

STATE OF NEW JERSEY
DEPARTMENT OF BANKING AND INSURANCE

IN THE MATTER OF ANNUAL FINANCIAL)
REPORTING AMENDMENTS TO)
N.J.A.C. 11:2-26 AND NEW RULE AT) ORDER
N.J.A.C. 11:2-26.15)

This matter having been opened by the Commissioner of the Department of Banking and Insurance (“the Commissioner”) pursuant to N.J.S.A. 17:1-8.1, 17:1-15e, 17:23-1, 17:23-2, 17:23-20 to -26, 17B:21-1 and 17B:21-2, and all powers expressed or implied therein; and

IT APPEARING that in 2014 the National Association of Insurance Commissioners (“NAIC”) adopted amendments to the NAIC Annual Financial Reporting Model Regulation, which amendments relate to internal audits by insurers; and

IT FURTHER APPEARING that the Department of Banking and Insurance (“the Department”) intends to propose amendments to appear in the February 18, 2020 issue of the New Jersey Register, to 11:2-26 and add a new rule at N.J.A.C. 11:2-26.15 to conform to the current NAIC Annual Financial Reporting Model Regulation; and

IT FURTHER APPEARING that these amendments are required to be adopted for state insurance departments to maintain accreditation under the NAIC Financial Regulation Standards and Accreditation Program; and

IT FURTHER APPEARING that, pending proposal and adoption of these changes, the Department believes that it is reasonable and appropriate to provide guidance to insurers at this time to reflect the current national standard as adopted by the NAIC;

NOW, THEREFORE IT IS on this 23rd day of January 2020 ORDERED that:

1. All entities subject to N.J.A.C. 11:2-26 shall comply with rules as set forth in the Appendix to this Order attached hereto and made a part hereof until superseded by the adoption of any amendments to N.J.A.C. 11:2-26;

2. Provisions of N.J.A.C. 11:2-26 not set forth in the Appendix to this Order shall remain unchanged; and

3. Failure to comply with the terms of this Order shall result in the imposition of penalties as authorized by law.



Marlene Caride
Commissioner

JD Order NAIC Financial Auditing/Orders

Appendix

SUBCHAPTER 26. ANNUAL FINANCIAL REPORTING

11:2-26.2 Scope

This subchapter shall apply to all insurers transacting business in the State of New Jersey except as provided at N.J.A.C. 11:2-26.18.

11:2-26.3 Definitions

The following words and terms, when used in this subchapter, shall have the following meanings, unless the context clearly indicates otherwise.

...

“Audit committee” means a committee (or equivalent body) established by the board of directors of an entity for the purpose of overseeing the accounting and financial reporting processes of an insurer or group of insurers, the internal audit function of an insurer or group of insurers, if applicable, and external audits of financial statements of the insurer or group of insurers. The audit committee of any entity that controls a group of insurers may be deemed to be the audit committee for one or more of these controlled insurers solely for the purposes of this subchapter at the election of the controlling person if it meets the requirements of N.J.S.A. 17:27A-4d(5).

...

“Internal audit function” means a person or persons that provide independent, objective and reasonable assurance designed to add value and improve an organization’s operations and accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

...

11:2-26.4 Filing of annual audited financial reports; extensions for filing of annual audited financial reports and audit committee appointment

(a) All insurers (unless exempted pursuant to N.J.A.C. 11:2-26.18) 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 upon 90 days advance written notice to the insurer.

Existing (b) – (d) are not changed.

11:2-26.9 Scope of audit and report

Financial statements furnished pursuant to N.J.A.C. 11:2-26.5 shall be examined by the independent certified public accountant. The audit of the insurer's financial statements shall be conducted in accordance with generally accepted auditing standards. In accordance with Section 319 of the Professional Standards of the AICPA, Consideration of Internal Control in a Financial Statement Audit, the independent certified public accountant should obtain an understanding of internal control sufficient to plan the audit. To the extent required by AU 319, for those insurers required to file a management's report of internal control over financial reporting pursuant to N.J.A.C. 11:2-26.17, the independent certified public accountant should consider (as that term is defined in Statement on Auditing Standards (SAS) No. 102, Defining Professional Requirements in Statements on Auditing Standards or its replacement) the most recently available report in planning and performing the audit of the statutory financial statements. Consideration shall be given to the 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.

11:2-26.14 Requirements for audit committees

Existing (a) - (b) are not changed.

(c) The audit committee of an insurer or group of insurers shall be responsible for overseeing the insurer's internal audit function and granting the person or persons performing the function suitable authority and resources to fulfill their responsibilities if required by 11:2-26.15.

(d) Each member of the audit committee shall be a member of the board of directors of the insurer or a member of the board of directors of an entity elected pursuant to (g) below and the definition of "audit committee" as set forth in N.J.A.C. 11:2-26.3.

Existing (d) through (g) are recodified as (e) through (h) with no change in text.

(i) If an insurer is a member of an insurance holding company system, the reports required by (h) above may be provided to the audit committee on an aggregate basis for insurers in the holding company system, provided that any substantial differences among insurers in the system are identified to the audit committee.

(j) The proportion of independent directors, committee members or audit committee members shall meet or exceed the following criteria:

Existing (j)1. - 2. are not changed.

3. The provisions of (j)1 and 2 above shall not apply to a domestic insurer if the person controlling the insurer is an entity having a board of directors and committees thereof that substantially meet the requirements of those paragraphs.

11:2-26.15 Internal audit function requirements

(a) An insurer is exempt from the requirements of this section if:

1. The insurer has annual direct written and unaffiliated assumed premium, including international direct and assumed premium but excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, less than \$500,000,000; and

2. If the insurer is a member of a group of insurers, the group has annual direct written and unaffiliated assumed premium including international direct and assumed premium, but excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, less than \$1,000,000,000.

(b) Notwithstanding (a) above, an insurer or group of insurers exempt from the requirements of this section may determine, but is not required, to conduct a review of the insurer business type, sources of capital, and other risk factors to determine whether an internal audit function is warranted. The potential benefits of an internal audit function should be assessed and compared against the estimated costs.

(c) The insurer or group of insurers shall establish an internal audit function providing independent, objective and reasonable assurance to the audit committee and insurer management regarding the insurer's governance, risk management and internal controls. This assurance shall be provided by performing general and specific audits, reviews and tests and by employing other techniques deemed necessary to protect assets, evaluate control effectiveness and efficiency, and evaluate compliance with policies and regulations.

(d) In order to ensure that internal auditors remain objective, the internal audit function shall be organizationally independent. Specifically, the internal audit function shall not defer ultimate judgment on audit matters to others, and shall appoint an individual to head the Internal

audit function who will have direct and unrestricted access to the board of directors. Organizational independence shall not preclude dual-reporting relationships.

(e) The head of the internal audit function shall report to the audit committee regularly, but no less than annually, on the periodic audit plan, factors that may adversely impact the internal audit function's independence or effectiveness, material findings from completed audits and the appropriateness of corrective actions implemented by management as a result of audit findings.

(f) If an insurer is a member of an insurance holding company system or included in a group of insurers, the insurer may satisfy the internal audit function requirements set forth in this section at the ultimate controlling parent level, an intermediate holding company level or the individual legal entity level.

Existing 11:2-26.15 and 11:2-26.16 are recodified as 11:2-26.16 and 11:2-26.17 with no change in text.

11:2-26.18 Exemptions and effective dates

Existing (a)-(g) are not changed.

(h) The requirements for management's report of internal control over financial reporting set forth at N.J.A.C. 11:2-26.17 are effective beginning with the reporting period ending December 31, 2010 and each year thereafter. An insurer or group of insurers that is not required to file a report because the total written premium is below the threshold and subsequently becomes subject to the reporting requirements shall have two years following the year the threshold is exceeded (but not earlier than December 31, 2010) to file a report. Likewise, an insurer acquired in a business combination shall have two calendar years following the date of acquisition or combination to comply with the reporting requirements.

Existing (i) is not changed.

(j) The requirements for an internal audit function set forth in N.J.A.C. 11:2-26.15 are effective January 1, 2020. If an insurer or group of insurers that is exempt from the N.J.A.C 11:2-26.15 requirements no longer qualifies for that exemption, it shall have one year after the year the threshold is exceeded to comply with the requirements of that section.

Existing (k) is not changed.

Existing 11:2-26.18 through 11:2-26.21 are recodified as 11:2-26.19 through 11:2-26.22 with no change in text.