

Model Audit Rule: Lessons learned from Implementation, Examination and Audit

Meet your presenters



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Today's topics

Understand the Model Audit Rule (MAR): Gain a comprehensive understanding of the internal control over financial reporting requirements under the Model Audit Rule (MAR) for insurers.

Identify Key Regulatory Compliance Requirements: Recognize the key compliance requirements for insurers approaching or exceeding \$500M in direct and assumed written premiums.

Prepare for MAR Implementation: Learn the necessary steps to implement an effective MAR program, ensuring alignment with regulatory expectations and industry best practices.

Optimize Existing MAR Programs: Explore strategies for evolving and optimizing an existing MAR program to enhance organizational value.

Align MAR Programs with Organizational Strategy: Define and align MAR program objectives with the broader goals of the organization for a strategic approach to compliance.

Discuss Industry Trends and Lessons Learned: Review industry trends, lessons learned, and common misconceptions regarding MAR implementation and evolution.

Takeaways for Different Stages of MAR: Identify key takeaways and considerations for insurers at various stages of their MAR journey, from initial implementation to program maturation.



Polling results from our last MAR webinar

What trend do you think will have the greatest impact on MAR compliance in the next three to five years?

- a) Automation of controls enabling reduction in sample requirements – **19%**
- b) Continuous monitoring and additional use of computer-assisted audit techniques – **17%**
- c) Unforeseen changes to regulatory requirements – **5%**
- d) Additional leverage of department resources to fulfill requirements – **3%**
- e) All of the above – **50%**

What trend has the greatest impact on the efficiency and effectiveness of your MAR program?

- a) Self-assessments – **18%**
- b) Utilization of a GRC system – **9%**
- c) Use of third-party consultants to assist – **11%**
- d) Improved project management – **18%**
- e) Rotational auditing – **20%**

What is your top challenge with maximizing the efficiency and effectiveness of your MAR program?

- a) Not maximizing reliance by our external auditor resulting in duplication of effort – **4%**
- b) Obtaining support from department personnel to take on the requirement of testing instead of a dedicated internal audit/compliance/SOX group – **15%**
- c) Identifying the “right amount” of key controls, as we have more key controls than we probably need – **26%**
- d) All of the above – **34%**



Model Audit Rule requirements



Where are you in your MAR journey?

- a) In the beginning stages of learning about MAR but do not have to be MAR compliant in the next few years
- b) Planning for MAR compliance implementation within the next one to three years
- c) Currently MAR compliant and always looking for ways to improve
- d) Currently MAR compliant, but may need to be SOX compliant in the next few years
- e) None of the above
- f) Not applicable



Model Audit Rule – summary of requirements

Applicable model

Annual Financial Reporting Model 205

Section 17 – Management’s Report of Internal Control over Financial Reporting Annual attestation on internal control

Purpose

To provide regulators greater confidence in accuracy of financial reporting

Increase efficiency of risk-focused examinations

Increase management’s confidence in internal controls

About the report

Statement that management is responsible for establishing and maintaining internal control

Statement that management has established internal control and whether management believes that internal control is effective

Brief description of the approach used to evaluate effectiveness

Scope of work and any excluded controls

“Bridge report” required for SOX compliant issuers

Disclosure of any unremediated material weaknesses in internal control as of Dec. 31, 20XX

Statement regarding any inherent limitations of internal control

Signatures of the CEO and CFO

Applicable threshold and filing timeline

Threshold: Direct written and assumed premium equal to or greater than \$500 million

Filing: Typically 60 days after Audited Financial report is filed, at the latest Aug. 1, with the exception of NYDFS that requires submission by May 31

Auditor and SOX attestation

- Independent audit attestation is not required. The auditor is required to disclose unremediated material weaknesses in a filing to the commissioner
- Can leverage SOX attestation. Still have to file SOX report, but include an addendum stating all MAR internal controls were included in scope of SOX report

Effective dates

Two calendar years from exceeding the threshold

\$ millions	201x	201x+1	201x+2	201x+3
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7
Add: Reinsurance ceded	100.5	115.7	115.8	120.1
Gross direct written and assumed premium	450.8	506.5	526.3	545.8

Exemptions and waivers

- Carriers under \$500M are exempt from requiring but the commissioner has authority to require compliance
- Hardship waiver is available, must determine reasons for hardship under section 17 (18), contact your financial analyst, file a written application for waiver, and receive approval for exemption (usually a year)



MAR overview

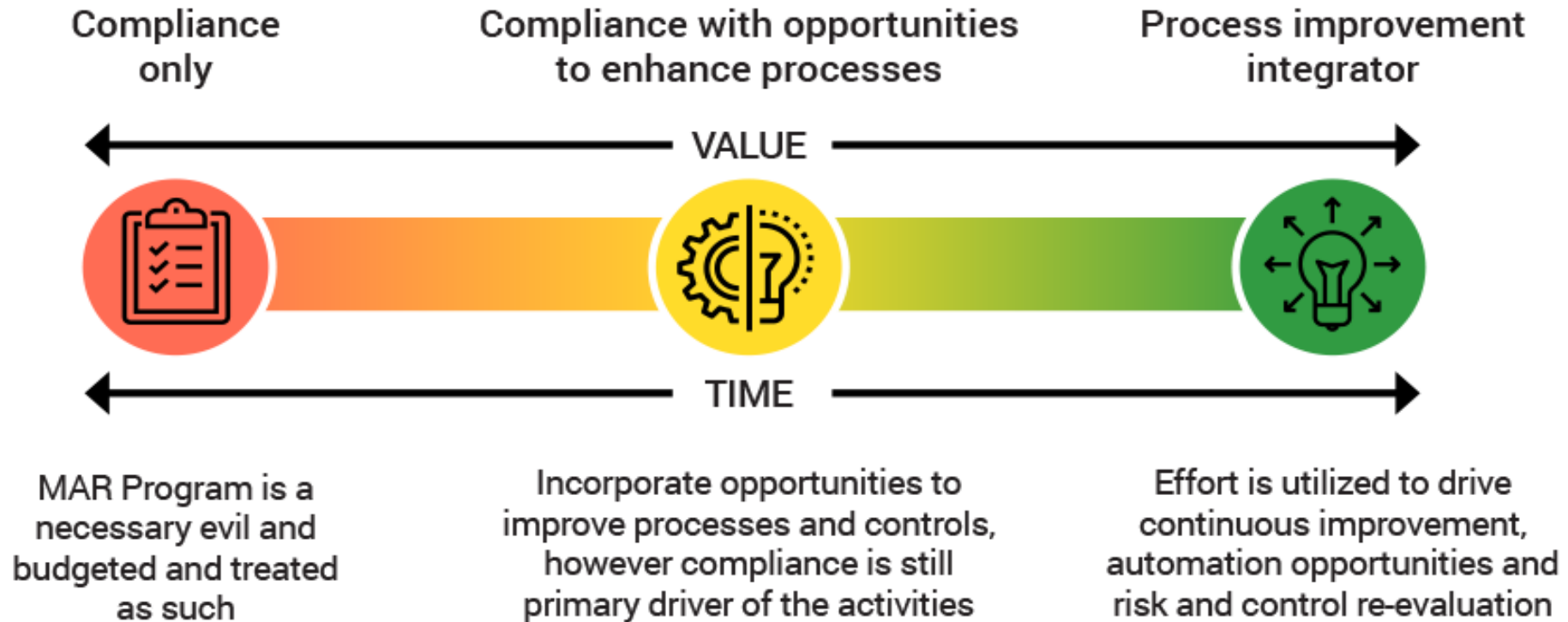
Management's responsibility for diligent inquiry:

- Section 17D(2) states that management's assertion regarding the effectiveness of the insurer's financial reporting controls must be made to the best of their knowledge after diligent inquiry
- Defining diligent inquiry according to the Model Audit Rule implementation guide:

For purposes of filing the report, **diligent inquiry** means conducting a search and thorough review of relevant documents which are reasonably likely to contain significant information with regards to internal control over financial reporting and making reasonable inquiries of current employees and agents whose duties include responsibility for internal control over financial reporting

Industry perspectives and viewpoints

Company perspectives and a tale of two clients:



Industry perspectives and viewpoints



Regulator:

- Adequacy of MAR is addressed during examinations
- Material weakness identification is followed up on when reported. May result in an increase in priority scoring



External audit:

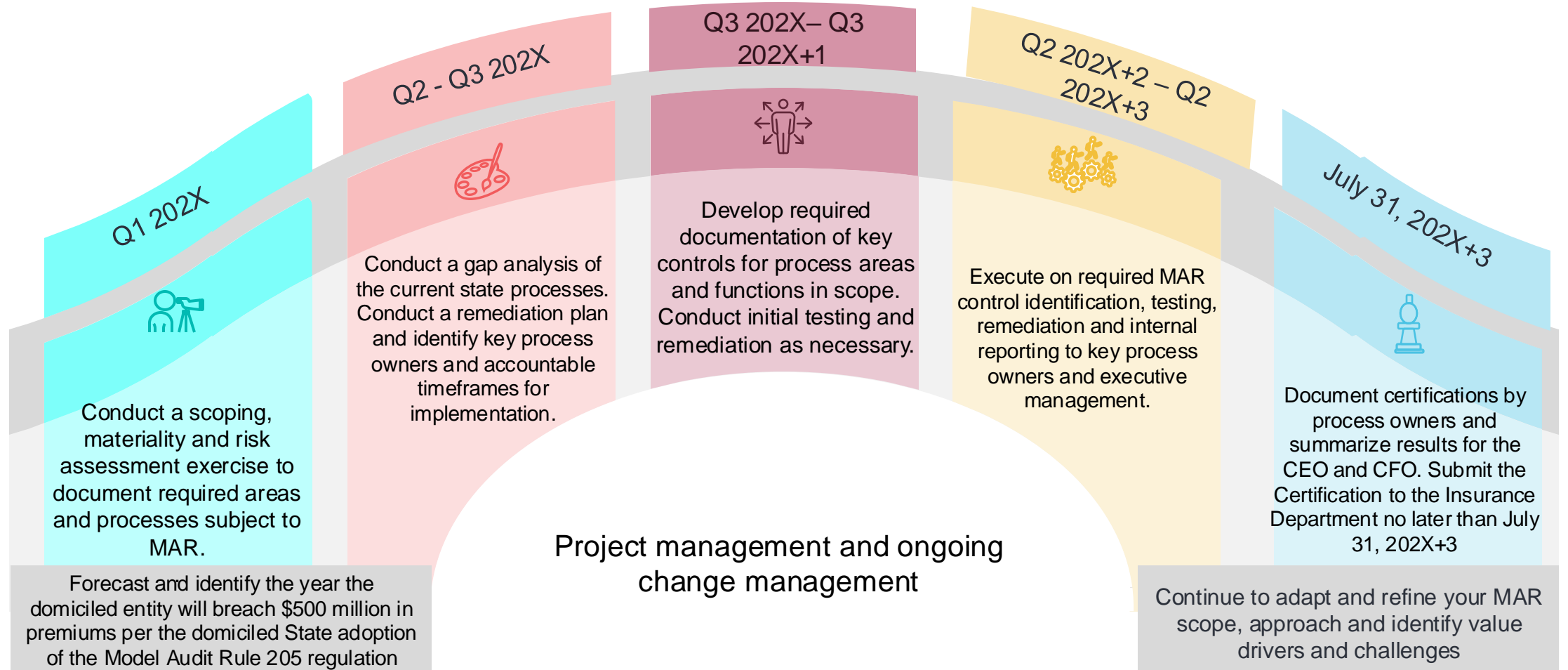
- Not required to report on the effectiveness of internal controls/MAR program
- Most auditors (non-SOX companies but large insurance groups) exhibit the following:
 - Use of internal audit/MAR team members for direct assistance
 - Rely on controls for some key areas, set control risk to maximum in critical areas
 - Use MAR documentation to assist within the audit but it doesn't create significant efficiencies due to increased scrutiny on control reliance

Implementation roadmap summary

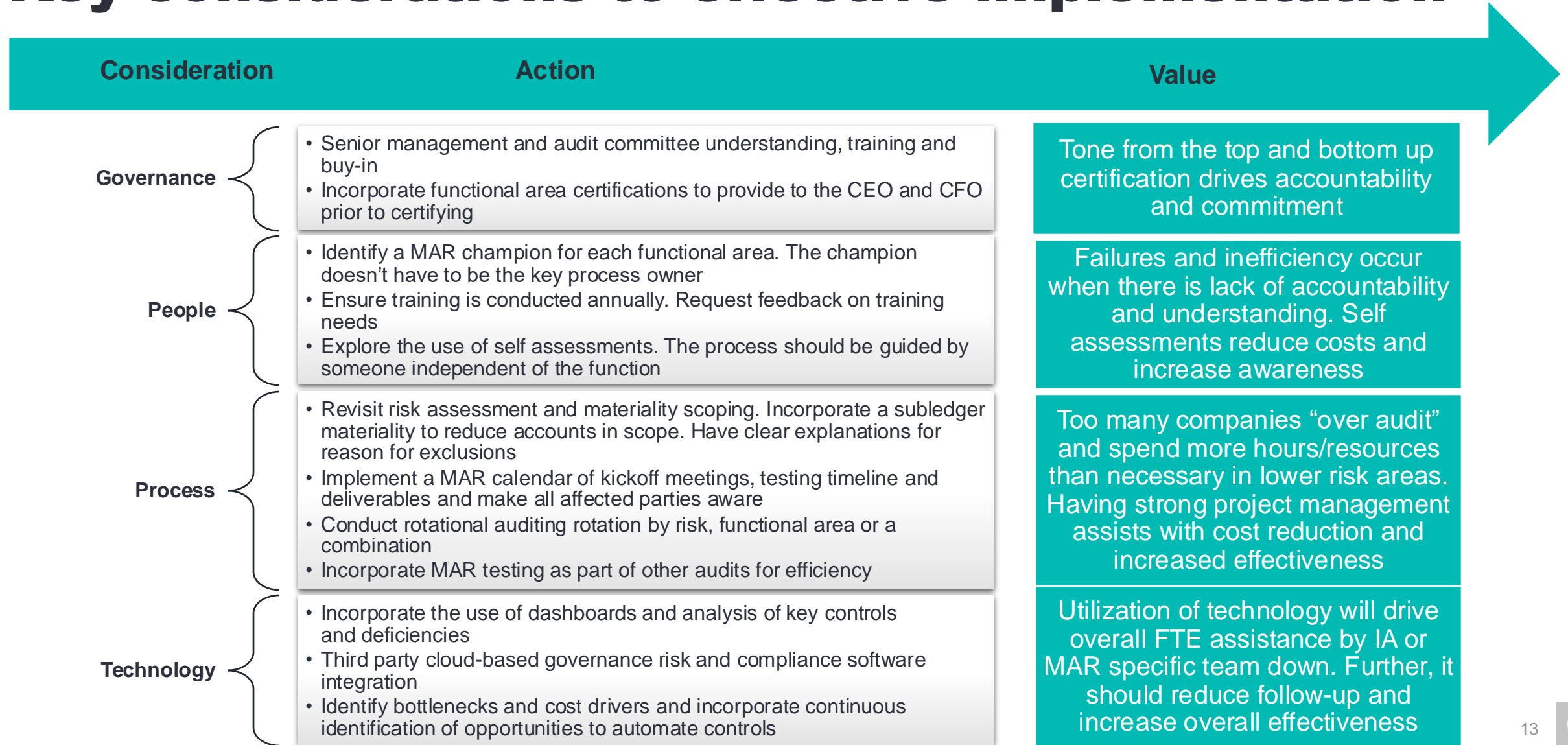
New implementation roadmap

Summary

Company (State of Domicile)	Year End Expected to Breach \$500M	Year-end MAR Certification Required	Filing of Certification Deadline
Company	202X	202X+2	7/31/202X+3



Key considerations to effective implementation



How many hours/Full time equivalents (FTEs) do you dedicate to your MAR compliance efforts annually?

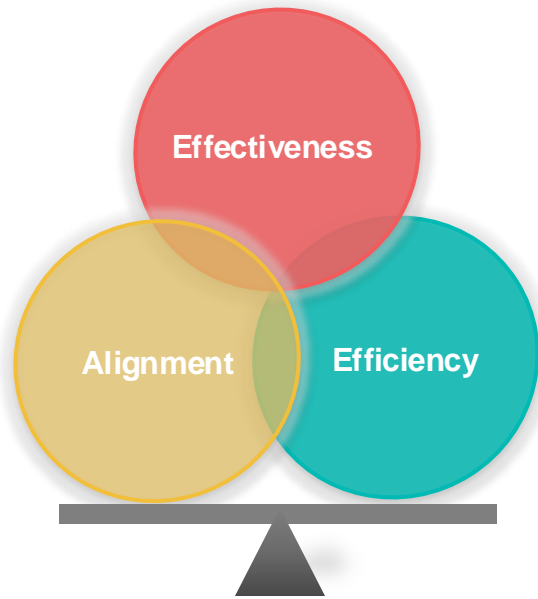
- a) None, we haven't started implementation yet
- b) 501 – 1,500 (1 FTE or less)
- c) 1,501 – 3,000 (2 FTEs)
- d) 3,001 – 4,500 (3 FTEs)
- e) 4,500+ (4 FTEs+)
- f) Unsure
- g) Not applicable

Considerations in addressing requirements for the basis for management's review and assertions

What is your top challenge in maximizing the efficiency and effectiveness of your MAR program?

- a) Identifying the “right amount” of key controls, as we have more key controls than we probably need and may be missing others
- b) Time of resources (internal audit, MAR team, business owners, etc.) to dedicate to improving the existing processes
- c) Being viewed by business owners as a compliance exercise
- d) People and change management, the lack of ability to change resulting in doing things “the same old way”
- e) None of the above
- f) Not applicable

Business process



Key considerations include balancing effectiveness, efficiency and alignment to optimize their financial reporting and internal control assessment efforts

Alignment

- Risk analysis
- Materiality scoping

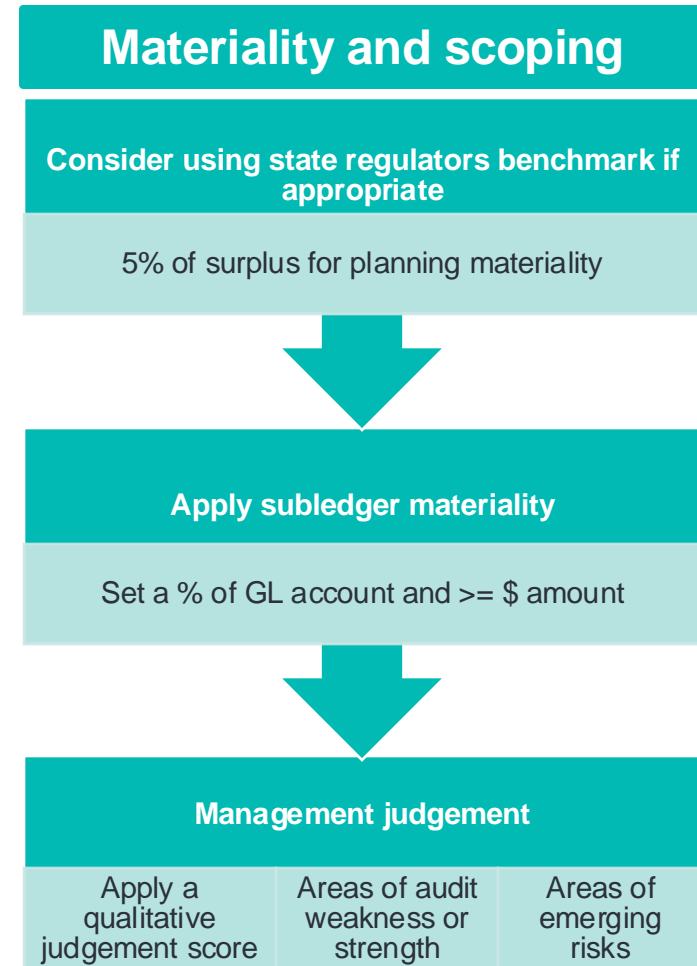
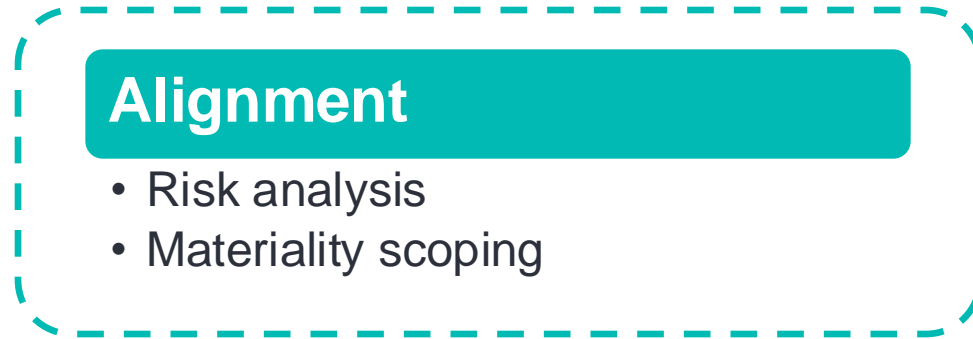
Efficiency

- Rotational auditing
- Self-assessments
- State examination/NAIC risk matrix approach

Effectiveness

- Key control and compensating control assessments
- Proper deficiency evaluation
- Dashboards, understand broader impact of results

Business process alignment



Business process efficiency

Efficiency

- Rotational auditing
- Self-assessments
- State examination/NAIC risk matrix approach

Ex. A - Claims administration

Risk	Risk assessment	Key control	Test frequency
Risk A	High	CLM1 – monthly	Annually
Risk B	Low	CLM2 - quarterly	Every two years

Ex. B - Function

Function	Risk assessment	Testing frequency
Claims and benefits	High	Annually
Policy loans	Moderate	Once every three years (self assessment)

Rotational auditing

- Risk-based within the functions (Ex. A)
 - Should reduce key control testing requirement but may require more support and explanation
- Function based on risks results (Ex. B) – more common
- Combination – would have largest efficiency impact, but may require more administration to track

Self-assessments

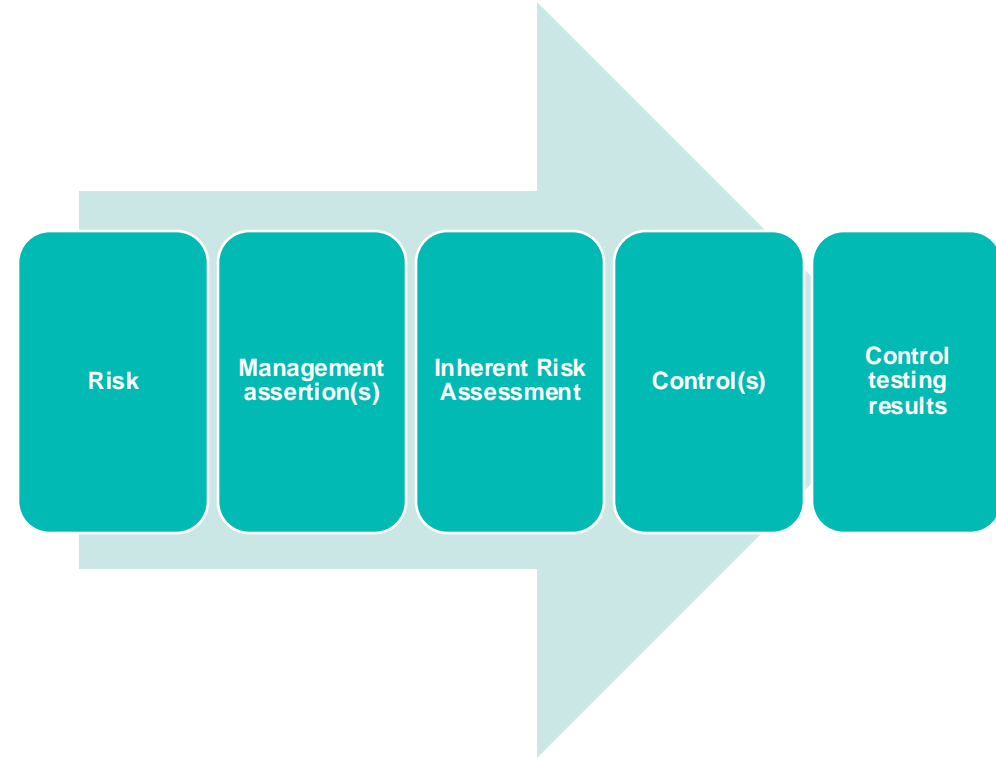
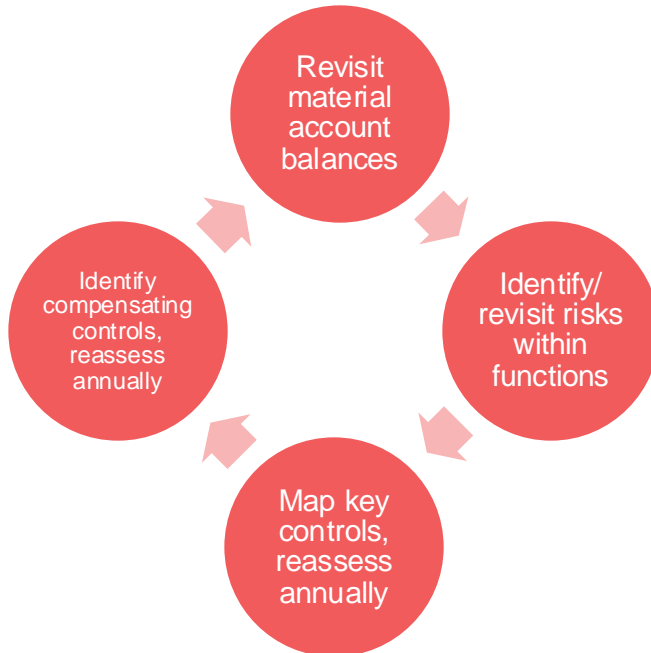
- Guided process
- Initially lower risk areas
- Rotational
- Internal audit verification
- Limit retention of documentation



Business process effectiveness

Effectiveness

- Key control and compensating control assessments
- Proper deficiency evaluation
- Dashboards, understand broader impact of results

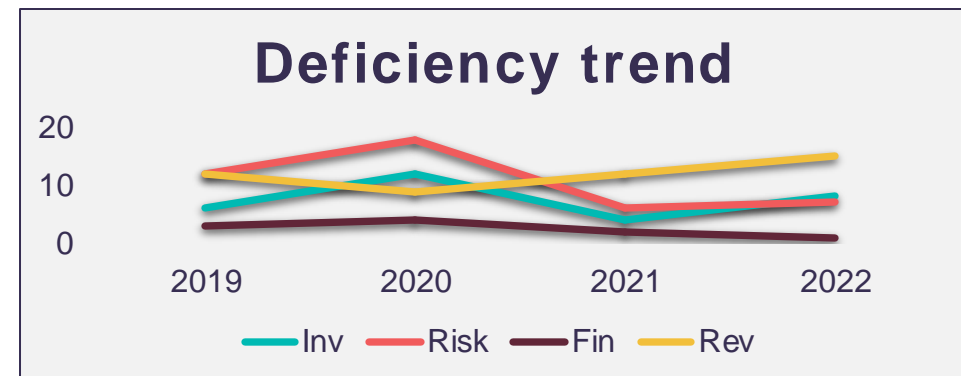
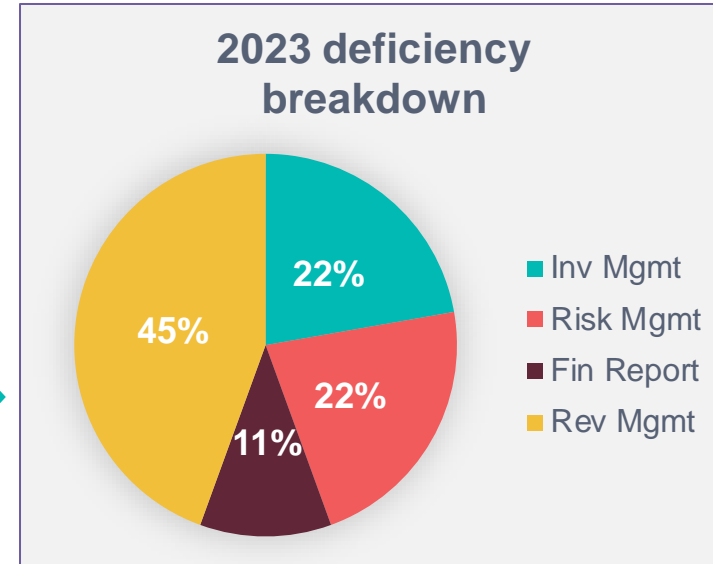
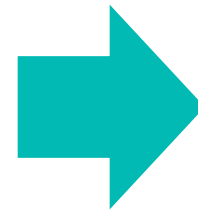


Set up and identify risks and controls in line with NAIC matrix approach. Consider speaking the same language as state regulators – which may also lead to a more efficient exam as well



Business process effectiveness

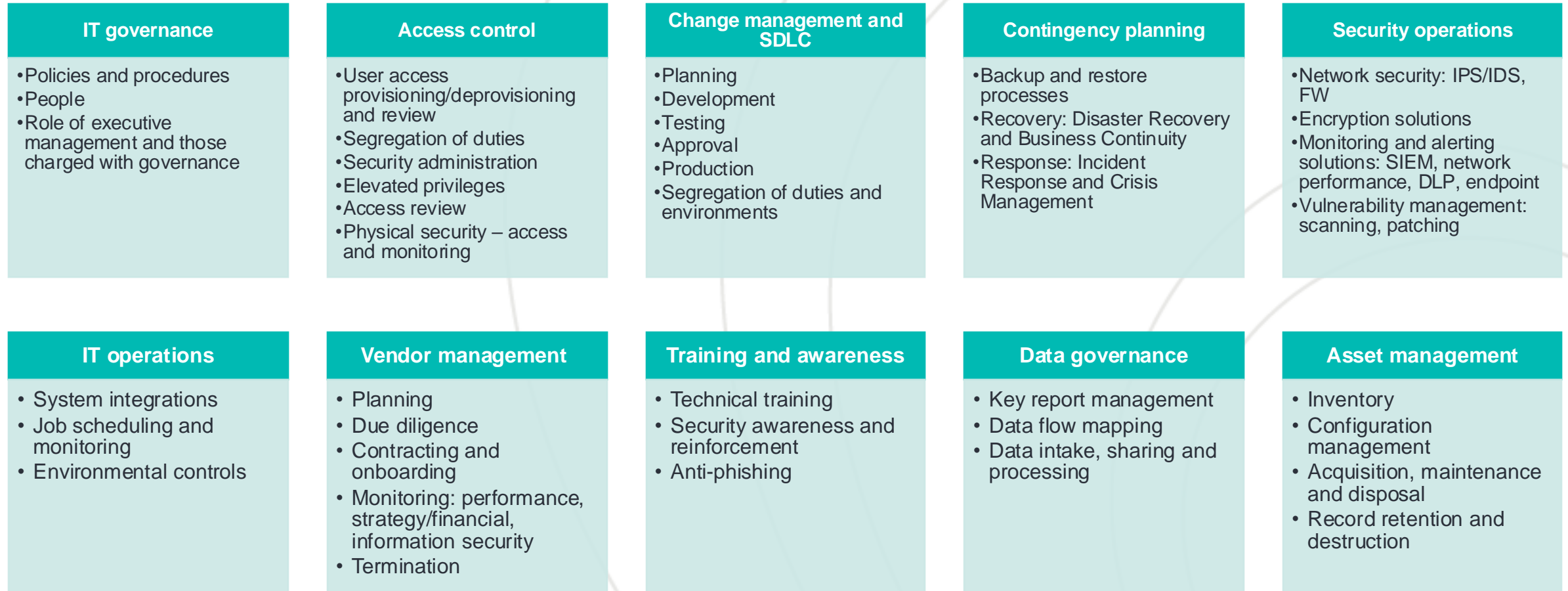
Function	Strategic function
Bond portfolio administration	Investment management
Stock portfolio administration	
Treasury	
Enrollment	Risk management
Claims administration	
IBNR and medical liabilities	
Tax accounting	Financial reporting
STAT reporting	
Provider incentives	Revenue management
Pharmacy rebates	
Member premium billing	



Information technology considerations and viewpoints



Information technology (IT) - scoping considerations



IT efficiency AND IT effectiveness

Risk-based IT system scoping

- Volume of users
- On premise vs hosted
- Volume of transactions
- Financial impact
- Level of automation/controls
- Down stream detective controls

Leverage other assessments

- Internal Audit
- SOC examinations
- HITRUST
- ISO
- NIST CSF
- Etc.

Identify automated controls

- Business process
 - Field edits
 - Data validation – process errors
 - Exception/anomaly reporting
 - Disbursement authority
- Information technology (IT)
 - Backup failure reporting
 - Segregation of duties
 - Role-based access
 - Access provisioning automation

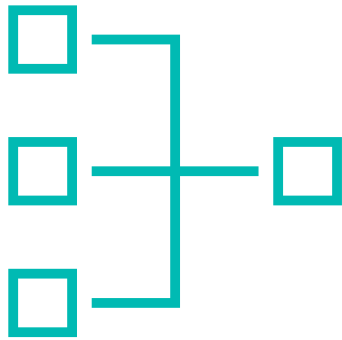
Completeness and accuracy

- IPE – Information Provided by the Entity
- Key reports
- Enables reliance and/or re-performance
- Identify issues and assess impact
- Accuracy of control performance (e.g., use of scripts to identify period over period permission changes within applications)



IT systems scoping considerations

System identification



- On premise
- Hosted solutions
- Web applications

System assessment



- Financial impact – material financial statement line items
- Mapping of systems to financial statement line items
- Relevant risks to key systems

Other considerations



Data governance and integrity

Questions?

Stay in touch



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For more information on these topics, check out
<https://www.bakertilly.com/specialties/model-audit-rule>

