

Overview of Audits in Insurance Sector

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Regulatory Framework

Overview of the regulatory framework governing insurance companies in India

- The Insurance Act, 1938 as amended by the Insurance Laws (Amendment) Act, 2015 (including Insurance Rules, 1939);
- The Insurance Regulatory and Development Authority Act, 1999 as amended by the Insurance Laws (Amendment) Act, 2015;
- The Companies Act, 2013;
- SEBI Act and SEBI Regulations;
- The Insurance Regulatory and Development Authority Regulations framed under the IRDAI, Act, 1999;
- IRDAI Investment Regulations (as amended from time to time);
- IRDAI Preparation of Financial Statements and Auditors Report Regulations and (as amended from time to time).

Financial Statements

Overview of financial statements for insurance companies

- Balance sheet
- Revenue Account
- Profit and loss account
- Receipts and Payment Account

Note: (Preparation of Financial statements and Auditor's Report of Insurers) Regulations, 2000 prescribes the format for preparation of Financial Statements of an insurer :

- **Schedule A (Life Insurance business)**
- **Schedule B (General Insurance business)**

Auditor's certifications required for Insurance company

- Solvency Margin Certificate – Non life
- Expenses of Management
- NAV Certification – Life
- Paragraphs 3 and 4 of Schedule C of IRDAI Certificate includes following matters :
 - i. Review of the Management Report
 - ii. Verification of Cash on hand balance as at year end
 - iii. The Company is not a trustee of any trust
 - iv. Proper application and investments of the Policyholders' Funds

Applicability of Accounting Standards

All Accounting Standards to the Insurance companies in India are applicable except for the following :

- AS 3 “Cashflow Statement “ as IRDAI specifies to use Direct Method.
- AS 9 “Revenue Recognition” as IRDAI specifies 64VB compliance for the premium recognition.
- AS 13 “Accounting for Investments” as IRDAI specifies Investment regulations.
- AS 17 “Segment Reporting” as IRDAI specifies its own Line of Business wise reporting.

Note : The Insurance Regulatory and Development Authority of India (IRDAI) has deferred the date of implementation of Indian Accounting Standard (Ind-AS) for the insurance sector from FY 22-23 till further notice.

Key Business Processes

- Premium
- Reinsurance
- Claims
- Investments
- Commissions and brokerage
- Operating Expenses
- Property plant and equipment
- Payroll

Deep Dive into Key Areas

- Premium
- Claims
- Investments
- **Actuarial liabilities for insurance contracts / Claims incurred but not reported or incurred but not enough reported**

Premium

Overall Audit Approach :

- Understanding the Business Process and Products
- Conducting detailed walkthrough
- Carry out risk assessment
- IFC testing – Test of controls (Identifying financial risks, testing controls, comment on effectiveness of controls)
- Substantive testing – Test of details
- Reporting and Documentation

Key Risk to be addressed :

- 64 VB compliance check- Premium is accounted without receipt of premium.
- Proper documentation including KYC compliance/AML compliance (PAN Card, Aadhar Card, IT Returns)
- For ULIP Policies – Calculation of correct NAV with proper time stamping (while issuance of policy) and compliance with the IRDAI regulations.
- Tracing of Premium with the bank accounts

Claims

- Understanding the Claim settlement process of the company for its different products.
- Conducting detailed walkthrough
- Carry out risk assessment including fraud risk factors
- IFC testing – Test of controls (Identifying financial risks, testing controls, comment on effectiveness of controls)
- Substantive testing – Test of details
- Reporting and Documentation

Key Risk to be addressed :

- Claims accepted during the year should be checked whether the incurrence is within coverage period
- Reconciliation of claims from intimation to acceptance and reserving should be traced.
- Claims documents like Death Certificate, Application of NAV for surrender, investigation report, etc should be verified properly.
- Claims payout should be as per the mentioned terms (inclusion and exclusions should be checked) in policy for the different products features

Investments

- Understand the Investment Process, company policy and systems used
- Conducting a detailed walkthrough
- Carry out compliance check mentioned as per IRDAI Investment Regulations
- IFC testing – Test of controls
- Substantive testing (including valuation, existence, amortization, impairment check) – Test of details.
- Reporting Requirements (Schedule 8 and 8A)

Key Risk to be addressed :

- Ensure that the system is be able to automatically monitor various Regulatory limits. (Limit breach check)
- Classification of the investments by the company based on the CAT codes should be verified.
- Ensure that there is split between Shareholders' and Policyholders' funds and earmarking of securities between various funds namely Life (Participating and Non-Participating), Pension and Group (Participating and Non-Participating) and Unit Linked Fund.
- Review of various documents like deal tickets, custodian report, NAV reports, original FD receipts, etc.
- Controls over NAV computation and declaration.

Policy liabilities / Claims o/s liabilities for Insurance contracts

- The Appointed Actuary of the company are required to certify the policy liabilities (in case of life insurance company) and claims outstanding {incurred but not reported (IBNE) or incurred but not enough reported (IBNER)} (in case of general insurance company)
- As required by the IRDAI guidelines, Auditors may place reliance on such certification of appointed actuary and refer the same in their Audit report. However, the auditors are expected to ensure the data supplied to actuaries was complete.
- The auditor should consider as part of their audit procedures:
 - Obtain and discuss the assumptions used or changes in assumptions in valuation of policy liabilities or claims IBNE / IBNER
 - Perform benchmarking analysis for the assumptions being used
 - Verify the completeness of data and controls around data being used by the Appointed Actuary in their valuation

Information Technology General Controls (ITGC)

Most of the systems used by the insurance companies have automated controls and the dependency on such systems have been increased over the period of time. To ensure such controls are effective, auditor needs to conduct ITGC audit.

The objectives of ITGCs are to ensure the integrity of the data and processes that the systems support. The most common ITGCs are as follow :

- Logical access controls over applications, data and supporting infrastructure
- Program change management controls
- Backup and recovery controls
- Computer operation controls
- Data center physical security controls
- General IT Administration
- Cyber security

Data analytical tools

Auditors may perform analytical procedures for some of the audit areas on complete population:

- Investment holding statement reconciliation
- Re-performance of Investment Income and Profit / loss on sale of Investments
- Identifying claims demographics and early claim analysis
- Re-performance of Maturity benefits payable to policy holders
- Commission payout vis-à-vis premium income to identify the outliers for regulatory breach

Following are some of the analytical tools used while auditing of insurance companies :

- IDEA data analytical tool
- Power BI
- Alteryx
- Qlikview

to sum up...

Auditing an insurance company requires a comprehensive understanding of the regulatory framework, the business operations, and the internal controls of the company. From above mentioned pointers, you can conduct an effective audit that will help identify areas for improvement.

Questions ?