

191—5.25(505) Annual audited financial reports.

5.25(1) Purpose. The purpose of this rule is to improve the Iowa insurance division's surveillance of the financial condition of insurers by requiring an annual examination by independent certified public accountants of the financial statements reporting the financial position and the results of operations of insurers.

Every insurer (as defined in subrule 5.25(2), paragraph "c,") shall be subject to this rule. Insurers having direct premiums written in this state of less than \$1 million in any calendar year and less than 1,000 policyholders or certificate holders of directly written policies nationwide at the end of such calendar year shall be exempt from this rule for such year (unless the commissioner makes a specific finding that compliance is necessary for the commissioner to carry out statutory responsibilities) except that insurers having assumed premiums pursuant to contracts or treaties of reinsurance of \$1 million or more will not be so exempt.

Foreign or alien insurers filing audited financial reports in another state, pursuant to such other state's requirement of audited financial reports which has been found by the commissioner to be substantially similar to the requirements herein, are exempt from this rule if:

a. A copy of the Audited Financial Report, Report on Significant Deficiencies in Internal Controls, and the Accountant's Letter of Qualifications which are filed with such other state are filed with the commissioner in accordance with the filing dates specified in subrules 5.25(3), 5.25(10), and 5.25(11), respectively (Canadian insurers may submit accountants' reports as filed with the Canadian Dominion Department of Insurance).

b. A copy of any Notification of Adverse Financial Condition Report filed with such other state is filed with the commissioner within the time specified in subrule 5.25(9).

This rule shall not prohibit, preclude or in any way limit the commissioner of insurance from ordering or conducting or performing examinations of insurers under the rules of the division of insurance and the practices and procedures of the division of insurance.

5.25(2) Definitions. As used in this rule:

"Audited financial report" means and includes those items specified in subrule 5.25(4).

"Accountant" or *"independent certified public accountant"* means an independent certified public accountant or accounting firm in good standing with the American Institute of CPAs and in all states in which they are licensed to practice; for Canadian and British companies, it means a Canadian-chartered or British-chartered accountant.

"Indemnification" means an agreement of indemnity or 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.

"Insurer" means a licensed insurer under Title XIII of the Iowa Code, except entities organized under Iowa Code chapters 512A, 512B, 518, and 518A.

5.25(3) Filing and extensions for filing of annual audited financial reports. All insurers shall have an annual audit by an independent certified public accountant and shall 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 90 days' advance notice to the insurer.

Extensions of the June 1 filing date may be granted by the commissioner for 30-day periods upon showing by the insurer and its independent certified public accountant the reasons for requesting such extension and determination by the commissioner of good cause for an extension. The request for extension must be submitted in writing not less than ten days prior to the due date in sufficient detail to permit the commissioner to make an informed decision with respect to the requested extension.

5.25(4) Contents of annual audited financial report. 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 division of insurance of the state of domicile.

The annual audited financial report shall include the following:

- a. Report of independent certified public accountant.
- b. Balance sheet reporting admitted assets, liabilities, capital and surplus.
- c. Statement of operations.
- d. Statement of cash flows.
- e. Statement of changes in capital and surplus.
- f. Notes to financial statements. These notes shall be those required by the appropriate National Association of Insurance Commissioners (NAIC) annual statement instructions and the NAIC accounting practices and procedures manual. The notes shall include:

(1) A reconciliation of differences, if any, between the audited statutory financial statements and the annual statement filed pursuant to Iowa Code sections 508.11 and 515.63 with a written description of the nature of these differences.

(2) A summary of ownership and relationships of the insurer and all affiliated companies.

g. 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, and 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.)

5.25(5) *Designation of independent certified public accountant.* Each insurer required by this rule to file an annual audited financial report must, within 60 days after becoming subject to such requirement, register with the commissioner in writing the name and address of the independent certified public accountant or accounting firm (generally referred to in this rule as the “accountant”) retained to conduct the annual audit set forth in this rule. Insurers not retaining an independent certified public accountant on August 28, 1991, shall register the name and address of their retained certified public accountant not less than six months before the date when the first audited financial report is to be filed.

The insurer shall obtain a letter from the accountant, and file a copy with the commissioner, stating that the accountant is aware of the provisions of Title XIII of the Iowa Code and administrative rules thereunder that relate to accounting and financial matters and affirming that the accountant will express an opinion on the financial statements in terms of their conformity to the statutory accounting practices prescribed or otherwise permitted by the insurance division, specifying such exceptions as the accountant may believe appropriate.

If an accountant who was the accountant for the immediately preceding filed audited financial report is dismissed or resigns, the insurer shall within five business days notify the division of this event. The insurer shall also furnish the commissioner with a separate letter within ten business days of the above notification stating whether in the 24 months preceding such event there were any disagreements with the former accountant on any matter of accounting principles or practices, financial statement disclosure, or 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 opinion. The disagreements required to be reported in response to this rule include both those resolved to the former accountant’s satisfaction and those not resolved to the former accountant’s satisfaction. Disagreements contemplated by this rule are those that occur at the decision-making level, i.e., 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 such 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 the disagreement; and the insurer shall furnish such responsive letter from the former accountant to the commissioner together with its own.

5.25(6) *Qualifications of independent certified public accountant.*

a. The commissioner shall not recognize any person or firm as a qualified independent certified public accountant that:

(1) Is not in good standing with the American Institute of CPAs and in all states in which the accountant 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 herein, independent certified public accountants shall be recognized as qualified as long as they conform to the standards of their profession, as contained in the Code of Professional Ethics of the American Institute of Certified Public Accountants and rules and regulations and code of ethics and rules of professional conduct of the Iowa accountancy examining board, 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 Iowa Code chapter 507C, the mediation or arbitration provisions shall operate at the option of the statutory successor.

d. No partner or other person responsible for rendering a report may act in that capacity for more than seven consecutive years. Following any period of service such 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 years. An insurer may make application to the commissioner for relief from the above rotation requirement on the basis of unusual circumstances. The commissioner may consider the following factors in determining if the relief should be granted:

(1) Number of partners, expertise of the partners or the number of insurance clients in the currently registered firm;

(2) Premium volume of the insurer; or

(3) Number of jurisdictions in which the insurer transacts business.

The requirements of this paragraph became effective on August 28, 1993.

e. The commissioner shall not recognize as a qualified independent certified public accountant, or accept any annual audited financial report prepared in whole or in part by, any natural person who:

(1) Has been convicted of fraud, bribery, a violation of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. Sections 1961-1968, or any dishonest conduct or practices under federal or state law;

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

(3) Has 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 of insurance, under 191—Chapter 3, may hold a hearing to determine whether a certified public accountant is qualified and, considering the evidence presented, may rule that the accountant is not qualified for purposes of expressing the opinion of the accountant on the financial statements in the annual audited financial report made pursuant to this rule and require the insurer to replace the accountant with another whose relationship with the insurer is qualified within the meaning of this rule.

5.25(7) Consolidated or combined audits. 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 is part of a group of insurance companies which utilizes a pooling or 100 percent reinsurance agreement that affects the solvency and integrity of the insurer's reserves and such insurer cedes all of its direct and assumed business to the pool. In such cases, a columnar consolidating or combining worksheet shall be filed with the report as follows:

a. Amounts shown on the consolidated or combined audited financial report shall be shown on the worksheet.

b. Amounts for each insurer subject to this rule shall be stated separately.

c. Noninsurance operations may be shown on the worksheet on a combined or individual basis.

d. Explanations of consolidating and eliminating entries shall be included.

e. A reconciliation shall be included 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.

5.25(8) *Scope of examination.* Financial statements furnished pursuant to subrule 5.25(4) shall be examined by an independent certified public accountant. The examination of the insurer's financial statements shall be conducted in accordance with generally accepted auditing standards. Consideration should also be given to such other procedures illustrated in the Financial Condition Examiner's Handbook promulgated by the National Association of Insurance Commissioners as the independent certified public accountant deems necessary.

5.25(9) *Notification of adverse financial condition.* The insurer required to furnish the annual audited financial report shall require the independent certified public accountant to report, in writing, within five business days to the board of directors or its audit committee any determination by the independent certified public accountant that the insurer has materially misstated its financial condition as reported to the commissioner as of the balance sheet date currently under examination or that the insurer does not meet the applicable minimum capital and surplus requirements of Iowa Code sections 508.5, 508.10, 515.8, 515.10 and subsection 515.12(5) as of that date. An insurer who has received a report pursuant to this paragraph shall forward a copy of the report to the commissioner within five business days of receipt of such 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 such evidence within the required five-business-day period, the independent certified public accountant shall furnish to the commissioner a copy of its report within the next five business days.

No independent public accountant shall be liable in any manner to any person for any statement made in connection with the above paragraph if such statement is made in good faith in compliance with the above paragraph.

If the accountant, subsequent to the date of the audited financial report filed pursuant to this rule, becomes aware of facts which might have affected this report, the insurance division notes the obligation of the accountant to take such action as prescribed in Volume 1, Section AU561 of the Professional Standards of the American Institute of Certified Public Accountants.

5.25(10) *Report on significant deficiencies in internal controls.* In addition to the annual audited financial statements, each insurer shall furnish the commissioner with a written report prepared by the accountant describing significant deficiencies in the insurer's internal control structure noted by the accountant during the audit. SAS No. 60, Communication of Internal Control Structure Matters Noted in an Audit (AU section 325 of the Professional Standards of the American Institute of Certified Public Accountants) requires an accountant to communicate significant deficiencies (known as "reportable conditions") noted during a financial statement audit to the appropriate parties within an entity. No report should be issued if the accountant does not identify significant deficiencies. If significant deficiencies are noted, the written report shall be filed annually by the insurer with the insurance division within 60 days after the filing of the annual audited financial statements. The insurer is required to provide a description of remedial actions taken or proposed to correct significant deficiencies, if such actions are not described in the accountant's report.

5.25(11) *Letter furnished to insurer.* The accountant shall furnish the insurer, in connection with, and for inclusion in, the filing of the annual audited financial report, a letter stating:

a. That the accountant is independent with respect to the insurer and conforms to the standards of the profession as contained in the Code of Professional Ethics and pronouncements of the American Institute of Certified Public Accountants and the rules of professional conduct of the Iowa accountancy examining board, or similar code.

b. The background and experience in general, and 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 is deemed appropriate where use is consistent with the standards prescribed by generally accepted auditing standards.

c. That the accountant understands the annual audited financial report and the 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.

d. That the accountant consents to the requirements of subrule 5.25(12) and that the accountant consents and agrees to make available for review by the commissioner, or a designee or appointed agent, the workpapers, as defined in subrule 5.25(12).

e. A representation that the accountant is properly licensed by an appropriate state licensing authority and is a member in good standing in the American Institute of Certified Public Accountants.

f. A representation that the accountant is in compliance with the requirements of subrule 5.25(6).

5.25(12) *Definition, availability and maintenance of CPA workpapers.* Workpapers are the records kept by independent certified public accountants of the procedures followed, the tests performed, the information obtained, and the conclusions reached pertinent to their examination 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 independent certified public accountants in the course of their examination of the financial statements of an insurer and which support their opinions thereof.

Every insurer required to file an audited financial report pursuant to this rule shall require the accountant to make available for review by insurance division examiners all workpapers prepared in the conduct of the examination and any communications related to the audit between the accountant and the insurer, at the offices of the insurer, at the insurance division, or at any other reasonable place designated by the commissioner. The insurer shall require that the accountant retain the audit workpapers and communications until the insurance division has filed a report on examination covering the period of the audit but no longer than seven years from the date of the audit report.

In the conduct of the aforementioned periodic review by insurance division examiners, it shall be agreed that photocopies of pertinent audit workpapers may be made and retained by the division. Such reviews by the division 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 division.

5.25(13) *Exemption from compliance.* Upon written application of any insurer, the commissioner may grant an exemption from compliance with 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 days from a denial of an insurer's written request for an exemption from this rule, such insurer may request in writing a hearing on its application for an exemption. Such hearing shall be held in accordance with 191—Chapter 3.

Domestic insurers retaining a certified public accountant on August 28, 1991, who qualify as independent shall comply with this rule for the year ending December 31, 1992, and each year thereafter unless the commissioner permits otherwise.

Domestic insurers not retaining a certified public accountant on August 28, 1991, who qualify as independent may meet the following schedule for compliance unless the commissioner permits otherwise:

a. As of December 31, 1992, file with the commissioner:

- (1) Report of independent certified public accountant;
- (2) Audited balance sheet;
- (3) Notes to audited balance sheet.

b. For the year ending December 31, 1992, and each year thereafter, such insurers shall file with the commissioner all reports required by this rule.

Foreign insurance shall comply with this rule for the year ending December 31, 1992, and each year thereafter unless the commissioner permits otherwise.

5.25(14) *Canadian and British companies.* 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

such companies with their domiciliary supervision authority duly audited by an independent chartered accountant.

For such insurers, the letter required in subrule 5.25(5) shall state that the accountant is aware of the requirements relating to the annual audited statement filed with the commissioner pursuant to subrule 5.25(3).

This rule is intended to implement Iowa Code section 505.8.