

## AICPA NAIC

## Task Force

## Best Practices: Insurance Regulator Access to Audit Documentation



This document is an other auditing publication, as defined in AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards (AICPA, Professional Standards). Other auditing publications have no authoritative status; however, they may help the auditor understand and apply generally accepted auditing standards. In applying the auditing guidance included in an other auditing publication, the auditor should, using professional judgment, assess the relevance and appropriateness of such guidance to the circumstances of the audit. The auditing guidance in this document has been reviewed by the AICPA Audit and Attest Standards staff and published by the AICPA and is presumed to be appropriate. This document has not been approved, disapproved, or otherwise acted on by a senior technical committee of the AICPA.

### **Best Practices: Insurance Regulator Access to Audit Documentation**

Section 13 C of the NAIC Model Audit Rule (“MAR”) requires that independent certified public accountants (external auditors) provide timely access to or copies of audit documentation when requested by insurance regulators. That guidance is as follows:

In the conduct of the aforementioned periodic review by the insurance department examiners, it shall be agreed that photocopies of pertinent audit workpapers may be made and retained by the department. Such reviews by the department examiners shall be considered investigations and all working papers and communications obtained during the course of such investigations shall be afforded the same confidentiality as other examination workpapers generated by the department.

Section 13 A of the MAR defines audit workpapers as follows:

Workpapers are the records kept by the independent certified public accountant of the procedures followed, the tests performed, the information obtained, and the conclusions reached pertinent to the accountant’s audit of the financial statements of an insurer. Workpapers, accordingly, may include audit planning documentation, work programs, analyses, memoranda, letters of confirmation and representation, abstracts of company documents and schedules or commentaries prepared or obtained by the independent certified public accountant in the course of his or her audit of the financial statements of an insurer and which support the accountant’s opinion.

Although the MAR requires that CPA firms provide “photocopies” of their workpapers, in response to requests from insurance regulators, the CPA firms have at times satisfied this regulatory requirement by providing audit workpapers in non-photocopy formats, including electronic copies of workpapers in a Portable Document Format (“PDF”) (i.e., the native files have been converted to PDF). Notwithstanding

the limit of the regulatory requirement to provide photocopies of audit workpapers, regulators have expressed a view that the provision of some workpapers (e.g., Excel spreadsheets) as a photocopy or in an electronic format such as PDF is not sufficient for their purposes due to an inability to view certain information, such as:

1. Information included in hidden columns or rows that can only be reviewed in native format.
2. Information imbedded in formulas or comment boxes that can only be reviewed in native format.
3. Information that is difficult to utilize due to formatting issues associated with generation of PDF documents (e.g. illegible font sizes, large spreadsheets breaking over many pages, etc.).

Because of the inability to access and utilize information contained in electronic workpapers when presented in PDF form, regulators have asked the AICPA NAIC Task Force to suggest potential accommodations for regulator access to audit documentation.

The following list of best practices to be considered by both CPA firms and insurance regulators attempts to balance regulators' needs, examination efficiency, the ability of auditors and companies to prevent access to auditors' workpapers by unauthorized persons, and the requirement for auditors to maintain control over audit documentation as required by generally accepted auditing standards. These best practices are not meant to and do not change the scope of the actual regulatory requirements incumbent on audit firms, which are contained in each state's law.

#### **CPA Firms:**

It is suggested that CPA Firms consider the following actions:

- At the outset of the regulatory examination, when feasible, provide the insurance regulators with secure, remote access to view read-only versions of the audit workpapers and make appropriate staff available to address questions, which may allow the insurance regulators to be more selective in requesting copies of any individual workpapers.
- To the extent that workpapers are requested by insurance regulators in a common native format (i.e., a file format associated with widely available commercial word processing or spreadsheet software, such as Microsoft Word or Excel) as opposed to converting to PDF, determine whether additional security measures are appropriate, including, for example, password protection on a CD of individual files or USB drive, to prevent access by unauthorized persons (Insurance regulators strongly discourage password protection directly on individual workpapers to avoid usability issues).
- When providing regulators with workpapers, include a disclosure stating that original workpapers are maintained/owned by the CPA firm, and that the CPA firm expressly disclaims any responsibility for any alteration of files, reports which may be created from such files such as additional test items added to an insurer's or auditor's Excel spreadsheet, and any reliance which may be placed on such alterations to the workpaper files.

#### **Insurance Regulators:**

When requesting access to audit documentation, it is suggested that insurance regulators consider the following actions:

- Have a planning meeting with relevant engagement team members from the CPA Firm to facilitate the workpaper review, including gaining an understanding of:
  - CPA firm audit approach and how to utilize electronic workpapers
  - Key risk areas
  - Expected reliance on internal controls
  - Timing of external audit internal controls testing, and
  - Availability of workpapers
- Consider the scope of what workpapers are necessary for the examination by reviewing the audit workpapers before requesting copies (photocopies, PDF and/or native formats) of any workpapers. In particular, consider whether a request for all workpapers without reviewing the audit files is necessary and efficient. To the extent electronic copies of audit workpapers in native format (e.g., Excel spreadsheets) might be preferable, recognize that such request goes

beyond the regulatory requirements imposed by the law, also recognizing that the original workpaper must be legible in photocopy or PDF form.

- Communicate with the CPA firm and local engagement team members on matters related to workpaper access and copies, before involving the insurer<sup>1</sup>.
- For coordinated examinations involving more than one regulatory entity, consider improving coordination among the various regulators to review all applicable legal entities' workpapers at the same time.

\*\*\*

As stated in Section 13 of the MAR, the review by insurance department examiners of workpapers prepared by the independent certified public accountant in the conduct of the audit and any communications related to the audit between the independent certified public accountant and the insurer shall be considered investigations and all workpapers and communications obtained from the CPA Firm during the course of such investigations shall be afforded the same confidentiality as other examination workpapers generated by the department.

---

<sup>1</sup> In 2003 the AICPA/ NAIC Working Group (with assistance from the AICPA NAIC Task Force) developed and adopted a process, for external auditors and financial examiners related to access to audit documentation, that also included a list of individuals that the financial examiner should contact in the event of any issues. This information was included in the AICPA Audit Risk Alert – Insurance Industry Developments 2007/08 and has also been integrated into the NAIC's Financial Examiners Handbook. That information is attached in Appendix A.

## Appendix A

In 2003 the AICPA/ NAIC Working Group (with assistance from the AICPA NAIC Task Force) developed and adopted a process (below) for auditors and financial examiners related to access to audit documentation that included a list of individuals that the financial examiner should contact in the event of any issues.

This information was included in the AICPA Audit Risk Alert – Insurance Industry Developments 2007/08 and has also been integrated into the NAIC’s Financial Examiners Handbook. It was emphasized that this process would be informal, non-authoritative, and non-binding. The AICPA NAIC Task Force envisioned that the adoption of this process would be additive to the remedies available to insurance regulators. The benefits of this additive process would (1) help enhance communication between regulators and independent certified public accountants, (2) improve the effectiveness of obtaining access to audit workpapers on a timely basis, and (3) assist in strengthening the quality of statutory audits.

### Reminder—Access to CPA Audit Documentation

An external auditor is required by the NAIC Model Audit Rule to provide timely access to or copies of audit documentation when requested by regulators.

Interpretation No. 1, “Providing Access to or Copies of Audit Documentation to a Regulator,” in AU section 9339, *Audit Documentation: Auditing Interpretations of Section 339* (AICPA, *Professional Standards*, vol. 1, AU sec. 9339.01–.15), addresses the responsibilities of an auditor when a regulator requests access to audit documentation. Auditors should note that PCAOB Auditing Standard No. 3, *Audit Documentation* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, “Standards”), supersedes AU section 339, *Audit Documentation* (AICPA, *Professional Standards*, vol. 1), for audits of public companies and other issuers.

The AICPA’s task force on NAIC matters has worked actively with subgroups consisting of designated regulators and NAIC representatives to pursue ways to increase the examiners’ reliance upon the statutory audit and use of underlying audit documentation. Suggested protocols were forwarded to the Financial Examiners Handbook Technical Group for consideration of possible revisions to the Examiners Handbook and have been incorporated into the Handbook.

The AICPA NAIC Task Force helped to establish the four-step process to provide a protocol for financial examiners who are having difficulty pursuing a resolution of (1) questions with respect to a firm’s individual engagement to perform a statutory audit, (2) difficulties in gaining access to working papers, or (3) the regulator concerns about the work performed by the CPA. If a financial examiner determines that an additional response is required, after informing appropriate management, the financial examiner would contact the following individuals in this suggested order, as needed:

1. The engagement partner
2. The designated national firm representative (included on the NAIC website)
3. Chair of the insurer’s audit committee
4. State board of accountancy, ethics (or quality review) committee, or other regulatory bodies as deemed appropriate

Firms or individual practitioners performing statutory audits of regulated insurance entities that wish to designate a national firm representative and have not already done so should contact NAIC representatives at (816) 783-8006 or (816) 783-8132.