AUDIT REQUIREMENTS FOR INSURER DATA RETURNS

Reserve Bank of New Zealand Consultation Paper

SUBMISSION

From

ICNZ Insurance Council of New Zealand

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1. INTRODUCTION

The Insurance Council of New Zealand (ICNZ) thanks you for the opportunity to provide a submission on this consultation paper on Audit Requirements for Insurer Data Returns.

This ICNZ submission has been prepared after consultation with ICNZ members and represents a general insurance industry consensus. We understand that a number of ICNZ members will be making individual submissions and while on some issues they may present additional positions, in the main the industry is fully behind this submission.

2. INSURANCE COUNCIL OF NEW ZEALAND

ICNZ is the industry representative for fire and general insurers in New Zealand. We aim to assist our members in the key areas that affect their business through effective advocacy and communication.

ICNZ currently has 27 members who collectively write more than 95 percent of all fire and general insurance in New Zealand. ICNZ members, both insurers and reinsurers, make up a significant part of the New Zealand financial services system. ICNZ members currently protect more than three quarters of a trillion dollars' worth of New Zealanders' assets.

ICNZ plays an active role in representing the insurance industry. Our members are licensed under the Insurance (Prudential Supervision) Act 2010 ("IPSA") and are signatories to the Fair Insurance Code, which requires our members to act ethically. We also perform an important role in informing and educating consumers about key insurance issues and risks.

3. HIGH LEVEL COMMENTS

(i) Proposal locks in a permanent layer of unnecessary cost

Insurers acknowledge the need for accuracy and timeliness in all reporting to the industry regulator. All insurers have established detailed processes for extracting information from their IT systems and reviewing this data through various levels of sign off process. The data reporting process in New Zealand is in its infancy and both the industry and the regulator are still coming to grips with definitions, guidelines and how to extract the correct data in a single template format that does not match any of the individual insurers internal reporting.

This proposal, in seeking accuracy in the reporting process by imposing audit requirements on all insurers for annual data returns and upgrading the solvency return audit requirements, locks in a permanent layer of unnecessary cost into the regulatory process. Clearer definitions and guidance along with greater engagement with insurers can fix the problems without imposing a permanent costly audit requirement on insurers.

(ii) Risk-based audit approach should be considered

Insurers believe in certain circumstances, audits will be justified where individual insurers are consistently misreporting and making mistakes with data. In these circumstances audits could be undertaken. In this way, a risk-based audit approach will target those who are consistently getting data wrong and across the industry will incentivise accuracy. It will also mean insurers who are consistently reporting to high levels of accuracy are not required to undertake high cost audits because others are failing to provide accurate returns.

(iii) Suggestion for improving accuracy

In order to improve the clarity of the insurer returns, it is suggested that RBNZ provides a simple template for insurers to show how their insurer return reconciles to their financial statements or solvency return. We would suggest that this should be requested only at a high level for the following data:

- Gross written premium
- Reinsurance premiums
- investment income
- gross claims paid
- liabilities

The requirement for insurers to reconcile their data to their published financial accounts would impose a discipline which should have a positive effect on improving the accuracy of the data.

(iv) Need for clear guidance and definitions

Insurers acknowledge that data reporting is an area which can be open to errors and mistakes. Insurers often find this relates to ambiguous guidance and unclear definitions and a tidy up in this area will promote more accurate data returns. Timely notification of errors found by RBNZ can also improve accuracy and will ensure similar future mistakes are not made. Feedback should also include that no issues were found with the Insurer Return so the insurer is not left wondering.

The consultation paper outlines a number of steps which the bank proposes to raise the quality of the data. One of the steps is the publication of full definitions and guidance for completing returns. Insurers believe that this should be the first step before any consideration is given to imposing costly audit procedures on any of the data reporting to RBNZ.

One insurer gave an example of how their classification of Defined Benefit was resolved following feedback and guidance which has prevented future problems. Better definitions and guidelines can eliminate the need for audits.

Publication of feedback on common errors (without identifying at fault insurers) on a regular basis would assist all insurers with their Insurer Return preparation. This could be done six monthly, following each round of data collection.

if errors are occurring consistently as a result of poor guidelines or obscure definitions, fixing these problems may mean a move to auditing data returns is not necessary.

(v) Validation of data within the spreadsheet

RBNZ should review the entire data reporting spreadsheets to ensure that the figures cross add and down add accurately and summary totals agree to the detail.

(vi) Need for RBNZ to recognise materiality thresholds

ICNZ members report that many of the problems RBNZ come back to them with, are immaterial and well below the level that would cause issues with the reports. RBNZ should review its definition of materiality to ensure that minor errors are not captured. Errors of several hundred thousand dollars are not regarded as material in the context of the full insurer returns, however even larger insurers are being asked to restate figures when errors of this magnitude are found.

(vii) Cost of "reasonable assurance" audits

ICNZ surveyed members with GWP above $50 million to establish what the cost of their limited assurance audit for their solvency return was at the last financial year end. The aim was to provide an indication of potential cost for a higher level" reasonableness assurance audit" that is proposed for the insurer return and an indication of the potential additional costs for the reviews of the insurance solvency return which will take place twice a year. Twelve member companies reported a total cost of $410,500 in the last financial year. If the cost of the audits for medium companies every three years is added to this figure it is likely that the "reasonable assurance" audits would cost the industry well in excess of half a million dollars per annum. The industry does not accept that costs of this magnitude can be justified in order to improve the accuracy of the data returns.

4. PROPOSED WAY FORWARD

Insurers agree with the drive by RBNZ to improve the accuracy of data, however this needs to be done in a structured way which minimises the opportunities for errors and targets those insurers that continue to make mistakes. ICNZ believes that the focus in improving data return accuracy should be a three-step process in the following order of priority:

- Improvement of fuller definitions and guidance for completing returns by RBNZ
- Improved validation within worksheets that make it difficult to enter inaccurate totals
- Introduce audit requirements for insurers who continually return inaccurate data.

ICNZ and its insurer members are happy to provide members for a joint working group with RBNZ to develop the improved guidance and definitions and provide input into developing improvements in the reporting worksheets.

The focus for the second part of this submission will be on the individual questions posed in the consultation document.

5. CONSULTATION PAPER QUESTIONS

1) Do you support the idea of introducing an Insurer Return audit/review requirement?

Insurers do not support the need for the introduction of the audit/review requirement for Insurer Returns. The cost is not justified by the benefits and insurers' Boards and

Management use the same data for risk management purposes and are comfortable with the current level of review undertaken.

However, if an audit/review is to be imposed on the industry, insurers would only support this for those insurers who are consistently misreporting or providing inaccurate data. Only these insurers should be liable to undertake a limited audit/review of their Insurer Return.

2) ***What would your organisation expect the audit fee to be for***
    a) ***A reasonableness audit***
    b) ***A limited assurance review***

Our twelve members with GDP over $50 million have reported that the cost of their solvency limited assurance review in aggregate totals $410,000 pa. It is expected that adding the medium sized members who would require an audit every three years would take this figure to over half a million dollars per annum. This cost excludes the extra costs insurers would incur for system costs and staff and management input to the audit as well which could well double the cost.

This is a guide to the potential cost to the industry of an audit/review of the Insurer Return, however our members advise this cost can only be accurately obtained from the audit firms.

3) ***How effective do you think an audit would be in identifying deficiencies in the processes and systems contributing to the insurer return? Please answer separately in respect of***
    a) ***A reasonableness audit***
    b) ***A limited assurance review***

Insurers have already identified deficiencies in processes and systems that contribute data for the Insurer Return, following feedback from RBNZ over the period the returns have been requested. An audit would provide little if any additional benefits.

4) ***Please discuss the timeframes that you believe would be reasonable for the remediation of systems and processes identified as deficient by an audit.***

This is a difficult question to answer without knowing what the major issues of concern are. However, if there are significant levels of data inaccuracy that require IT system changes or process revisions, these could take twelve to eighteen months to complete. Insurers face ongoing demands for data that require constant changes and upgrading of their IT systems, such as the FENZ and EQC changes currently being scoped. These need to be worked around the ongoing business initiative IT programmes which are ongoing at the same time.

5) ***To what extent do you believe the time to complete the insurer return will be impacted if it is subjected to***
    a) ***A reasonableness audit***
    b) ***A limited assurance review***

This would depend largely on the audit resources available and the scope of the audit. This question is best directed to the audit firms.

6) ***How much lead time would you require from notification of the requirement to implementation should the RBNZ decide to impose an Insurer Return audit/review requirement?***

This needs to be addressed to audit firms. Has the Bank developed guidelines for auditors?

7) ***What types of insurers should be in-scope for an Insurer Return audit/review and why?***

As mentioned above, ICNZ members believe the Bank should adopt a risk based approach to audits and only those insurers that have consistently inaccurate data returns should be required to undertake an audit.

The Bank has correctly identified that the focus should be on large and medium insurers.

8) ***How frequently should an audit/review of an insurer return be performed (given one is required)?***

Audits/reviews should be undertaken on a risk basis, based on the history of accuracy of the returns filed.

Does your answer differ by size and/or nature of the insurer, or by level of assurance provided?

No.

9) ***Have you identified any benefits and costs (other than those listed in the introduction) of introducing an audit requirement for the Insurer return?***

In addition to the actual cost of the audits which are estimated to be around half a million dollars, there will potentially be very large costs associated with systems and process changes.

Insurer Solvency Return

10) Has the existing audit/review of the Insurer Solvency Return been beneficial in improving the quality of the data submitted?

Some members report that the audit proved useful in the early stages as it assisted them to understand or make informed guesses about the standards guidance, however more recently the audit has proven not to be so beneficial.

helpful. Most members indicated they have had very little feedback on their Solvency returns following the audit/review. They would expect to maintain the same quality of data whether an audit requirement is imposed or not.

11) What would your organisation expect the audit fee to be for
a) A reasonableness audit of the solvency return?
b) A limited assurance review of the solvency return?

See the answer to 3 (viii) and 5 (2) above,

12) How can a greater degree of assurance be obtained with respect to the Catastrophe Risk Charge?

The audit itself doesn't necessarily provide a greater degree of assurance, given that auditors are not specialists at risk modelling. This is even difficult for the Approved Actuary. Different results could be obtained by different actuarial professionals based on varying assumptions. What would improve assurance is greater guidance from RBNZ about specific models and the approach to calculating the Catastrophe Risk Charge. In this respect, ICNZ is willing to assist bringing together a working group of industry specialists to look at improving the guidance in this area.

General

13) Do you see any difficulties in attracting assurance professionals to perform a reasonable assurance audit of returns to the RBNZ, e.g. with respect to their capacity to evaluate data systems and infrastructure?

This is a question that is better directed to the audit firms. Insurers do have some concerns about the audit firm resources available to complete audit in a timely manner, especially at June and December year ends.

14) Do you have any other comments that you would like to make?

The introduction of IFRS 17 will impact insurers from 2019 (for early adopters) and 2020 for comparatives. Insurers will be faced with large changes to data collection and reporting systems and inevitably these will follow through to the Insurer and Solvency Returns. Requiring insurers to focus time and cost on audit requirements at this stage is not warranted unless the individual insurer's data returns are consistently poor quality.

6. CONCLUSION

ICNZ and its members are strongly of the belief that imposing audits on insurers for Insurer Returns would be a costly and unnecessary move. We do concede that where data returns are consistently inaccurate, the Bank should be entitled to impose an audit obligation on these insurers until the returns accuracy is up to standard.

ICNZ has also presented a number of suggestions to assist the Bank with bringing together industry working groups to help develop meaningful guidelines and definitions for data returns and to assist with developing guidance for calculating the Catastrophe Risk Charge.

Please contact us if you require further information on any of these points.

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