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Financial Services Council of New Zealand
Level 33, ANZ Centre,
23-29 Albert St, Auckland 1010
P: +64 9 985 5762
E: fsc@fsc.org.nz
www.fsc.org.nz

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Adrian Allott, Senior Adviser
Prudential Supervision Department
Reserve Bank of New Zealand

By email: Adrian.allott@rbnz.govt.nz

Feedback: **Audit requirements for insurer data returns**

The Financial Services Council of New Zealand Incorporated (**FSC**) thanks the Reserve Bank of New Zealand (**RBNZ**) for the opportunity to provide feedback on audit requirements for insurer data returns. This topic is highly relevant to our members and we are supportive of continued consultation about data quality improvement initiatives.

The FSC represents New Zealand's financial services industry having 32 members at 15 December 2017. Companies represented in the FSC include the major insurers in life, disability, income, and trauma insurance, and some fund managers and KiwiSaver providers plus law firms, audit firms, and other providers to the financial services sector.

Our submission has been developed through consultation with our members, and represents the views of our members and our industry. For depth, there are instances in the 'Specific Responses' section where we have included a range of member views. Our intent in doing this is to highlight the material concerns of our members and open the door for continued conversation with the RBNZ. We acknowledge the time and input of all our members in contributing to this submission.

The intent of the proposed requirement is clear – improving data quality to enable improved market discipline and regulator oversight. The FSC strongly supports initiatives that are designed to deliver:

1. Strong and sustainable consumer outcomes;
2. Sustainability of the financial services sector; and
3. Increasing professionalism and trust of the industry.

Therefore, we support the RBNZ's intent to drive greater market discipline, which will in turn build the sustainability of the financial services sector.

However, our view is that the proposed requirements in the Consultation Paper add material cost with little benefit, and that there are better ways to improve the consistency and delivery of data from some market participants. Recognising that preventative controls and process-improvements are generally simpler and more cost-effective than detective controls (such as audits), we recommend prioritising improvements to the Insurer Returns process and forms instead.

This focus on getting the data correct up-front, together with a more targeted corrective approach (for example, tighter enforcement for insurers who do not adhere to the standards expected by RBNZ) will bring a better balance of cost/benefit than the one-size fits all approach proposed in the Consultation Paper.

We therefore submit that there should be **no extension of the current assurance requirements** until such time as a preventive/corrective approach has been tested and results assessed. Our specific responses to the individual consultation questions continue on pages 3-6.

As always, we are interested in discussing our submission further and working with RBNZ to find industry-solutions to this issue. Please contact me on 021 0233 5414 or richard.klipin@fsc.org.nz.

Yours sincerely

Richard Klipin

Chief Executive Officer

Specific Responses

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

No. In respect of the solvency return and submission, the current requirement for a non-audit assurance engagement is appropriate and proportionate.

In respect of the insurer data returns, we consider the costs of an audit/review requirement outweigh any potential benefit. Such costs although initially absorbed by the insurer, would eventually be felt across the industry and by consumers.

Further, our members note the reference in the Background section of the consultation paper to the publication of data at aggregate and company level. We have concerns regarding the publication at company level as given the size of the New Zealand market there is potential that anonymity would not be maintained. For this reason, any data the FSC collects from our members is made public at an aggregate-level only.

2. What would your organisation expect the audit fee to be for

a. a reasonable assurance audit of the Insurer Return?

b. a limited assurance review of the Insurer Return?

Our members advise that audit fees are already high, and that extra auditing will add extra time, complexity and fees. Estimates range from $20,000 to more than $135,000. Early indications are that the fee for a reasonable assurance audit of the Insurer Return will be in excess of the current fee for the limited assurance audit of the Insurer Solvency Return.

3. How effective do you believe an audit requirement would be in identifying deficiencies in the processes and systems contributing to the Insurer Return? Please answer separately in respect of

a. a reasonable assurance audit, and

b. a limited assurance review.

Insurers have their own risk management programmes which identify deficiencies, and our members do not consider that additional external audit is necessary. Our view is that the insurer should determine whether any deficiencies identified are material and need to be remediated based on its risk management framework after considering the cost of any remediation.

Our members have told us that deficiencies in the design of the Insurer Return itself are contributing to inconsistent data across the industry. The information requested from RBNZ as part of the Return process is typically in a form that insurers do not produce data in, making it difficult to supply the information mandated by the Return. A potential solution to this issue is to gather input from the industry on the adequacy and appropriateness of the Insurer Return process itself, with a view to resolving some root issues before considering any assurance activities.

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

Timeframes would vary depending on the remediation required and the size and scope of impacted systems and processes.

5. To what extent do you believe the time to complete the Insurer Return will be impacted if it is subject to
a. a reasonable assurance audit?

b. a limited assurance review?

The time required will increase due to the additional step in the process. With time comes cost and therefore this additional step would add extra cost to the industry, with such cost either being absorbed by the insurer or passed on to the consumer.

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 depends on the complexity of the requirements, and one FSC member estimates no less than 12 months.

Another member notes that, as the information in the Insurer Return will need to change with the implementation of IFRS 17, if the RBNZ proceeds with any audit/review requirement, this should not be imposed until after the IFRS 17 related changes have been made.

7. What types of insurers do you believe should be in-scope for an Insurer Return audit/review requirement, and why?

As stated before, we disagree with the introduction of an Insurer Return audit/review requirement. However, for fairness and consistency, if the requirement is introduced, then all insurers should be in-scope. Alternatively, RBNZ could consider limiting the requirement for audit/review to those insurers that are known to have material data quality issues, until such issues are resolved.

8. How frequently should an audit/review of the Insurer Return be performed (given that one is required)?

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

It would seem reasonable and fair that insurers with previous instances of non-compliance with Insurer Returns were audited most frequently. The AML/CFT regime requires assurance every two years and provides a potential benchmark. The size and nature of the insurance should make no difference.

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

No. The proposal adds additional time and cost without adding any additional benefit. In addition to the financial costs highlighted in the Consultation Paper, there is significant time and effort for insurers to manage Insurer Return audits/review.

In addition, we consider that introducing an audit requirement could result in the need to remediate deficiencies (purely to obtain an unqualified audit report) where the cost of doing so outweighs any benefit. This may also take resources away from development or improvement of other systems and processes which would have more benefit and impact on improving the insurer's management data, reducing risk and generating good customer outcomes. Our members recognise that external audits can provide valuable operational insights.

10. Has the existing audit/review of the Insurer Solvency Return been beneficial in improving the quality of the data submitted? In what respects?

No. Our members submit that they would maintain and submit the same quality of data regardless of the audit/review requirement. Instead, the existing audit/review of the Insurer Solvency Return has created additional overheads without realising any benefits.

11. What would your organisation expect the audit fee to be for

a. a reasonable assurance audit of the Solvency Return?

Please see response to Question 2.

b. a limited assurance review of the Solvency Return?

Please see response to Question 2.

12. How can a greater degree of assurance be obtained with respect to the Catastrophe Risk Charge? What approach could work in practice?

Insurers would benefit from more defined clarity from RBNZ about the purpose and intended benefits of the Catastrophic Risk Charge. That would allow greater industry analysis of how the Charge could be improved and drive consistency in application across the industry.

13. Do you foresee any difficulties in contracting 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?

We understand that the major firms are currently assessing their ability to perform reasonable assurance audits of the Insurer Return. Although FSC members would generally be able to access sufficient assurance services, there is only a small pool of practitioners in New Zealand who can provide this assurance.

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

A preventative approach will be more useful in improving data quality than the introduction of an audit/review requirement. For example, we support the RBNZ's initiative to publish fuller definitions and guidance for completing returns, given there is a degree of ambiguity and uncertainty in the current definitions.

This focus on getting the data correct up-front, together with a more targeted corrective approach (e.g. tighter enforcement for insurers who do not adhere to the standards expected by RBNZ) will bring a better balance of cost/benefit than the one size fits all approach proposed in the Consultation Paper.

On the proposal to impose audit requirements on the Insurer Return, we note that Part 1 of this return should be reconcilable to the company's Financial Statements, which are themselves audited. Rather than impose additional audit requirements here, it would make more sense and be more efficient for the insurer to reconcile to audited Financial Statements and explain the differences.

Our members note that some items in the Insurer Return may be hard to produce, let alone audit. For example, the numbers of lives insured – if a single policyholder has three separate life insurance benefits, we need to find and agree a method to ensure they are counted only as one life. This may be difficult to ascertain as ‘correct’. While important, this is arguably a less important metric to get right compared to financial / solvency information.

Finally, the RBNZ consultation paper mentions ‘difficulties with presentation of life insurance liabilities and the taxation thereon’. Although no further explanation is given, it would appear this is a wholly different issue from data quality. It is acknowledged that there are a variety of methods used in the industry for reporting deferred tax on policy liabilities. However, both the RBNZ Insurer Return guidelines and the Solvency Standard do give explicit instructions on how these should be dealt with in the Insurer Return and Solvency Return respectively. The RBNZ needs to make it clearer what the particular issue is here, but we submit it appears distinct from a data quality issue.