



HELP! I'M BEING AUDITED

AGENDA

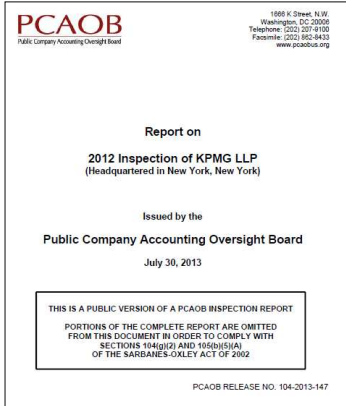

- Audit Mindset
- Audit Goals
- Audit Process
- Audit Approach
- Dealing with Auditors

The Audit Mindset

Controls	Detect & Prevent Errors <ul style="list-style-type: none"> ▪ Review ▪ Authorization ▪ Restriction ▪ Reconciliation ▪ Monitoring
Control Mindset	<ul style="list-style-type: none"> ▪ To err is human ... to really foul things up, you need an actuarial model ▪ Increasing complexity → Increasing likelihood of error
Assurance	<ul style="list-style-type: none"> ▪ Positive Assurance vs. Negative Assurance ▪ Absolute Assurance vs. Relative Assurance ▪ Assurance Level Drives Testing Level
Status Quo Doesn't Define Acceptable	<ul style="list-style-type: none"> ▪ Audit Evidence

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Audit Goals

Audit Goals vs. Operational Considerations	Regulatory Considerations	External Audit Considerations
 <p style="font-size: x-small; margin-top: 10px;">THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT PORTIONS OF THE COMPLETE REPORT ARE OMITTED FROM THIS DOCUMENT IN ORDER TO COMPLY WITH SECTIONS 106(g) AND 105(b)(5)(A) OF THE SARBANES-OXLEY ACT OF 2002</p> <p style="font-size: x-small; margin-top: 5px;">PCAOB RELEASE NO. 104-2013-147</p>	 <p style="font-size: 1.2em; font-weight: bold; color: white;">PCAOB Issues</p>	<ul style="list-style-type: none"> ▪ Chains of Reliance ▪ Insufficiency of Substantive Testing ▪ Others

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Typical Audit Goals

Audits are long-duration projects resulting in an audit report, whose conclusions are supported by audit evidence.

Typical Stakeholders	Typical Audit Report Elements
Regulator	Explanation of audit scope and approach
External auditor	Workpapers generated from audit evidence
Internal auditor	Audit findings
Counterparty	Conclusion/rating and recommendations

Typical audit covers controls, operational effectiveness, and governance.

Goal is to give the client assurance about operational effectiveness.

Understanding the auditor's stakeholders and goals helps optimize the audit.

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Typical Internal Audit Process

	Auditor Activities	Auditor-Client Interaction
Planning	<ul style="list-style-type: none"> Understand the business Set initial audit objectives and scope Perform initial risk analysis Engagement memorandum 	<ul style="list-style-type: none"> Schedule the audit timing Agree on scope and objectives with management
Design	<ul style="list-style-type: none"> Analyze risks and controls Concentrate on material risks Document business process and controls Control design evaluation Develop test plan including sample 	<ul style="list-style-type: none"> Interact with management to analyze procedures and controls Promptly communicate issues Partner with management to determine risks and control mitigations
Testing	<ul style="list-style-type: none"> Test controls Test achievement of business objectives Conclude on control design and effectiveness 	
Results	<ul style="list-style-type: none"> Present audit results, exposures, conclusions, and mitigations to senior management and BoD 	<ul style="list-style-type: none"> Discuss audit conclusions Confirm issues and mitigations Determine risk and control mitigations Identify the best control solutions Validate risk and control mitigations prior to closure
Closure	<ul style="list-style-type: none"> Survey client management Verify mitigations were performed Report overdue items to senior management 	

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Focus area: end-to-end transactions

Audit procedures often designed for an 'end-to-end' view: from contract inception to balance sheet entries

Auditor typically evaluates the successful application of management intentions clearly in the results, such as:

- Assumptions
- Accounting policy
- Risk management activities
- Derivatives usage policy, etc.
- Connection risks
- Consistency

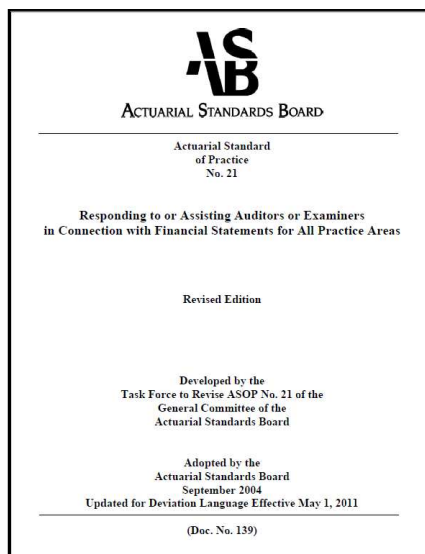


It's not always the complex operations which cause issues.

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Applicable Standards: ASOP 21



Responding to or Assisting Auditors or Examiners in Connection with Financial Statements for All Practice Areas, effective April 30, 2005 and revised as of May 1, 2011.

Applies to actuaries when providing professional services as a responding actuary or as a reviewing actuary, in connection with an audit or examination of a financial statement. Also:

ASOP 23

ASOP 41

ASB Exposure Draft on Modeling

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Applicable Standards: ASOP 21

“The responding actuary should be **appropriately responsive** to the auditor’s or examiner’s reasonable requests” and “prepared to discuss with the auditor or examiner...”

- **Data used, sources of assumptions, methods used, basis for assumptions** which are not prescribed
- **Circumstances** that had a significant effect on the preparation of financial statements such as changes in the operating environment, trends, changes in mix of business, changes in methods policies, and procedures, etc.



The reviewing actuary should “discuss the scope of the audit or examination with the auditor or examiner as well as the **nature, extent, and timing of the reviewing actuary’s procedures, including how the results of the review will be communicated.**”

Contains specific guidance on applying ASOP 41 to audit procedures.

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Approach Taken by Auditors

CPAs vs. FSAs

- Testing
- Documentation
- Review of Controls

Coordination Among Multiple Auditors

- Within same audit team
- Across different audit teams

Typical Audit Testing

- Recalculations
- Directed Sensitivity Tests
- Tests of controls
- Walk through
- Review & Testing of Experience studies
- Reconciliation to Ledger
- Quantification of Unlocking or Assumption Change
- Tests of reinsurance
- Test of changes in credited interest or dividends

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Approach Taken by Auditors (continued...)

Sampling Approach

- Risk-based sampling
- Incremental sampling
- Random sampling

Audit Red Flags

- New or amended reinsurance treaties
- Large unexplained changes in reserve trends or DAC unlocking
- Aggregate k-factor approaching unity
- System conversion
- New complete product
- Acquisition or Divestiture
- Turnover in key staff

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Governance and Reliances

Governance

- Who is ultimately responsible for your reporting output?
- What direct and indirect guidance have you been given on preparing financial reporting output?
- What guidance on preparing financial reporting output have you given to your staff?

Reliances

- Chain of Reliances
- Leading Practices
- Responsibility to Review & Challenge

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Getting the most from the audit

1 Prepare

- Accurate, current, and detailed documentation with sufficient context to understand the appropriateness of your actuarial work
- Routinely ask peers to review your documentation; incorporate insights

2 Discover the ?-behind-the-?

- Understand auditor's preparation
- Explain functional responsibilities and business practices
- Avoid drip-feeding questions; follow-ups after long delays

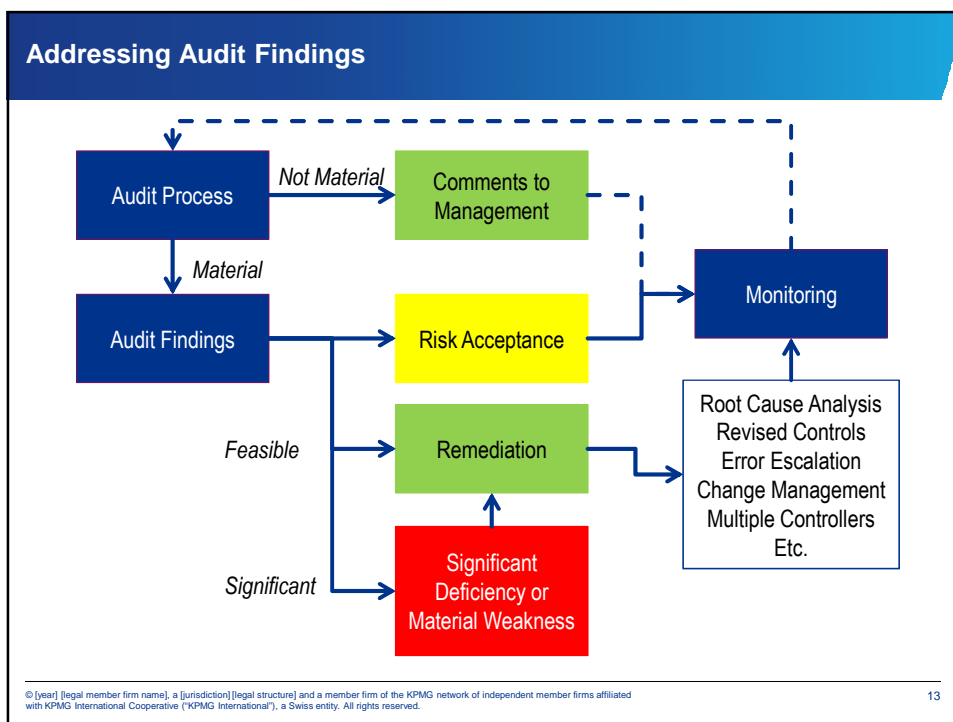
3 Project Management

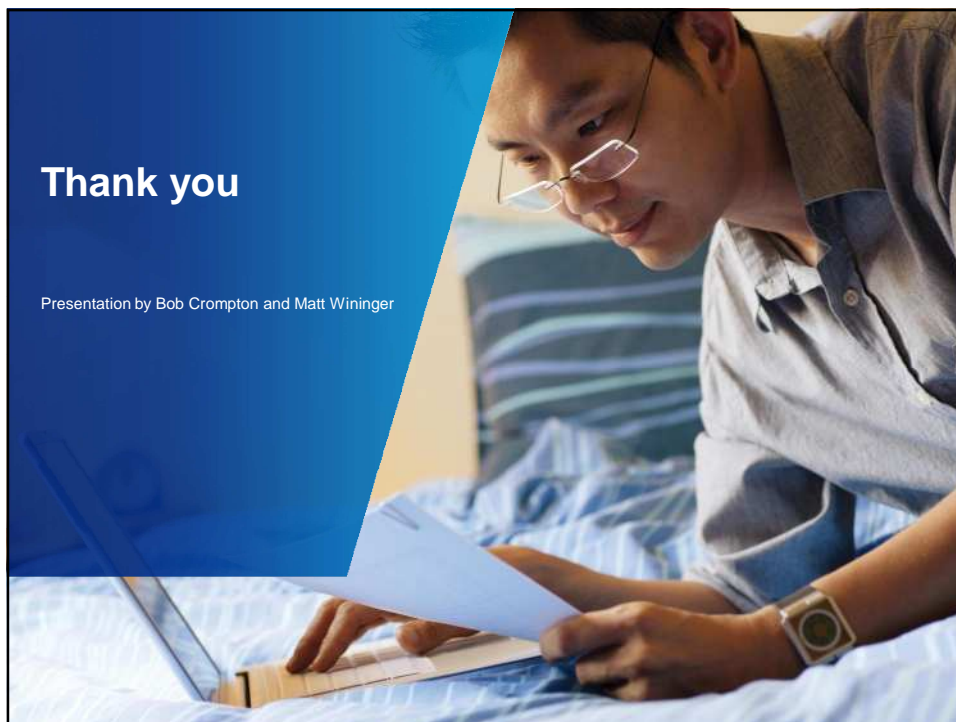
- Establish work times and locations, blackout dates with backup contacts
- Get audit timeframe and project plan
- Audit resource commitment matches risk profile (from whose P.O.V.?)
- Escalation procedure

4 Post-Audit Value

- Understand conclusion reasoning
- All insights may not appear in audit conclusions
- Market intelligence
- Awareness of industry practices and alternatives

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Thank you

Presentation by Bob Crompton and Matt Winger



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