher the supervision category, the greater the impact serious problems at or default of an institution would have on the supervisory objectives, and the deeper the risk analysis. The classification is updated each year, and in the event of significant developments between these updates (such as a change of licence or rapid growth of an institution), an interim assessment is carried out to determine whether the classification should be adjusted. In adopting this approach, DNB is in the good company of a number of supervisory authorities in other countries, including the Australian APRA and the British FSA.

The systemic importance of an institution is an important criterion in deciding on the appropriate supervision category. Serious problems at a systemically important institution would have a major impact on the ability of the financial system to continue performing its core activities, such as payments, lending and risk transfer. Consideration is also given to aspects relating to the solidity and integrity of an institution, which are not always adequately expressed in the financial stability score. Examples include the risk of infringements of integrity (such as non-compliance with sanctions) which by their nature could result in major financial loss or reputational damage. Some institutions may have little individual relevance for the supervisory objectives of DNB, but a group of similar institutions as a whole can have a great deal of relevance. These institutions are then placed in a higher supervision category as a group.

Each supervision category has its own basic programme of analytical activities. Depending on the specific circumstances, it is possible to deviate from these activities and to perform a deeper analysis of some or all aspects. For institutions placed in category T1, the analysis is in principle limited to an (automated) analysis of statutory financial criteria, such as the funding ratio of pension funds and the solvency ratio of insurers. These institutions are only occasionally selected for inclusion in a thematic examination. Automated reports and analyses are also the main sources of information for institutions placed in category T2, but institutions in this category are included in DNB-wide thematic projects, just as institutions in the higher categories. In special situations, an analysis of risk drivers is also carried out for T2 institutions. Institutions in category T3 and above are always assessed with respect to business model and strategy, culture, conduct and governance, infrastructure and IT, as well as general risk management. For institutions in categories T2 and T3, the risk analysis in principle relates to a group of institutions with similar characteristics. A supervision plan is drawn up and the relevant risks are selected for each group as a whole. In category T3, institution-specific risks can also be incorporated in the supervision plan. Notwithstanding the group-based approach, it may emerge from a group analysis that the risk profile of an individual institution deviates from that of the group as a whole. This can lead to an intervention targeting that institution.

In principle, analysis of individual prudential and integrity risks is only conducted at institutions in categories T4 and T5. A supervision plan is drawn up for each institution in these categories, geared to the individual institution. The main difference between supervision categories T4 and T5 lies in the complexity of the institutions and the associated risks, and therefore in the depth and intensity of supervision.

Supervision category and supervision intensity



3.4 Top-down work practices

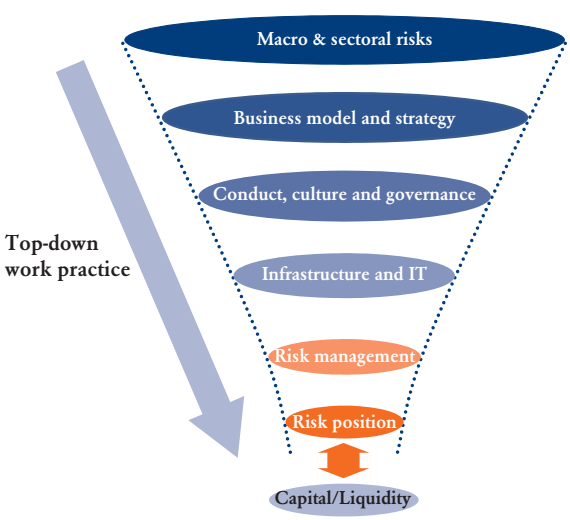
A complete process of risk identification and assessment begins with the external environment and steadily moves towards an assessment of the individual prudential and integrity risks. During this process, an increasingly clear picture of the most relevant risks emerges. Supervisory attention will naturally focus on those risks that jeopardise the continuity of an institution.

The main external threats are made accessible to the supervisor using risk registers – a macro-register, sector registers and a theme-based register. The macro-register contains the main macroeconomic risks for the Dutch financial sector. This register is based on the Overview of Financial Stability in the Netherlands, which is published every six months by DNB. Clear priorities are set and for each risk a description is given of (i) which sectors are affected; (ii) how the risk can affect an individual institution; and (iii) which risk indicators can help in assessing the vulnerability of the institution. For sector-specific risks (e.g. the implementation of Solvency II), a sector register is maintained for each sector/division, again with a clear description of the relevant institutions and the risk areas that are affected. The theme-based register lists the risks that can emerge from thematic projects, i.e. in-depth examinations of a specific risk area carried out at selected institutions. Each year, DNB publishes the themes it wishes to address in the coming year. For 2012, the main themes will be restoring financial buffers, the sustainability of business models, better risk management, supervision of governance, integrity of the financial sector and better data quality (see *DNB Supervisory Themes 2012*, http://www.dnb.nl/en/binaries/711325_ThemaDNBtoez12WEB_tcm47-267717.pdf).

Against the backdrop of the main external risks, DNB looks at the business model and strategy of institutions, at their conduct, culture and governance, and at their infrastructure and IT. A new Culture, Organisation and Integrity department specifically targets the conduct and culture of financial institutions. The analysis of these elements is forward-looking in nature, and is essential in order to obtain a clear picture of future risks. These elements also offer pointers for the link between the macro and micro-approach. An example might be a situation where several institutions simultaneously assume they are able to attract substantially more domestic savings. From a macro-perspective, the conclusion might be that this strategy will not be achievable for some or all of these institutions. The risk management at an institutional level is also assessed in this phase. This assessment looks at general aspects, such as the involvement of senior management and the Supervisory Board in establishing the institution's risk attitude. Overall, this thorough analysis of risk drivers makes clear which individual risk groups have the greatest potential impact and must therefore be given priority in the subsequent steps.

Depending on the basic programme, the follow-up analysis focuses on the individual prudential risks – credit risk, market risk, matching/interest rate risk, operational risk, underwriting risk, liquidity risk – and integrity risk. Here again, a top-down procedure is applied. The risk assessment starts from the impact of the risk drivers. If the impact on a specific risk is limited, no further analysis is carried out. If the risk is potentially significant, however, an assessment is made of the quality of the control of the specific risk and of the risk position.

Top-down analysis



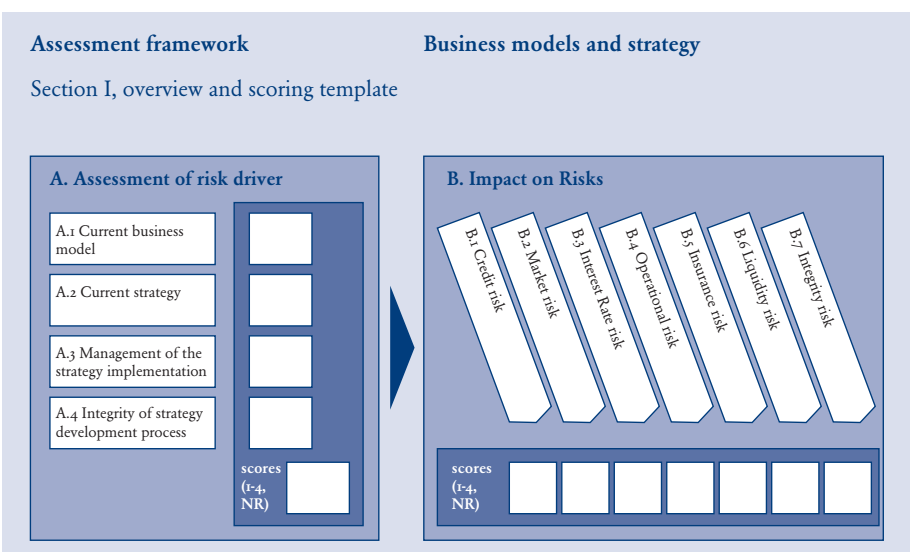
Controls will never be able to eliminate the possibility of residual risks entirely. In fact, residual risks are sometimes deliberately chosen as a source of profit. As these residual risks could lead to an acute loss of capital or liquidity, the final step in the analysis is to establish whether the institution's capital and liquidity are adequate. Not just at present, but also in the medium and longer term and in a number of stress scenarios. Institutions must hold sufficient capital and liquidity to cover their current risks, and must have a solid capital and liquidity plan guaranteeing the presence of sufficient capital and liquidity in a wide range of foreseen and unforeseen circumstances.

Notwithstanding the top-down approach, information and signals received bottom-up by the supervisor can also be fed into the process at any point. These signals are generally unexpected and are an essential addition to the systematic top-down analysis by DNB.

3.5 Assessment frameworks and scores

A supervisor cannot operate without the proper tools. In FOCUS! the risk analysis is supported by a range of assessment frameworks, a number of which have been newly developed:

Risk driver scoring template for 'Business models and strategy'



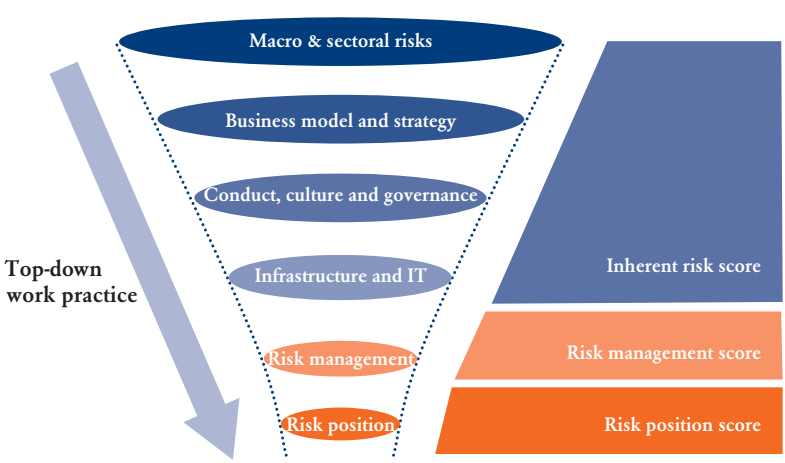
- for assessing the business model and strategy, conduct, culture and governance, and infrastructure and IT;
- for assessing the individual prudential and integrity risks;
- for assessing the general risk management and the adequacy of capital and liquidity.

The assessment of the risk drivers and the prudential and integrity risks is recorded on risk cards. Action scores can also be added to indicate where action is required.

The assessment frameworks for the risk drivers have a uniform design, in which both the risk itself and its impact on the various prudential and integrity risks are assessed. The same applies for the macro and sectoral risks that are included in the various registers. This approach makes the consequences of the risk drivers for the various prudential and integrity risks visible, in so far as those consequences can be foreseen without an in-depth analysis of the risks themselves. The British FSA makes use of a comparable practice.

The assessment frameworks for the prudential and integrity risks also have a uniform design. For some of the prudential and integrity risks, an in-depth assessment framework is used in addition to the basic assessment framework. While the basic frameworks are uniform, in-depth frameworks make it possible to look in more detail at risk aspects which are, for example, relevant for one specific sector. The assessment of individual prudential or integrity risks is expressed in three risk scores: the inherent risk score, the risk management score and the risk position score. The inherent risk score summarizes the impact of the various risk drivers on the risk in question. This approach ensures that consistent attention is given to qualitative and strategic elements in the supervision. The risk management score

Assessment of prudential and integrity risks in three scores



reflects the assessment of the quality of risk management, while the risk position score expresses the 'quantity' of the risk in question.

The various assessments of an institution are combined to create the institution's risk profile and are recorded on a score card. The uniformity of frameworks and scores ensures a consistent approach and assessment across institutions and across sectors. The uniform recording method enables sector analyses and benchmarking, and supports the transfer of cases.

3.6 Supervision regimes

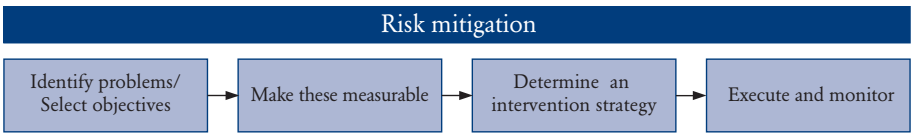
Risk analysis is not an end in itself, but is ultimately about preventing or mitigating risks. To this end, DNB's approach to supervision makes a distinction between four regimes: low, neutral, high and urgent. Each institution is assigned to one of these supervision regimes, based on an assessment of the chance that the identified risks within an institution could harm DNB's supervisory objectives. The risk profile of the institution forms the basis for this. New institutions entering the market are placed in a high supervision regime for the first one or two years, depending on the complexity of the institution.

The supervision regimes set the tone for the risk mitigation. No substantial intervention is needed in the lowest regime. Neutral supervision is the basic regime of regular supervision; risks or infringements may occur, but mitigating them is straightforward and transparent. In the high supervision regimes (potentially) serious risks are at hand, and a formal risk mitigation project is always drawn up. In the urgent supervision regime the risks are even such that immediate intervention is required, and all possible measures are used to mitigate the risk. In principle, the Intervention and Enforcement expert centre has operational control in the highest supervision regime. Supervisory measures are intended to lower the risk profile and supervision regime of the institution to 'neutral'. The content of the mitigation activities in a supervision regime varies across the supervision categories: the measures required and their complexity will be greater for institutions in the higher categories.

3.7 Targeted risk mitigation

Risk mitigation is addressed on a project basis within FOCUS!. All mitigation activities are based on a clear and in-depth picture of the problem and the underlying cause, the supervisory strategy and the intended effect. This applies across the board, from simple activities such as conducting a supervisory interview, through imposing formal measures, to larger and more complex supervision projects that

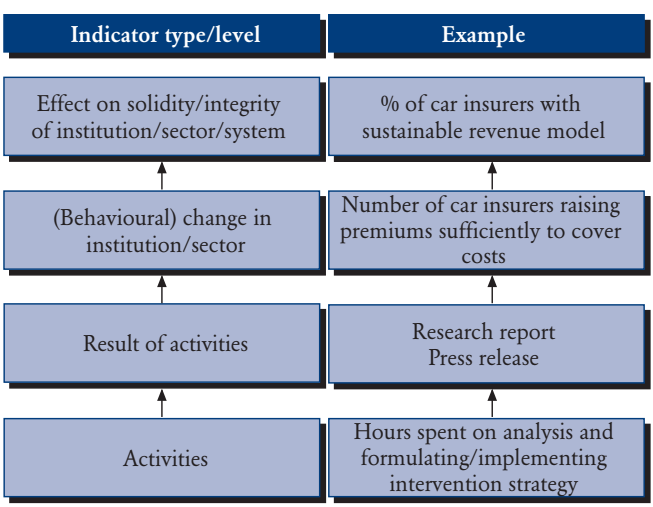
The four risk mitigation steps



require a detailed risk mitigation plan. To facilitate monitoring, and where necessary an adjustment or intensification of the supervisory activities, explicit timelines are indicated within which the effect must be achieved.

Effect measurement and evaluation based on preselected performance indicators play a central role in risk mitigation. At the start of a risk mitigation plan, it will be made explicit how the effects will be measured and at what point the mitigation will be regarded as successful. It is not always that straightforward. Sometimes, the effect of intervention relating to the solidity or integrity of an institution and the stability of the financial system is not easy to observe clearly and in time. The desired changes may for example only become visible in the longer term. Moreover, supervision is only one of the factors that determine the solidity of institutions and the stability of the system. Demonstrating effective prevention is even more difficult in terms of impact measurement and evaluation: how can it be shown that

Chain of effects and indicators

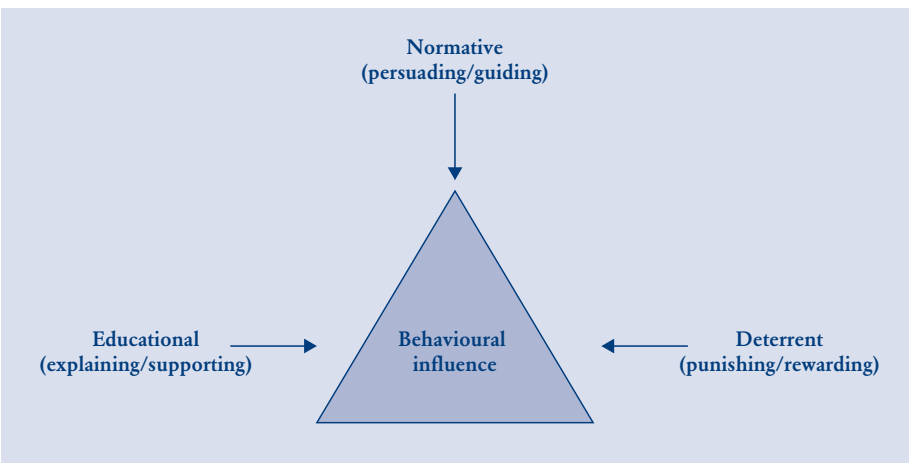


problems did not occur because of supervision? Sometimes, describing the impact in qualitative terms may be an appropriate alternative.

When deciding on an intervention strategy a choice will be made from three different strategies for influencing the supervised institution: educational (explaining and/or supporting), normative (persuading and/or guiding) and deterrent (punishing and/or rewarding). In some cases, explaining the background to a standard or norm suffices, while in others it will be necessary to impose a sanction. A choice will also have to be made between a group or individual approach; formal measures will always be targeted at an individual institution. Interventions are geared to the specific situation, cause and severity. In extreme cases, a solution will have to be found on the same day. In the vast majority of cases, relatively light interventions will suffice and the use of formal enforcement instruments will not be necessary. Choices made are subject to peer review by colleagues, and the choice of enforcement instruments to be used is based on the enforcement policy of DNB and the Netherlands Authority for the Financial Markets (AFM).

Project progress also plays a role in determining the choice of intervention: the more serious and long-lasting the undesirable situation is, the more intensive the intervention. When appropriate, a scenario will be constructed at the start of the mitigation process consisting of increasingly severe measures. For example, if explaining a standard or norm has no effect, the next step may be to ask the institution to produce a plan for resolving the issue. If this is still not sufficient, a cease and desist order under penalty can be imposed, a director can be replaced or the

Three possible influencing strategies



institution's licence can even be revoked. The new Intervention and Enforcement department at DNB plays a key role in the intervention process. The department has three main tasks in the event of problem situations: issuing non-committal or binding advice on the intervention strategy, coordinating formal measures and taking operational control in complex problem situations. If there is a reasonable chance of a formal measure or an incident under the Dutch Financial Supervision Act *(Wet op het financieel toezicht / Wft)*, it is mandatory to call in the department to issue binding recommendations. In exceptional cases, operational control is transferred to the department. This procedure guarantees adequate escalation and ensures the optimum deployment of available capacity and expertise.

3.8 Quality control

The success of a supervisory approach depends on adequate application. As part of the Action Plan for a change in the conduct of supervision, DNB set up the Risk Management of Supervision Processes department. This department verifies whether supervision is being conducted in accordance with the defined supervisory approach and whether it produces the desired results. This quality control puts DNB in good company with a number of supervisory authorities in other countries, including the Australian APRA and the FSA in the UK, which have traditionally devoted a good deal of attention to the application, development and maintenance of their supervisory methodology.

The new supervisory approach is not set in stone. The various elements of the supervisory approach offer scope for flexible application. Moreover, this approach will be worked out in more detail as time goes by. The environment within which financial institutions operate will change, as will the institutions themselves and the public expectations about what financial supervision should deliver. These developments have led to adaptations in the supervisory approach in the past, and will continue to do so in the future. DNB is therefore constantly focused on further improving its supervision. The Risk Management of Supervision Processes department plays a special role in this process by monitoring and if necessary initiating changes in the supervisory methodology.

Constructive criticism makes one stronger. This also applies to DNB. External assessment, feedback and criticism make our supervision more effective. The *Action Plan for a change in the conduct of supervision* states that more use will be made of independent assessments of DNB's supervision. Since the Plan was published, evaluations have been carried out by the Netherlands Court of Audit, the IMF and international supervisory authorities. The Netherlands Court of Audit concluded that the supervision exercised by DNB meets the required standards of impartiality, functional separation, expertise and integrity, but stated that there could be more

transparency regarding the achievements and effects of DNB's supervision. The Court of Audit also recommended that the new supervisory approach be evaluated at an early stage.

The IMF published the outcomes of its Financial Sector Assessment Program (FSAP) for the Netherlands in June 2011. As part of this Program, experienced experts investigate the stability of a country's financial sector and the quality of its supervision. The IMF concluded that supervision in the Netherlands fully meets practically all international standards. The Netherlands also scored better than other countries which had recently undergone an assessment. This positive assessment was accompanied by a number of recommendations, including a suggestion that the supervisory approach be intensified. The practice described here fully meets this recommendation. Other recommendations related to adequate availability of financial data, safeguarding independence, supervision of (international) groups and strengthening the crisis management apparatus. In the area of integrity the IMF, via the Financial Action Task Force on Money Laundering, evaluated the Dutch system for preventing and combating money-laundering and the financing of terrorism. The IMF's recommendations in both these areas have been or will be incorporated in DNB's work programme. Finally, the European Insurance and Occupational Pensions Authority, examined compliance with the protocol on collaboration between supervisory authorities in cross-border activities, and the European Banking Authority examined compliance with the provisions on cooperation deriving from the European Capital Requirements Directive and the functioning of supervisory colleges. In both cases, DNB received a positive assessment.

All in all, DNB will continue to improve its supervision and benefit from external assessments and evaluations. The renewed supervisory approach will be evaluated in 2013.

4 Developments in the supervisory framework

The impact of supervision is not only determined by the supervisory approach, but also by the regulatory framework within which financial supervisors operate. In its *Supervisory Strategy 2010-2014*, DNB set out the main lessons drawn from the credit crisis for the supervisory framework. The Dutch government drew comparable lessons in its outlook on the future of the financial sector. The implementation of these lessons into regulation has begun, with input from DNB. To a greater extent than in the past, these regulations are drawn up at a European level.

The tightening of the solvency and liquidity requirements is well under way. For the banking sector, the European Capital Requirements Directive was reinforced in 2011, but the major tightening of standards will take place when the global Basel III framework is incorporated in the regulations via a European Directive/ Regulation ('CRD IV'). The Financial Stability Board has developed a framework for systemically important banks, to which DNB has signed up. Important elements include higher capital requirements as the systemic importance of an institution increases, the creation of an effective set of instruments for enabling a failing institution to be wound up in an orderly fashion, and the formulation of recovery

DNB Supervisory Strategy 2010-2014 : lessons drawn from the credit crisis with respect to the supervisory framework

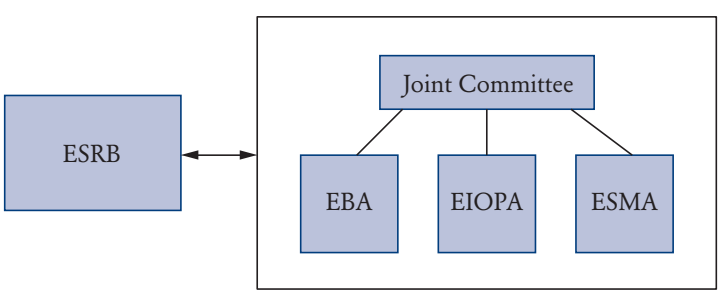
International
- Strengthening of solvency requirements for banks, insurers and pension funds
- Strengthening of macroprudential supervisory framework
- Strengthening of European supervision of cross-border institutions
- Reappraisal of the scope of supervision

National
- Continuation of Twin Peaks model
- Strengthening the crisis instruments
- Improving the deposit guarantee scheme
- Limiting the liability of financial supervisors

and resolution plans. The fifth impact study for a new, risk-based supervisory framework for insurers, Solvency II, was completed in early 2011. Based on the results, the European Commission, Member States and the European Insurance and Occupational Pensions Authority are working on the further development of the framework, which is scheduled to be introduced in 2014. For the pensions sector, the Dutch Minister of Social Affairs and Employment outlined the planned tightening of the Financial Assessment Framework (FTK) in 2010. The introduction of these changes depends on the development and implementation of a supervisory framework for the intended new contracts, which is still being debated. The European Commission has also expressed the intention of issuing a proposal to amend the European Pension Funds Directive (which dates from 2003) at the end of 2012.

A new European supervisory structure, the European System of Financial Supervision (ESFS), came into operation on January 1, 2011. The microprudential pillar of the ESFS is made up of three European authorities: the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA). These authorities have more extensive tasks and authorities than their predecessors. Among other things, their role entails the formulation of binding standards for the conduct of supervision and ensuring the best possible functioning of colleges of supervisors. The ESFS also has a macroprudential pillar, formed by the European Systemic Risk Board (ESRB). The ESRB identifies risks to the stability of the financial system, both at EU level and within Member States, and issues warnings and recommendations on the basis of its findings. This has strengthened the macroprudential architecture. DNB is an active member of EBA, EIOPA and ESRB.

The new European supervisory structure



Macroprudential supervision Microprudential supervision

The credit crisis made clear that unregulated market players such as hedge funds and private equity can also pose a threat to the stability of the financial sector. In recognition of this, the Alternative Investment Fund Managers Directive (AIFM Directive) was adopted in 2011. Among other things, the AIFM Directive provides an extensive framework of prudential rules for these market parties. Member States must have incorporated this Directive into their national legislation by 2013. Additionally, the European Credit Rating Agencies Regulation came into force in 2010, imposing requirements on credit rating agencies. The corresponding supervision is conducted by ESMA.

Finally, progress has been made in adjusting the domestic institutional framework. In close collaboration with DNB, the Dutch government has tabled the Intervention Act *(Interventiewet)* in Parliament, which would enable more rapid and effective intervention in the event that a bank is about to fail. DNB would for example have the authority to transfer deposits, (certain) assets or liabilities or shares of an institution to a third party or to an intermediate bank if the institution is in danger of collapsing. The Dutch deposit guarantee scheme is also being revised in two ways. First, a fund will be set up in 2012 from which payments can be made under the deposit guarantee scheme in the event of a bank failure. The fund will be financed out of risk-dependent contributions, which will provide an incentive to banks to behave in a less risky way. In addition, the term within which payments are made under the deposit guarantee scheme will be shortened.

The above changes in the supervisory framework, together with DNB's supervisory approach outlined in this brochure, will contribute to a stable financial sector.

Background documents

Australian Prudential Supervision Authority (2010), The APRA Supervision Blueprint
DNB (2012), Supervisory Themes 2012
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IMF (2011), Kingdom of the Netherlands – Financial System Stability Assessment
IMF (2010), The making of good supervision: Learning to say 'No', IMF Staff Position Note, May 18 2010
Netherlands Court of Audit (2011), DNB's supervision of bank stability
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