

Proposed Rule
LSA Document #09-376

DIGEST

Adds [760 IAC 1-78](#) to improve the Department of Insurance's surveillance of the financial condition of insurers by requiring an annual audit of financial statements reporting the financial position and the results of operations of insurers by independent certified public accountants, requiring the communication of internal control related matters noted in an audit, and requiring the management's report of internal control over financial reporting. Effective 30 days after filing with the Publisher.

[IC 4-22-2.1-5 Statement Concerning Rules Affecting Small Businesses](#)

[760 IAC 1-78](#)

SECTION 1. [760 IAC 1-78](#) IS ADDED TO READ AS FOLLOWS:

Rule 78. Annual Financial Reporting

[760 IAC 1-78-1](#) Applicability and scope

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 1. (a) This rule applies to all insurers as defined in section 2 of this rule, except insurers having direct premiums written of less than:

(1) one million dollars (\$1,000,000) in any calendar year; and

(2) one thousand (1,000) policyholders or certificate holders of direct written policies nationwide at the end of the calendar year;

shall be exempt from this rule for the year, unless the commissioner makes a specific finding that compliance is necessary for the commissioner to carry out statutory responsibilities. Insurers having assumed premiums pursuant to contracts or treaties of reinsurance of one million dollars (\$1,000,000) or more will not be so exempt.

(b) Foreign or alien insurers filing the audited financial report in another state, pursuant to that state's requirement for filing of audited financial reports, which has been found by the commissioner to be substantially similar to the requirements herein, are exempt from sections 3 through 12 of this rule if as follows:

(1) A copy of the following documents filed with the other state are filed with the commissioner in accordance with the filing dates specified in sections 3, 10, and 11 of this rule, respectively:

(A) Audited financial report.

(B) Communication of internal control related matters noted in an audit.

(C) The accountant's letter of qualifications.

Canadian insurers may submit accountants' reports as filed with the Office of the Superintendent of Financial Institutions, Canada.

(2) A copy of any notification of adverse financial condition report filed with the other state is filed with the commissioner within the time specified in section 9 of this rule.

(c) Foreign or alien insurers required to file management's report of internal control over financial reporting in another state are exempt from filing the report in this state if the:

(1) other state has substantially similar reporting requirements; and

(2) report is filed with the commissioner of the other state within the time specified.

(d) This rule shall not prohibit, preclude, or in any way limit the commissioner from:

(1) ordering;

(2) conducting; or

(3) performing;
examinations of insurers under the rules of the department and the practices and procedures of the department.

(Department of Insurance; [760 IAC 1-78-1](#))

[760 IAC 1-78-2](#) Definitions

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#); [IC 27-1-23](#)

Sec. 2. The following definitions apply throughout this rule:

(1) "Accountant" or "independent certified public accountant" means an independent certified public accountant or accounting firm in good standing:

(A) with the AICPA; and

(B) in all states in which the person or firm is licensed to practice.

For Canadian and British companies, it means a Canadian-chartered or British-chartered accountant.

(2) "Affiliate of" or "affiliated with" (a specific person) means a person that directly, or indirectly through one (1) or more intermediaries:

(A) controls;

(B) is controlled by; or

(C) is under common control with;

the person specified.

(3) "AICPA" means the American Institute of Certified Public Accountants.

(4) "Audit committee" means a committee (or equivalent body) established by the board of directors of an entity for the purpose of overseeing:

(A) the accounting and financial reporting processes of an insurer or group of insurers; and

(B) audits of financial statements of the insurer or group of insurers.

The audit committee of any entity that controls a group of insurers may be deemed to be the audit committee for one (1) or more of these controlled insurers solely for the purposes of this rule at the election of the controlling person. If an audit committee is not designated by the insurer, the insurer's entire board of directors shall constitute the audit committee.

(5) "Audited financial report" means and includes those items specified in section 4 of this rule.

(6) "Commissioner" means the commissioner of the department.

(7) "Department" means the Indiana department of insurance.

(8) "Group of insurers" means:

(A) those licensed insurers included in the reporting requirements of [IC 27-1-23](#); or

(B) a set of insurers as identified by management for the purpose of assessing the effectiveness of internal control over financial reporting.

(9) "Indemnification" means:

(A) an agreement of indemnity; or

(B) a release from liability;

where the intent or effect is to shift or limit in any manner the potential liability of the person or firm for failure to adhere to applicable auditing or professional standards, whether or not resulting in part from knowing of other misrepresentations made by the insurer or its representatives.

(10) "Independent board member" has the same meaning as described in section 13(d) of this rule.

(11) "Insurer" means a company required to be:

(A) licensed; or

(B) authorized;

under the laws of this state to provide insurance products.

(12) "Internal control over financial reporting" means a process effected by an entity's board of directors, management, and other personnel designed to provide reasonable assurance regarding the reliability of the financial statements. This includes the following:

(A) Those items specified in section 4(b)(2) through 4(b)(7) of this rule.

(B) Those policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of assets;

(ii) provide reasonable assurance that:

(AA) transactions are recorded as necessary to permit preparation of the financial statements, that is, those items specified in section 4(b)(2) through 4(b)(7) of this rule; and

- (BB) receipts and expenditures are being made only in accordance with authorizations of management and directors; and
- (iii) provide reasonable assurance regarding prevention or timely detection of:
- (AA) unauthorized acquisition;
 - (BB) use; or
 - (CC) disposition of assets;
- that could have a material effect on the financial statements, that is, those items specified in section 4(b)(2) through 4(b)(7) of this rule.
- (13) "NAIC" means the National Association of Insurance Commissioners.
- (14) "SEC" means the United States Securities and Exchange Commission.
- (15) "Section 404" means Section 404 of the Sarbanes-Oxley Act of 2002 and the SEC's rules and regulations promulgated thereunder.
- (16) "Section 404 report" means management's report on internal control over financial reporting as defined by the SEC and the related attestation report of the independent certified public accountant as described in this section.
- (17) "SOX compliant entity" means an entity that either is required to be compliant with or voluntarily is compliant with all of the following provisions of the Sarbanes-Oxley Act of 2002:
- (A) The preapproval requirements of Section 201 (Section 10A(i) of the Securities Exchange Act of 1934).
 - (B) The audit committee independence requirements of Section 301 (Section 10A(m)(3) of the Securities Exchange Act of 1934).
 - (C) The internal control over financial reporting requirements of Section 404 (Item 308 of SEC Regulation S-K).

(Department of Insurance; [760 IAC 1-78-2](#))

[760 IAC 1-78-3](#) General requirements related to filing and extensions for filing of annual audited financial reports and audit committee appointment

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 3. (a) All insurers shall:

- (1) have an annual audit by an independent certified public accountant; and
- (2) file an audited financial report with the commissioner on or before June 1 for the year ended December 31 immediately preceding. The commissioner may require an insurer to file an audited financial report earlier than June 1 with ninety (90) days advance notice to the insurer.

(b) Extensions of the June 1 filing date may be granted by the commissioner for thirty (30) days under the following conditions:

- (1) A showing by the insurer and its independent certified public accountant of the reasons for requesting an extension.
- (2) A determination by the commissioner of good cause for an extension.

The request for extension must be submitted in writing not less than ten (10) days prior to the due date in sufficient detail to permit the commissioner to make an informed decision with respect to the requested extension.

(c) If an extension is granted in accordance with the provisions in subsection (b), a similar extension of thirty (30) days is granted to the filing of management's report of internal control over financial reporting.

(d) Every insurer required to file an annual audited financial report under this rule shall designate a group of individuals as constituting its audit committee, as defined in section 2 of this rule. The audit committee of an entity that controls an insurer may be deemed to be the insurer's audit committee for purposes of this rule at the election of the controlling person.

(Department of Insurance; [760 IAC 1-78-3](#))

[760 IAC 1-78-4](#) Contents of annual audited financial report

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#); [IC 27-1-20-21](#)

Sec. 4. (a) The annual audited financial report shall report the financial position of the insurer as of the end of the most recent calendar year and the results of its operations, cash flows, and changes in capital and surplus for the year then ended in conformity with statutory accounting practices prescribed, or otherwise permitted, by the department of insurance of the state of domicile.

(b) The annual audited financial report shall include the following:

(1) The report of an independent certified public accountant.

(2) A balance sheet reporting the following:

(A) Admitted assets.

(B) Liabilities.

(C) Capital.

(D) Surplus.

(3) A statement of operations.

(4) A statement of cash flow.

(5) A statement of changes in capital and surplus.

(6) Notes to financial statements. These notes shall be those required by the appropriate NAIC Annual Statement Instructions and the NAIC Accounting Practices and Procedures Manual, which shall include the following:

(A) A reconciliation of differences, if any, between the audited statutory financial statements and the annual statement filed under [IC 27-1-20-21](#).

(B) A written description of the nature of the differences described in clause (A).

(7) The financial statements included in the audited financial report shall be prepared in a form and using language and groupings substantially the same as the relevant sections of the annual statement of the insurer filed with the commissioner. The financial statement shall be comparative, presenting the amounts as of December 31 of the current year and the amounts as of the immediately preceding December 31. However, in the first year in which an insurer is required to file an audited financial report, the comparative data may be omitted.

(Department of Insurance; [760 IAC 1-78-4](#))

[760 IAC 1-78-5](#) Designation of independent certified public accountant

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 5. (a) Each insurer required by this rule to file an annual audited financial report must, within sixty (60) days after becoming subject to the requirement, register with the commissioner in writing the name and address of the independent certified public accountant or accounting firm retained to conduct the annual audit set forth in this rule. Insurers not retaining an independent certified public accountant on the effective date of this rule shall register the name and address of their retained independent certified public accountant not less than six (6) months before the date when the first audited financial report is to be filed.

(b) The insurer shall:

(1) obtain a letter from the accountant; and

(2) file a copy with the commissioner that:

(A) states that the accountant is aware of the provisions of the insurance code and the rules of the insurance department of the state of domicile that relate to accounting and financial matters; and

(B) affirms that the accountant will express the accountant's opinion on the financial statements in terms of their conformity to the statutory accounting practices prescribed or otherwise permitted by that insurance department, specifying such exceptions as the accountant may believe appropriate.

(c) If an accountant who was the accountant for the immediately preceding filed audited financial

report is dismissed or resigns, the insurer shall within five (5) business days notify the commissioner of this event. The insurer shall also furnish the commissioner with a separate letter within ten (10) business days of the notification stating whether in the twenty-four (24) months preceding the event there were any disagreements with the former accountant on any matter of:

- (1) accounting principles or practices;
- (2) financial statement disclosure; or
- (3) auditing scope or procedure;

which disagreements, if not resolved to the satisfaction of the former accountant, would have caused the accountant to make reference to the subject matter of the disagreement in connection with the accountant's opinion. The disagreements required to be reported in response to this section include both those resolved to the former accountant's satisfaction and those not resolved to the former accountant's satisfaction. Disagreements contemplated by this section are those that occur at the decision making level, that is, between personnel of the insurer responsible for presentation of its financial statements and personnel of the accounting firm responsible for rendering its report. The insurer shall also in writing request the former accountant to furnish a letter addressed to the insurer stating whether the accountant agrees with the statements contained in the insurer's letter and, if not, stating the reasons for which the accountant does not agree. The insurer shall furnish the responsive letter from the former accountant to the commissioner together with its own.

(Department of Insurance; [760 IAC 1-78-5](#))

[760 IAC 1-78-6](#) Qualifications of independent certified public accountant

Authority: [IC 27-1-3-7](#)

Affected: [IC 4-21.5-3](#); [IC 27-1-3.5](#); [IC 27-9](#)

Sec. 6. (a) The commissioner shall not recognize a person or firm as a qualified independent certified public accountant if the person or firm:

- (1) is not in good standing with the AICPA and in all states in which the person or firm is licensed to practice, or, for a Canadian or British company, that is not a chartered accountant; or
- (2) has either directly or indirectly entered into an agreement of indemnity or release from liability, collectively referred to as indemnification, with respect to the audit of the insurer.

(b) Except as otherwise provided in this rule, the commissioner shall recognize an independent certified public accountant as qualified as long as the accountant conforms to the standards of the accountant's profession, as contained in the Code of Professional Ethics of the AICPA and Rules and Regulations and Code of Ethics and Rules of Professional Conduct of the Indiana Board of Accountancy, or similar code.

(c) A qualified independent certified public accountant may enter into an agreement with an insurer to have disputes relating to an audit resolved by mediation or arbitration. However, in the event of a delinquency proceeding commenced against the insurer under [IC 27-9](#), the mediation or arbitration provisions shall operate at the option of the statutory successor.

(d) The lead (or coordinating) audit partner (having primary responsibility for the audit) may not act in that capacity for more than seven (7) consecutive years. The person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of two (2) consecutive years. An insurer may make application to the commissioner for relief from the above rotation requirement on the basis of unusual circumstances. This application should be made at least thirty (30) days before the end of the calendar year. The commissioner may consider any of the following factors in determining if the relief should be granted:

- (1) The number of partners, expertise of the partners, or the number of insurance clients in the currently registered firm.
- (2) The premium volume of the insurer.
- (3) The number of jurisdictions in which the insurer transacts business.

The insurer shall file, with its annual statement filing, the approval for relief from this subsection with the states that it is licensed in or doing business in and with the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer shall file the approval in an electronic format acceptable to the

(e) The commissioner shall neither recognize as a qualified independent certified public accountant, nor accept an annual audited financial report, prepared in whole or in part by, a natural person who has:

(1) been convicted of:

(A) fraud;

(B) bribery;

(C) a violation of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. Sections 1961 to 1968; or

(D) any dishonest conduct or practices under federal or state law;

(2) been found to have violated the insurance laws of this state with respect to any previous reports submitted under this rule; or

(3) demonstrated a pattern or practice of failing to detect or disclose material information in previous reports filed under the provisions of this rule.

(f) The commissioner, as provided in [IC 4-21.5-3](#), may:

(1) hold a hearing to determine whether an independent certified public accountant is qualified; and

(2) after considering the evidence presented:

(A) rule that the accountant is not qualified for purposes of expressing the accountant's opinion on the financial statements in the annual audited financial report made under this rule; and

(B) require the insurer to replace the accountant with another whose relationship with the insurer is qualified within the meaning of this rule.

(g) The commissioner shall not recognize as a qualified independent certified public accountant or accept an annual audited financial report prepared, in whole or in part, by an accountant who provides to an insurer, contemporaneously with the audit, any of the following nonaudit services:

(1) Bookkeeping or other services related to the accounting records or financial statements of the insurer.

(2) Financial information systems design and implementation.

(3) Appraisal or valuation services, fairness opinions, or contribution-in-kind reports.

(4) Actuarially-oriented advisory services involving the determination of amounts recorded in the financial statements. The accountant may assist an insurer in understanding the methods, assumptions, and inputs used in the determination of amounts recorded in the financial statement only if it is reasonable to conclude that the services provided will not be subject to audit procedures during an audit of the insurer's financial statements. An accountant's actuary may also issue an actuarial opinion or certification on an insurer's reserves if the following conditions have been met:

(A) Neither the accountant nor the accountant's actuary has performed any management functions or made any management decisions.

(B) The insurer has competent personnel, or engages a third party actuary, to estimate the reserves for which management takes responsibility.

(C) The accountant's actuary tests the reasonableness of the reserves after the insurer's management has determined the amount of the reserves.

(5) Internal audit outsourcing services.

(6) Management functions or human resources.

(7) Broker or dealer, investment adviser, or investment banking services.

(8) Legal services or expert services unrelated to the audit.

(9) Any other services that the commissioner determines, by rule, are impermissible.

(h) Insurers having direct written and assumed premiums of less than one hundred million dollars (\$100,000,000) in any calendar year may request an exemption from subsection (g). The insurer shall file with the commissioner a written statement discussing the reasons why the insurer should be exempt from these provisions. If the commissioner finds, upon review of this statement, that compliance with this rule would constitute a financial or organizational hardship upon the insurer, an exemption may be granted.

(i) A qualified independent certified public accountant who performs the audit may engage in other nonaudit services, including tax services, that are not described in subsection (g) or that do not conflict with subsection (g)(2), only if the activity is approved in advance by the audit committee, in accordance with subsection (j).

(j) All auditing services and nonaudit services provided to an insurer by the qualified independent certified public accountant of the insurer shall be preapproved by the audit committee. The preapproval requirement is waived with respect to nonaudit services if the insurer is a SOX compliant entity, a direct or indirect wholly-owned subsidiary of a SOX compliant entity, or all of the following are met:

- (1) The aggregate amount of all such nonaudit services provided to the insurer constitutes not more than five percent (5%) of the total amount of fees paid by the insurer to its qualified independent certified public accountant during the fiscal year in which the nonaudit services are provided.
- (2) The services were not recognized by the insurer at the time of the engagement to be nonaudit services.
- (3) The services are promptly brought to the attention of the audit committee and approved prior to the completion of the audit by the audit committee or by one (1) or more members of the audit committee who are the members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee.

(k) The audit committee may delegate to one (1) or more designated members of the audit committee the authority to grant the preapprovals required by subsection (j). The decisions of any member to whom this authority is delegated shall be presented to the full audit committee at each of its scheduled meetings.

(l) The commissioner shall not recognize an independent certified public accountant as qualified for a particular insurer if:

- (1) a member of the board;
- (2) the president;
- (3) the chief executive officer;
- (4) the controller;
- (5) the chief financial officer;
- (6) the chief accounting officer; or
- (7) any person serving in an equivalent position for that insurer;

was employed by the independent certified public accountant and participated in the audit of that insurer during the one-year period preceding the date that the most current statutory opinion is due. This subsection shall only apply to partners and senior managers involved in the audit. An insurer may make application to the commissioner for relief from the above requirement on the basis of unusual circumstances. The insurer shall file, with its annual statement filing, the approval for relief from this subsection with the states that it is licensed in or doing business in and the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer shall file the approval in an electronic format acceptable to the NAIC.

(Department of Insurance; [760 IAC 1-78-6](#))

[760 IAC 1-78-7](#) Consolidated or combined audits

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 7. (a) An insurer may make written application to the commissioner for approval to file audited consolidated or combined financial statements in lieu of separate annual audited financial statements if the insurer:

- (1) is part of a group of insurance companies that utilizes a pooling or one hundred percent (100%) reinsurance agreement that affects the solvency and integrity of the insurer's reserves; and
- (2) cedes all of its direct and assumed business to the pool.

(b) If an insurer makes written application to the commissioner under subsection (a), a columnar consolidating or combining worksheet shall be filed with the report containing the following information:

- (1) Amounts shown on the consolidated or combined audited financial report.
- (2) Amounts for each insurer subject to this section, stated separately.
- (3) Noninsurance operations, on a combined or individual basis.
- (4) Explanations of consolidating and eliminating entries.

(5) A reconciliation of any differences between the amounts shown in the individual insurer columns of the worksheet and comparable amounts shown on the annual statements of the insurers.

(Department of Insurance; [760 IAC 1-78-7](#))

[760 IAC 1-78-8](#) Scope of audit and report of independent certified public accountant

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 8. Financial statements furnished under section 4 of this rule shall be examined by the independent certified public accountant. The audit of the insurer's financial statements shall be conducted in accordance with generally accepted auditing standards. In accordance with AU Section 319 of the Professional Standards of the AICPA, Consideration of Internal Control in a Financial Statement Audit, the independent certified public accountant should obtain an understanding of internal control sufficient to plan the audit. To the extent required by AU 319, for those insurers required to file a management's report of internal control over financial reporting under section 15 of this rule, the independent certified public accountant should consider (as that term is defined in Statement on Auditing Standards (SAS) No. 102, Defining Professional Requirements in Statements on Auditing Standards or its replacement) the most recently available report in planning and performing the audit of the statutory financial statements. Consideration shall be given to the procedures illustrated in the Financial Condition Examiners Handbook promulgated by the NAIC as the independent certified public accountant deems necessary.

(Department of Insurance; [760 IAC 1-78-8](#))

[760 IAC 1-78-9](#) Notification of adverse financial condition

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 9. (a) The insurer required to furnish the annual audited financial report shall require the independent certified public accountant to report, in writing, within five (5) business days to the board of directors or its audit committee any determination by the independent certified public accountant that the insurer:

(1) has materially misstated its financial condition as reported to the commissioner as of the balance sheet date currently under audit; or

(2) does not meet the minimum capital and surplus requirement set forth in [IC 27](#) as of that date.

An insurer that has received a report under this section shall forward a copy of the report to the commissioner within five (5) business days of receipt of the report and shall provide the independent certified public accountant making the report with evidence of the report being furnished to the commissioner. If the independent certified public accountant fails to receive the evidence within the required five (5) business day period, the independent certified public accountant shall furnish to the commissioner a copy of its report within the next five (5) business days.

(b) No independent certified public accountant shall be liable in any manner to any person for any statement made in connection with subsection (a) if the statement is made in good faith in compliance with subsection (a).

(c) If the accountant, after the date of the audited financial report filed under this rule, becomes aware of facts that might have affected the accountant's report, the accountant must take such action as prescribed in Volume 1, Section AU 561 of the Professional Standards of the AICPA.

(Department of Insurance; [760 IAC 1-78-9](#))

[760 IAC 1-78-10](#) Communication of internal control related matters noted in an audit

Authority: [IC 27-1-3-7](#)

Sec. 10. (a) In addition to the annual audited financial report required by section 3 of this rule, each insurer shall furnish the commissioner with a written communication as to any unremediated material weaknesses in its internal control over financial reporting noted during the audit. The communication shall:

- (1) be prepared by the accountant within sixty (60) days after the filing of the annual audited financial report; and
- (2) contain a description of any unremediated material weakness (as the term material weakness is defined by Statement on Auditing Standard 60, Communication of Internal Control Related Matters Noted in an Audit, or its replacement) as of December 31 of the year immediately preceding. If no unremediated material weaknesses were noted, the communication should so state.

(b) The insurer shall provide a description of remedial actions taken or proposed to correct unremediated material weaknesses, if the actions are not described in the accountant's communication.

(Department of Insurance; [760 IAC 1-78-10](#))

[760 IAC 1-78-11](#) Accountant's letter of qualifications

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 11. The accountant shall furnish the insurer in connection with, and for inclusion in, the filing of the annual audited financial report, a letter stating the following:

- (1) That the accountant:
 - (A) is independent with respect to the insurer; and
 - (B) conforms to the standards of the accountant's profession as contained in the Code of Professional Ethics and pronouncements of the AICPA and the Rules of Professional Conduct of the Indiana Board of Accountancy, or similar code.
- (2) The background and experience in general, the experience in audits of insurers of the staff assigned to the engagement, and whether each is an independent certified public accountant. Nothing within this rule shall be construed as prohibiting the accountant from utilizing such staff as the accountant deems appropriate where use is consistent with the standards prescribed by generally accepted auditing standards.
- (3) That the accountant understands the annual audited financial report and his or her opinion thereon will be filed in compliance with this rule and that the commissioner will be relying on this information in the monitoring and regulation of the financial position of insurers.
- (4) That the accountant consents to the requirements of section 12 of this rule and that the accountant consents and agrees to make available for review by the commissioner, or the commissioner's designee or appointed agent, the work papers, as defined in section 12 of this rule.
- (5) A representation that the accountant is:
 - (A) properly licensed by an appropriate state licensing authority; and
 - (B) a member in good standing in the AICPA.
- (6) A representation that the accountant is in compliance with the requirements of section 6 of this rule.

(Department of Insurance; [760 IAC 1-78-11](#))

[760 IAC 1-78-12](#) Definition, availability, and maintenance of independent certified public accountants' work papers

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.1](#); [IC 27-1-3.5](#)

Sec. 12. (a) As used in this section, "work papers" means the:

- (1) records kept by the independent certified public accountant of the procedures followed;

- (2) tests performed;
- (3) information obtained; and
- (4) conclusions reached;

pertinent to the accountant's audit of the financial statements of an insurer.

(b) Work papers may include:

- (1) audit planning documentation;
- (2) work programs;
- (3) analyses;
- (4) memoranda;
- (5) letters of confirmation and representation;
- (6) abstracts of company documents; and
- (7) schedules or commentaries;

prepared or obtained by the independent certified public accountant in the course of the accountant's audit of the financial statements of an insurer and that support the accountant's opinion.

(c) Every insurer required to file an audited financial report under this rule shall require the accountant to make the following available for review by department examiners:

- (1) All work papers prepared in the conduct of the accountant's audit.
- (2) Any communications related to the audit between the accountant and the insurer at:
 - (A) the offices of the insurer;
 - (B) the department; or
 - (C) any other reasonable place designated by the commissioner.

The insurer shall require that the accountant retain the audit work papers and communications until the department has filed a report on examination covering the period of the audit but not longer than seven (7) years from the date of the audit report.

(d) In the conduct of the periodic review by the department examiners described in subsection (c), it shall be agreed that photocopies of pertinent audit work papers may be made and retained by the department. The reviews by the department examiners shall be considered investigations, and all working papers and communications obtained during the course of the investigations shall be afforded the same confidentiality as other examination work papers generated by the department under [IC 27-1-3.1](#).

(Department of Insurance; [760 IAC 1-78-12](#))

[760 IAC 1-78-13](#) Requirements for audit committee

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 13. (a) This section shall not apply to:

- (1) foreign or alien insurers licensed in this state;
- (2) an insurer that is a SOX compliant entity; or
- (3) a direct or indirect wholly-owned subsidiary of a SOX compliant entity.

(b) The audit committee shall be directly responsible for the:

- (1) appointment;
- (2) compensation; and
- (3) oversight of the work;

of any accountant, including resolution of disagreements between management and the accountant regarding financial reporting, for the purpose of preparing or issuing the audited financial report or related work under this rule. Each accountant shall report directly to the audit committee.

(c) Each member of the audit committee shall be a member of the board of directors of:

- (1) the insurer; or
- (2) an entity elected under subsection (f) and section 2(4) of this rule.

(d) In order to be considered independent for purposes of this section, a member of the audit committee may not, other than in the member's capacity as a member of the audit committee, the board of directors, or any other board committee, accept any:

- (1) consulting fee;
- (2) advisory fee; or
- (3) other compensatory fee;

from the entity or be an affiliated person of the entity or any subsidiary thereof. However, if law requires board participation by otherwise nonindependent members, that law shall prevail and such members may participate in the audit committee and be designated as independent for audit committee purposes, unless they are an officer or employee of the insurer or one (1) of its affiliates.

(e) If a member of the audit committee ceases to be independent for reasons outside the member's reasonable control, that person, with notice by the responsible entity to the state, may remain an audit committee member of the responsible entity until the earlier of the next annual meeting of the responsible entity or one (1) year from the occurrence of the event that caused the member to be no longer independent.

(f) To exercise the election of the controlling person to designate the audit committee for purposes of this rule, the ultimate controlling person shall provide written notice to the commissioners of the affected insurers. Notification shall:

- (1) be made timely prior to the issuance of the statutory audit report; and
- (2) include a description of the basis for the election.

The election can be changed through notice to the commissioner by the insurer, which shall include a description of the basis for the change. The election shall remain in effect for perpetuity, until rescinded.

(g) The audit committee shall require the accountant that performs for an insurer any audit required by this rule to timely report to the audit committee in accordance with the requirements of SAS 61, Communication with Audit Committees, or its replacement, including the following:

- (1) All significant accounting policies and material permitted practices.
- (2) All material alternative treatments of financial information within statutory accounting principles that have been discussed with management officials of the insurer, ramifications of the use of the alternative disclosures and treatments, and the treatment preferred by the accountant.
- (3) Other material written communications between the accountant and the management of the insurer, such as any management letter or schedule of unadjusted differences.

If an insurer is a member of an insurance holding company system, the reports required by this subsection may be provided to the audit committee on an aggregate basis for insurers in the holding company system, provided that any substantial differences among insurers in the system are identified to the audit committee.

(h) The proportion of independent audit committee members shall meet or exceed the following criteria:

Prior Calendar Year Direct Written and Assumed Premiums		
\$0 - \$300,000,000	Over \$300,000,000 - \$500,000,000	Over \$500,000,000
No minimum requirements.	Majority (50% or more) of members shall be independent.	Supermajority of members (75% or more) shall be independent.

(i) An insurer with direct written and assumed premium, excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, less than five hundred million dollars (\$500,000,000) may make application to the commissioner for a waiver from the requirements set forth in this section based upon hardship. The insurer shall file, with its annual statement filing, the approval for relief from the requirements set forth in this section with the states that it is licensed in or doing business in and the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer shall file the approval in an electronic format acceptable to the NAIC.

(Department of Insurance; [760 IAC 1-78-13](#))

[760 IAC 1-78-14](#) Conduct of insurer in connection with the preparation of required reports and documents

Sec. 14. (a) No director or officer of an insurer shall, directly or indirectly:

(1) make or cause to be made a materially false or misleading statement to an accountant in connection with any:

(A) audit;

(B) review; or

(C) communication;

required under this rule; or

(2) omit to state, or cause another person to omit to state, any material fact necessary in order to make statements made, in light of the circumstances under which the statements were made, not misleading to an accountant in connection with any:

(A) audit;

(B) review; or

(C) communication;

required under this rule.

(b) No officer or director of an insurer, or any other person acting under the direction thereof, shall directly or indirectly take any action to:

(1) coerce;

(2) manipulate;

(3) mislead; or

(4) fraudulently influence;

any accountant engaged in the performance of an audit under this rule if that person knew or should have known that the action, if successful, could result in rendering the insurer's financial statements materially misleading.

(c) For purposes of subsection (b), actions that, "if successful, could result in rendering the insurer's financial statements materially misleading" include, but are not limited to, actions taken at any time with respect to the professional engagement period to coerce, manipulate, mislead, or fraudulently influence an accountant:

(1) to issue or reissue a report on an insurer's financial statements that is not warranted in the circumstances, due to material violations of statutory accounting principles prescribed by:

(A) the commissioner;

(B) generally accepted auditing standards; or

(C) other professional or regulatory standards;

(2) not to perform audit, review, or other procedures required by generally accepted auditing standards or other professional standards;

(3) not to withdraw an issued report; or

(4) not to communicate matters to an insurer's audit committee.

(Department of Insurance; [760 IAC 1-78-14](#))

[760 IAC 1-78-15](#) Management's report of internal control over financial reporting

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#); [IC 27-1-36](#)

Sec. 15. (a) Every insurer required to file an audited financial report under this rule that has annual direct written and assumed premiums, excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, of five hundred million dollars (\$500,000,000) or more shall prepare a report of the insurer's or group of insurers' internal control over financial reporting, as these terms are defined in section 2 of this rule. The report shall be filed with the commissioner along with the communication of internal control related matters noted in an audit described under section 10 of this rule. Management's report of internal control over financial reporting shall be as of December 31 immediately preceding.

(b) Notwithstanding the premium threshold in subsection (a), the commissioner may require an insurer to file management's report of internal control over financial reporting if the insurer is in any risk based capital level event as referenced in [IC 27-1-36](#), or meets any one (1) or more of the standards of an insurer deemed to be in hazardous financial condition as defined in [760 IAC 1-53](#).

(c) An insurer or a group of insurers that is:

- (1) directly subject to Section 404;
- (2) part of a holding company system whose parent is directly subject to Section 404;
- (3) not directly subject to Section 404 but is a SOX compliant entity; or
- (4) a member of a holding company system whose parent is not directly subject to Section 404 but is a SOX compliant entity;

may file its or its parent's Section 404 report and an addendum in satisfaction of the requirement in this section provided that those internal controls of the insurer or group of insurers having a material impact on the preparation of the insurer's or group of insurers' audited statutory financial statements (those items included in section 4(b)(2) through 4(b)(7) of this rule) were included in the scope of the Section 404 report.

(d) The addendum described in subsection (c) shall be a positive statement by management that there are no material processes with respect to the preparation of the insurer's or group of insurers' audited statutory financial statements (those items included in section 4(b)(2) through 4(b)(7) of this rule excluded from the Section 404 report). If there are internal controls of the insurer or group of insurers that have a material impact on the preparation of the insurer's or group of insurers' audited statutory financial statements and those internal controls were not included in the scope of the Section 404 report, the insurer or group of insurers may either file:

- (1) a report as required by this section; or
- (2) the Section 404 report and a report as required by this section;

for those internal controls that have a material impact on the preparation of the insurer's or group of insurers' audited statutory financial statements not covered by the Section 404 report.

(e) Management's report of internal control over financial reporting shall include the following:

- (1) A statement that management is responsible for establishing and maintaining adequate internal control over financial reporting.
- (2) A statement that management has established internal control over financial reporting and an assertion, to the best of management's knowledge and belief, after diligent inquiry, as to whether its internal control over financial reporting is effective to provide reasonable assurance regarding the reliability of financial statements in accordance with statutory accounting principles.
- (3) A statement that briefly describes the approach or processes by which management evaluated the effectiveness of its internal control over financial reporting.
- (4) A statement that briefly describes the scope of work that is included and whether any internal controls were excluded.
- (5) Disclosure of any unremediated material weaknesses in the internal control over financial reporting identified by management as of December 31 immediately preceding. Management is not permitted to conclude that the internal control over financial reporting is effective to provide reasonable assurance regarding the reliability of financial statements in accordance with statutory accounting principles if there is one (1) or more unremediated material weaknesses in its internal control over financial reporting.
- (6) A statement regarding the inherent limitations of internal control systems.
- (7) Signatures of the chief executive officer and the chief financial officer, or equivalent position or title.

(f) Management shall document and make available upon financial condition examination the basis upon which its assertions, required in subsection (e), are made. Management may base its assertions, in part, upon its review, monitoring, and testing of internal controls undertaken in the normal course of its activities. Management shall have discretion as to the nature of the internal control framework used, and the nature and extent of documentation, in order to make its assertion in a cost effective manner and, as such, may include assembly of or reference to existing documentation. Management's report on internal control over financial reporting, required by subsection (a), and any documentation provided in support thereof during the course of a financial condition examination, shall be kept confidential by the department.

(Department of Insurance; [760 IAC 1-78-15](#))

[760 IAC 1-78-16](#) Exemptions and effective dates

Authority: [IC 27-1-3-7](#)

Affected: [IC 4-21.5-3](#); [IC 27-1-3.5](#)

Sec. 16. (a) Upon written application of any insurer, the commissioner may grant an exemption from compliance with any and all provisions of this rule if the commissioner finds, upon review of the application, that compliance with this rule would constitute a financial or organizational hardship upon the insurer. An exemption may be granted at any time and from time to time for a specified period or periods. Within ten (10) days from a denial of an insurer's written request for an exemption from this rule, the insurer may request in writing a hearing on its application for an exemption. The hearing shall be held in accordance with [IC 4-21.5-3](#).

(b) Domestic insurers retaining a certified public accountant on the effective date of this rule who qualify as independent shall comply with this rule for the year ending December 31, 2009, and each year thereafter unless the commissioner permits otherwise.

(c) Foreign insurers shall comply with this rule for the year ending December 31, 2009, and each year thereafter, unless the commissioner permits otherwise.

(d) The requirements of section 6(d) of this rule shall be in effect for audits of the year beginning January 1, 2010, and thereafter.

(e) The requirements of section 13 of this rule are to be in effect January 1, 2010. An insurer or group of insurers that is not required to have independent audit committee members or only a majority of independent audit committee members, as opposed to a supermajority, because the total written and assumed premium:

(1) is below the threshold; and

(2) subsequently becomes subject to one (1) of the independence requirements due to changes in premium;

shall have one (1) year following the year the threshold is exceeded (but not earlier than January 1, 2010) to comply with the independence requirements. An insurer that becomes subject to one (1) of the independence requirements as a result of a business combination shall have one (1) calendar year following the date of acquisition or combination to comply with the independence requirements.

(f) The requirements of section 15 of this rule are effective beginning with the reporting period ending December 31, 2010, and each year thereafter. An insurer or group of insurers that is not required to file a report because the total written premium is below the threshold and subsequently becomes subject to the reporting requirements shall have two (2) years following the year the threshold is exceeded (but not earlier than December 31, 2010) to file a report. An insurer acquired in a business combination shall have two (2) calendar years following the date of acquisition or combination to comply with the reporting requirements.

(Department of Insurance; [760 IAC 1-78-16](#))

[760 IAC 1-78-17](#) Canadian and British companies

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3.5](#)

Sec. 17. (a) In the case of Canadian and British insurers, the annual audited financial report shall be defined as the annual statement of total business on the form filed by the companies with their supervision authority duly audited by an independent chartered accountant.

(b) For such insurers, the letter required in section 5(b) of this rule shall:

- (1) state that the accountant is aware of the requirements relating to the annual audited financial report filed with the commissioner under section 3 of this rule; and
- (2) affirm that the opinion expressed is in conformity with those requirements.

(Department of Insurance; [760 IAC 1-78-17](#))

[760 IAC 1-78-18](#) Severability

Authority: [IC 27-1-3-7](#)

Affected: [IC 27-1-3-7](#)

Sec. 18. If:

- (1) any section or portion of a section of this rule; or
- (2) its applicability to any person or circumstance;

is held invalid by a court, the remainder of the rule or the applicability of the provision to other persons or circumstances shall not be affected.

(Department of Insurance; [760 IAC 1-78-18](#))

[Notice of Public Hearing](#)

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