

Directives

of the Federal Office of Private Insurance FOPI

1st January 2007

1/2007 – on the Internal Audit Office¹

Legal basis: Article 4 para. 2 (b) ISA, Article 5 para. 2 ISA
Article 14 para. 1(a) ISA, art. 67 and 75 ISA
Article 27 para. 1 sentence 2 and para. 2 und 3 ISA
Article 29 para. 4 ISA
Article 68 and 76 ISA
Article 191 para. 1 and 2 SO
Article 204 SO

Decision of: 12 December 2006

Enter into force: on 1 January 2007

¹ “Internal Audit office” and “inspectorate” (article 27 para. 1 ISA) and “internal auditing department” and “internal auditing office” are synonyms. The term „internal audit office“ is used in this Directive.



1 Background

Article 27 ISA requires insurance undertakings to appoint an internal audit office that is independent of the general management. In justified individual cases, the supervisory authority may exempt an insurance undertaking from the requirement to appoint an internal audit office. At least once a year, the internal audit office compiles a report on its activities and submits it to the external audit office.

The provision on the internal control system, which is also contained in article 27 ISA, is elaborated in more detail in "Directive No. 15/2006 on Corporate Governance, Risk Management, and the Internal Control System".

The obligation to establish an internal audit office also applies to insurance groups and conglomerates. In this regard, FOPI relies on the powers contained in articles 68 and 76 ISA to issue requirements for monitoring group-internal occurrences and group-wide risk concentration.

When designing the internal audit office, the complexity and size of the insurance company, group, or conglomerate in question must be taken into account, as well as the principle of proportionality.

2 Purpose

This Directive serves to make the supervisory provisions governing the internal audit office more concrete. It is intended to ensure a principle-based minimum standard for the internal audit office.

3 Scope

These provisions apply to all insurance undertakings, groups, and conglomerates that are subject to Swiss insurance supervision. For health insurance schemes offering services under the Insurance Contract Act, FOPI Circular 11/2006 of 1 November 2006 applies. The following provisions also apply to branches in Switzerland of insurance undertakings domiciled abroad.

4 Definition of terms

The internal audit office is a control instrument of the board of directors. It performs objective, independent, and risk-oriented audits of the processes and structures of an insurance undertaking, group, or conglomerate. It supports the organization in achieving its goals by analyzing and reporting on the effectiveness of risk management, the internal control system, the management and monitoring processes, using a systematic and goal-oriented approach.

It acts on behalf of the board of directors or the audit committee and reports to these bodies.

5 Provisions on the internal audit office

As a standard for designing the internal audit office, the following provisions apply, supplemented by the "Guidelines on Internal Auditing" of the SIIA².

5.1 Organization

The head of the internal audit office is appointed by the board of directors. The internal audit office reports directly to the board of directors and fulfils the inspection and audit responsibilities assigned to it.

In order to guarantee cooperation between the board of directors and the internal audit office in insurance undertakings, groups, and conglomerates, it can be useful to form an audit committee consisting of members of the board of directors that regularly meets with the management of the internal audit office.

If an audit committee exists, the FOPI recommends that the audit committee submit a report on the activities and findings of the internal audit office to the board of directors at least once a year.

The FOPI recommends that that the board of directors or the audit committee discuss the reports of the internal audit office. Processes should be established that ensure that the recommendations made in the report are considered and, where necessary, measures are taken within a useful timeframe.

The FOPI recommends that the necessary foundations of the internal audit office (significance and purpose, area of work and powers, organization, scope of responsibilities, terms of reference, reporting, etc.) be specified in an audit charter and approved by the board of directors.

The internal audit office is organizationally independent of the operational business activity. Its processes are independent of daily business transactions. It has the unlimited right of access and audit within the insurance undertaking. All information must be granted to it that is necessary to fulfil its audit responsibilities.

Performing the function of internal audit office is incompatible with the function of responsible actuary.

5.2 Personnel requirements and professional standards

The FOPI recommends that the internal audit office be allocated sufficient staff with sufficient expertise. The audits must be performed with the requisite professional diligence. The professional and managerial qualifications should fulfil the following principles:

² SIIA = Swiss Institute of Internal Auditing

- As a whole, the members of the internal audit office must have thorough knowledge especially of the insurance business, insurance auditing, corporate governance, risk management, and internal control systems. The head of the internal audit office must ensure that proper business conduct and the appropriateness of the internal organization (including IT), risk management, and the internal control system can be assessed by qualified auditors with sufficient expertise.
- In particular, the internal auditors must have comprehensive knowledge of audit principles, procedures, and techniques as well as accounting standards and procedures in the area of insurance.
- They understand the principles and concepts of corporate governance, quantitative methods, and computer-aided information systems and their risks.
- They have a basic understanding of the different areas of business economics and national economics as well as trade and tax law.
- Internal auditors expand their knowledge, their skills, and their other qualifications through systematic training.

5.3 Reporting

The internal audit office reports in writing and in a timely and appropriate manner on all the important findings of an audit to the board of directors or the audit committee. Serious deficiencies must be notified to the board of directors (or the audit committee) immediately.

Processes must be established that ensure rapid notification and reaction of the board of directors or audit committee and the executive management in the event that significant problems are discovered.

At least once a year, the internal audit office must compile a complete report of its audit activities and submit it to the board of directors (or the audit committee). This report must then be forwarded to the external audit office. Conversely, the external audit office must make its audit reports available to the internal audit office. On request, the internal audit office must make individual reports on specific topics available to the external audit office (article 29, paragraph 4 ISA).

5.4 Quality assurance

The FOPI recommends that the internal audit office periodically, but at least every 5 years, have a quality review of its work conducted by an independent, qualified expert body. This may be an external audit office authorized for insurance audits, the internal audit office of a different insurance undertaking, or a body designated by the SIIA.

5.5 Outsourcing of the company's internal audit office

Subject to approval by FOPI, the responsibilities of the internal audit office or parts thereof may be outsourced:

- a. to the internal audit office of the top-most group undertaking, provided that the supervised insurance undertaking is included in the group-wide control and guidance processes;
- b. to an external audit office recognized by FOPI that is independent of the external audit office already mandated by the insurance undertaking in accordance with article 28 ISA;
- c. to an external service provider that is independent of the external audit office already mandated by the insurance undertaking in accordance with article 28 ISA.

5.6 Exemption from the obligation to establish an internal audit office

In justified cases, insurance undertakings may be exempted from the requirement to establish an internal audit office. FOPI may approve an exemption if the insurance undertaking does not have a complex risk structure, for instance if there are no significant operational risks, market and credit risks (including group-internal linkages), or insurance risks.

6 Entry into force and transitional provisions

The insurance undertakings currently supervised by FOPI must meet the requirements set out in this Directive by 1 January 2008 at the latest.

Requests by existing insurance undertakings to outsource in accordance with point 6.5 of the Directive must be submitted by 1 January 2008 (article 216, paragraph 9 SO).

Requests by existing insurance undertakings for exemption from the establishment of an internal audit office must be submitted to FOPI by 31 March 2007.

In the event of changes to the organizational structure or to other conditions, subsequent requests may be submitted at any time.

Federal Office of Private Insurance

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