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Performing agreed-upon procedures engagements that address internal control over derivative transactions by the New York State insurance law; Statement of position 01-3;

American Institute of Certified Public Accountants. Reporting on Internal Control Over Derivative Transactions at Insurance Entities Task Force

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**STATEMENT OF
POSITION 01-3**

AICPA

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

June 15, 2001

**Performing Agreed-Upon
Procedures Engagements
That Address Internal
Control Over Derivative
Transactions as Required
by the New York State
Insurance Law**

*Issued by the
Auditing Standards Board*

NOTE

This Statement of Position represents the recommendations of the AICPA's Reporting on Internal Control Over Derivative Transactions at Insurance Entities Task Force regarding the application of Statements on Standards for Attestation Engagements to agreed-upon procedures engagements performed to comply with the requirements of Section 1410 (b)(5) of the New York State Insurance Law, as amended (the Law), which addresses the assessment of internal control over derivative transactions as defined in Section 1401(a) of the Law, and Section 178.6(b) of Regulation No. 163. The Auditing Standards Board has found the recommendations in this Statement of Position to be consistent with existing standards covered by Rule 202 of the AICPA Code of Professional Conduct. AICPA members should be aware that they may have to justify departures from the recommendations in this Statement of Position if the quality of their work is questioned.

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PERFORMING AGREED-UPON PROCEDURES ENGAGEMENTS THAT ADDRESS INTERNAL CONTROL OVER DERIVATIVE TRANSACTIONS AS REQUIRED BY THE NEW YORK STATE INSURANCE LAW

Introduction and Background

1. The New York State Insurance Department (the Department) has issued regulations to implement the New York Derivative Law (the Law) which amends Article 14 of the State of New York Insurance Law, effective July 1, 1999. The Law establishes certain requirements for domestic life insurers, domestic property and casualty insurers, domestic reciprocal insurers, domestic mortgage guaranty insurers, domestic cooperative property and casualty insurance corporations, and domestic financial guaranty insurers. Foreign insurers engaging in derivative transactions and derivative instruments are subject to and required to comply with all of the provisions of the Law. However, a foreign insurer may enter into other derivative transactions provided the insurer meets certain conditions of its domestic state law. In this document, an insurer covered by the Law is referred to as an *insurance company*.
2. The requirements of the Law include the following:
 - Approval by the board of directors, or a similar body, of derivative transactions
 - Submission of a derivative use plan (the DUP) to the Department
 - Assessment by an independent certified public accountant (CPA) of the insurance company's internal control over derivative transactions
3. In addition to the Law, the Department also has established Regulation No. 163, "Derivative Transactions" (11 NYCRR 178) (the Regulation), which provides guidance in imple-

menting the Law. Section 178.6(b) of Regulation No. 163 states the following.

As set forth in section 1410 (b)(5) of the Insurance Law, an insurer engaging in derivative transactions shall be required to include, as part of the evaluation of accounting procedures and internal controls required to be filed pursuant to section 307 of the Insurance Law, a statement describing the assessment by the independent certified public accountant of the internal controls relative to derivative transactions. The purpose of this part of the evaluation is to assess the adequacy of the internal controls relative to the derivative transactions. Such an assessment shall be made whether or not the derivative transactions are material in relation to the insurer's financial statements and shall report all material deficiencies in internal control relative to derivative transactions, whether or not such deficiencies would lead to an otherwise "reportable condition," as that term is used in auditing standards adhered to by certified public accountants. The statement describing the assessment need not be set forth in a separate report.

4. The Department has proposed that the Regulation be amended to provide that an assessment in the form of an agreed-upon procedures engagement or other attestation engagement, as those terms are used in standards adhered to by CPAs, may be used to meet the requirement for an assessment of internal control over derivative transactions. This proposed amendment to the Regulation has not been promulgated at the date of this Statement of Position (SOP). However, in a letter dated April 27, 2001, the Department stated the following:

This letter confirms that in determining compliance with Section 1410(b)(5) of the Insurance Law, the Department acknowledges that an agreed-upon procedures engagement, including an engagement performed using the procedures in the proposed SOP ("Performing Agreed-Upon Procedures Engagements that Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law"), can be used to satisfy the statutory requirement.

5. The DUP was due to be filed by applicable insurance companies by January 1, 2000. The first independent CPA's report is due on June 1, 2001. The Law expires on June 30, 2003; however, the State of New York may extend the expiration date.
6. As previously stated, the letter from the Department indicates that an agreed-upon procedures engagement or other attestation engagement may be used to satisfy the requirements of the Law. However, this SOP only describes an agreed-upon procedures engagement. It does not address any other attestation engagements that might be performed, such as an examination-level attestation engagement. For guidance on performing such other attestation engagements, see "Attest Engagements," in Statement on Standards for Attestation Engagements (SSAE) No. 10, *Attestation Standards: Revision and Codification* (AICPA, *Professional Standards*, vol. 1, AT sec 101).

Applicability

7. This SOP was developed to provide practitioners with guidance on performing agreed-upon procedures engagements that address an insurance company's internal control over derivative transactions to meet the requirements of the Law. Practitioners should note that the engagement described in this SOP is designed only to satisfy the requirements of the Law. The procedures, as set forth in this SOP, are not necessarily appropriate for use in any other engagement.
8. Although the Department has indicated that an agreed-upon procedures engagement pursuant to this SOP can be used to satisfy the requirements for an assessment of internal control over derivative transactions, the Department has not agreed to the sufficiency of the procedures included in this SOP for their purposes.

The Law

Definition of a Derivative

9. Article 14 of the Law defines a derivative instrument as including caps, collars, floors, forwards, futures, options, swaps, swaptions, and warrants.
10. The following definitions are included in the Law and are applicable when performing the agreed-upon procedures engagement described in this SOP.

Cap—An agreement obligating the seller to make payments to the buyer with each payment based on the amount by which a reference price or level or the performance or value of one or more underlying interests exceeds a predetermined number, sometimes called the strike rate or strike price.

Collar—An agreement to receive payments as the buyer of an option, cap, or floor and to make payments as the seller of a different option, cap, or floor.

Floor—An agreement obligating the seller to make payments to the buyer in which each payment is based on the amount by which a predetermined number, sometimes called the floor rate or price, exceeds a reference price, level, performance, or value of one or more underlying interests.

Forward—An agreement (other than a future) to make or take delivery in the future of one or more underlying interests, or effect a cash settlement, based on the actual or expected price, level, performance, or value of such underlying interests, but shall not mean or include spot transactions effected within customary settlement periods, when-issued purchases, or other similar cash market transactions.

Future—An agreement traded on a futures exchange, to make or take delivery of, or effect a cash settlement based on the actual or expected price, level, performance, or value of one or more underlying interests.

Option—An agreement giving the buyer the right to buy or receive (a *call option*), sell or deliver (a *put option*), enter into, extend or terminate, or effect a cash settlement based on the actual or expected price, spread, level, performance, or value of one or more underlying interests.

Swap—An agreement to exchange or to net payments at one or more times based on the actual or expected price, yield, level, performance, or value of one or more underlying interests.

Swaption—An option to purchase or sell a swap at a given price and time or at a series of prices and times. A swaption does not mean a swap with an embedded option.

Warrant—An instrument that gives the holder the right to purchase or sell the underlying interest at a given price and time or at a series of prices and times outlined in the warrant agreement.

11. Article 14 of the Law permits an insurance company to enter into *replication transactions* provided that certain conditions set forth in the Law are met. A replication transaction is defined in the Law as follows.

A derivative transaction or combination of derivative transactions effected either separately or in conjunction with cash market investments included in the insurer's investment portfolio in order to replicate the investment characteristic of another authorized transaction, investment or instrument and/or operate as a substitute for cash market transactions. A derivative transaction entered into by the insurer as a hedging transaction or income generation transaction authorized pursuant to this section [of the Law] shall not be considered a replication transaction.

Derivative Use Plan

12. An insurance company entering into derivative transactions must file a DUP with the Department. The DUP generally should include the following items:¹
- A certified copy of the authorization by the insurer's board of directors, or other similar body, to file the DUP, which should include authorization of derivative transactions and an assurance that individuals responsible for derivative transactions, processes, and controls have the necessary experience and knowledge
 - A section on management oversight standards including a discussion of the following:
 - Limits on identified risks
 - Controls over the nature and amount of identified risks
 - Processes for identifying such risks
 - Processes for documenting, monitoring, and reporting risk exposure
 - Internal audit and review processes that ensure integrity of the overall risk management process
 - Quarterly reporting to the board of directors
 - The establishment of risk tolerance levels
 - Management's measurement and monitoring against those levels
 - A section on internal control and reporting including a discussion of the following:
 - The existence of controls over the valuation and effectiveness of derivative instruments
 - Credit risk management
 - The adequacy of professional personnel
 - Technical expertise and systems
 - Management reporting

1. Reference should be made to the Law and the Regulation for specific details and exact requirements.

- The review and legal enforceability of derivative contracts between parties
- A section on documentation and reporting requirements which shall for each derivative transaction document the following:
 - The purpose of the transaction
 - The assets or liabilities to which the transaction relates
 - The specific derivative instrument used
 - For over-the-counter (OTC) transactions, the name of the counterparty and counterparty exposure amount
 - For exchange traded transactions, the name of the exchange and the name of the firm handling the trade
- Written guidelines to be followed in engaging in derivative transactions. The guidelines should include or address the following:
 - The type, maturity, and diversification of derivative instruments
 - The limitation on counterparty exposures, including limitations based on credit ratings
 - The limitations on the use of derivatives
 - Asset and liability management practices with respect to derivative transactions
 - The liquidity needs and the insurance company's capital and surplus as it relates to the DUP
 - The policy objectives of management specific enough to outline permissible derivative strategies
 - The relationship of the strategies to the insurer's operations
 - How the strategies relate to the insurer's risk
 - A requirement that management establish and execute management oversight standards as required by the Law

- A requirement that management establish and execute internal control and reporting standards as required by the Law
- A requirement that management establish and execute documentation and reporting standards as required by the Law
- Guidelines for the insurer’s determination of acceptable levels of basis risk, credit risk, foreign currency risk, interest rate risk, market risk, operational risk, and option risk
- A requirement that the board of directors and senior management comply with risk oversight functions and adhere to laws, rules, regulations, prescribed practices, or ethical standards

Related Professional Standards

AT Section 201, “Agreed-Upon Procedures Engagements,” Statement on Standards for Attestation Engagements No. 10

13. Agreed-upon procedures engagements performed to meet the requirements of the Law are to be performed in accordance with AT Section 201, “Agreed-Upon Procedures Engagements,” in SSAE No. 10. As described in AT Section 201.03, an agreed-upon procedures engagement is one in which a practitioner is engaged by a client to issue a report of findings based on specific procedures performed on the subject matter. Not all of the provisions of AT Section 201 are discussed herein. Rather, this SOP includes guidance to assist practitioners in the application of selected aspects of AT Section 201.
14. AT section 201.06 states, in part, that the practitioner may perform an agreed-upon procedures engagement provided that, “...(c) the practitioner and the specified parties agree upon the procedures performed or to be performed by the practitioner; and (d) the specified parties take responsibility for the sufficiency of the agreed-upon procedures for their purposes.”

15. As previously stated, the letter from the Department states that an agreed-upon procedures engagement may be used to meet the requirement for an independent CPA's assessment of internal control over derivative transactions, and acknowledges the use of this SOP in such engagements. Accordingly, practitioners should not eliminate any of the procedures presented in appendix B, "Agreed-Upon Procedures for Testing Internal Control Over Derivative Transactions," of this SOP or reduce the extent of the tests. The Department or the insurance company may request that additional procedures be performed and the practitioner may agree to perform such procedures. In those circumstances, it would be expected that the additional procedures would be performed in the context of a separate agreed-upon procedures engagement.
16. As previously noted, the Department has not agreed to the sufficiency of the procedures included in this SOP for their purposes. *Therefore, the Department should not be named as a specified party to the agreed-upon procedures report, and the use of a practitioner's agreed-upon procedures report, issued in accordance with this SOP, should be restricted to the board of directors and management of the insurance company.* Although the Department is not a specified party, footnote 15 of AT Section 101, *Attest Engagements*, states the following, in part:

... a regulatory agency as part of its oversight responsibility for an entity may require access to restricted-use reports in which they are not named as a specified party.

Statement on Auditing Standards No. 92, Auditing Derivative Instruments, Hedging Activities, and Investments in Securities

17. Statement on Auditing Standards (SAS) No. 92, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (AICPA, *Professional Standards*, vol. 1, AU sec. sec. 332), provides guidance to auditors in planning and performing auditing procedures for financial statement assertions about derivative instruments, hedging activities, and investments in securities in a financial statement audit performed in accordance with generally ac-

cepted auditing standards. A practitioner performing the agreed-upon procedures engagement described in this SOP may find it helpful to consider the guidance in SAS No. 92 and the related audit guide of the same name supporting SAS No. 92. Specifically, the practitioner should consider AU Sections 332.5 and 332.6 of SAS No. 92 which describe the need for special skill or knowledge to plan and perform the auditing procedures presented in SAS No. 92. That same skill and knowledge is needed to perform the procedures described in this SOP.

18. The procedures in this SOP are not designed to meet the requirements of generally accepted auditing standards for an audit of the financial statements of an entity that engages in derivative transactions. In addition, performing the audit procedures described in SAS No. 92 would not meet the requirements of this SOP.
19. In an audit of financial statements, the auditor may determine that he or she will not perform procedures related to derivative transactions because they are not material to the financial statements. There is no requirement to perform the procedures described in this SOP when performing an audit of financial statements. In contrast, the Law requires that an assessment of internal control be performed whether or not the derivative transactions are material to the insurer's financial statements. Accordingly, a decision not to perform procedures related to derivative transactions in an audit of financial statements, because of immateriality, would not alleviate the requirement to perform the agreed-upon procedures engagement described herein.

Procedures to Be Performed

20. The agreed-upon procedures to be performed are directed toward tests of controls over derivative transactions that occurred during the period covered by the practitioner's report. Any projection of the practitioner's findings to the future is subject to the risk that because of change, the controls may no longer be in existence, suitably designed, or operating effectively. Also, the potential effectiveness of controls over derivative transactions is subject to inherent

limitations and, accordingly, errors or fraud may occur and not be detected.

21. The procedures to be performed in the agreed-upon procedures engagement described in this SOP are presented in Appendix B. The procedures have been designed so that the findings resulting from the application of the procedures can be recorded in a tabular format. The findings for each procedure should be reported as *No Exception*, *Exception*, or *N/A* (not applicable). If a procedure is not applicable to a particular insurance company, the procedure should be marked N/A rather than deleted from the report.
22. Section 1 of Appendix B of this SOP is applicable to all insurance companies that enter into derivative transactions. Therefore, the procedures in section 1 are to be performed in all engagements performed in accordance with this SOP. Sections 2 through 10 of Appendix B of this SOP each address a specific type of derivative. The procedures in those sections are to be performed only if the insurance company entered into derivative transactions of the type covered by the section. Sections that address types of derivatives not used by the insurance company should not be attached to the agreed-upon procedures report.
23. If any portion of a procedure results in an exception, the findings for that entire procedure should be recorded as an exception and described in the section “Description of Exceptions If Any,” at the end of each section. The practitioner should provide a brief factual explanation for each exception that will enable the specified parties to understand the nature of the findings resulting in the exception. If management informs the practitioner that the condition giving rise to the exception was corrected by the date of the practitioner’s report, the practitioner’s explanation of the exception may include that information; for example, “Management has advised us that the condition resulting in the exception was corrected on Month X, 20XX. We have performed no procedures with respect to management’s assertion.”
24. A practitioner may perform significant portions of the agreed-upon procedures engagement before the end of the period covered by the report. If, during that time, the prac-

itioner identifies conditions that result in an exception in one or more agreed-upon procedures, he or she should report the exception in the findings section of the agreed-upon procedures report, even if management corrects the condition prior to the end of the period.

25. The Law requires the insurance company to provide the Department with a statement describing the independent CPA's assessment of the insurance company's internal control over derivative transactions. It also requires the insurance company to include a description of any remedial actions taken or proposed to be taken to correct any deficiencies identified by the independent CPA.
26. AT Section 201.40 states the following.

The practitioner need not perform procedures beyond the agreed-upon procedures. However, in connection with the application of agreed-upon procedures, if matters come to the practitioner's attention by other means that significantly contradict the subject matter (or written assertion related thereto) referred to in the practitioner's report, the practitioner should include this matter in his or her report. For example, if during the course of applying agreed-upon procedures regarding an entity's internal control, the practitioner becomes aware of a material weakness by means other than performance of the agreed-upon procedures, the practitioner should include this matter in his or her report.

27. A practitioner has no obligation to perform procedures beyond the agreed-upon procedures included in Appendix B of this SOP. However, if information indicating a weakness in internal control over derivative transactions comes to the practitioner's attention by other means, such information should be included in the practitioner's report. This would apply to conditions or events occurring during the subsequent-events period (subsequent to the period covered by the practitioner's report but prior to the date of the practitioner's report) that either contradict the findings in the report or that would have resulted in the reporting of an exception by the practitioner if that condition or event had existed during the period covered by the report. However, the practitioner has no responsibility to perform any procedure to detect such conditions or events.

Establishing an Understanding With the Client

28. In accordance with AT Section 201.10, the practitioner should establish an understanding with the client regarding the services to be performed. Such an understanding reduces the risk that the client may misinterpret the objectives and limitations of an agreed-upon procedures engagement performed to meet the regulatory requirements of the Law. Such an understanding also reduces the risk that the client will misunderstand its responsibilities and the responsibilities of the practitioner. The practitioner should document the understanding in the working papers, preferably through a written communication with the client (an *engagement letter*). The communication should be addressed to the client. Matters that might be included in such an understanding are the following:
- A statement confirming that an agreed-upon procedures engagement is to be performed to meet the requirements of Section 1410(b)(5) of the Law
 - A statement identifying the procedures to be performed as those set forth in SOP 01-3, *Performing Agreed-Upon Procedures Engagements That Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law*
 - A statement identifying the client as the specified party to the agreed-upon procedures report
 - A statement acknowledging the client's responsibility for the sufficiency of the procedures in the SOP
 - A statement acknowledging that the practitioner makes no representation regarding the sufficiency of the procedures in the SOP
 - A statement describing the responsibilities of the practitioner, including but not limited to the responsibility to perform the agreed-upon procedures and to provide the client with a report, and the circumstances under which the practitioner may decline to issue a report

- A statement indicating that the engagement will be conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants (AICPA)
- A statement indicating that an agreed-upon procedures engagement does not constitute an examination, the objective of which would be the expression of an opinion on the internal control over derivative transactions, and that if an examination were performed, other matters might come to the practitioner's attention
- A statement indicating that the practitioner will not express an opinion or any other form of assurance
- A statement describing the client's responsibility to comply with the Law and the client's responsibility for the design and operation of effective internal control over derivative transactions
- A statement describing the client's responsibility for providing accurate and complete information to the practitioner
- A statement indicating that the practitioner has no responsibility for the completeness or accuracy of the information provided to the practitioner
- A statement restricting the use of the report to the client
- A statement describing any arrangements to involve a specialist

Management Representations

29. Although AT Section 201 does not require a practitioner to obtain a representation letter from management in an agreed-upon procedures engagement, it is recommended that the practitioner obtain such a letter when performing the engagement described in this SOP. The representation letter generally should be signed by the appropriate members of management including the highest ranking officer responsible for internal control over derivative transac-

tions. Management's refusal to furnish written representations that the practitioner has determined to be appropriate for the engagement constitutes a limitation on the performance of the engagement that requires either modification of the report or withdrawal from the engagement.

30. The representations that a practitioner deems appropriate will depend on the specific nature of the engagement; however, the practitioner ordinarily would obtain the following representations from management:
- A statement acknowledging responsibility for establishing and maintaining effective internal control over derivative transactions
 - A statement that there have been no errors or fraud that might indicate a weakness in the internal control over derivative transactions
 - A statement that management has disclosed to the practitioner all significant deficiencies in the design or operation of the internal control over derivative transactions
 - A statement that management has disclosed to the practitioner any communications from regulatory agencies, internal auditors, and other practitioners or consultants relating to the internal control over derivative transactions
 - A statement that management has made available to the practitioner all information they believe is relevant to the internal control over derivative transactions
 - A statement that management has responded fully to all inquiries made by the practitioner during the engagement
 - A statement that no events have occurred subsequent to the date as of which the procedures were applied that would require adjustment to or modification to responses to the agreed-upon procedures
31. An illustrative representation letter is presented in appendix C, "Illustrative Management Representation Letter," of

this SOP. For additional information regarding management's representations in an agreed-upon procedures engagement, see AT Sections 201.37-39.

Restriction on the Performance of Procedures

32. As previously stated, a practitioner should not agree to do either of the following.
 - a. Eliminate any of the procedures presented in appendix B of this SOP, unless a section is not applicable because the insurance company did not enter into derivative transactions addressed by the section.
 - b. Reduce the extent of the tests in an applicable section.
33. If circumstances impose restrictions on the performance of the agreed-upon procedures presented in appendix B of this SOP, the practitioner should describe the restriction(s) in his or her report or withdraw from the engagement.

Dating the Report

34. The date of completion of the agreed-upon procedures should be used as the date of the practitioner's report.

Effective Date

35. This SOP is effective upon issuance and is applicable only to agreed-upon procedures engagements that address internal control over derivative transactions required by the Law.

APPENDIX A

Illustrative Agreed-Upon Procedures Report

The following is an illustrative agreed-upon procedures report based on the guidance in AT Section 201, “Agreed-Upon Procedures Engagements,” in Statement on Standards for Attestation Engagements (SSAE) No. 10, *Attestation Standards: Revision and Recodification* (AIPCA, *Professional Standards*, vol. 2, AT sec. 201).

Independent Accountant’s Report on Applying Agreed-Upon Procedures

To the Management of ABC Insurance Company:

We have performed the applicable procedures enumerated in the American Institute of Certified Public Accountants’ Statement of Position (SOP), 01-3, *Performing Agreed-Upon Procedures Engagements That Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law*, which were agreed to by ABC Insurance Company, solely to assist you in complying with the requirements of Section 1410 (b)(5) of the New York State Insurance Law, as amended (the Law), which addresses the assessment of internal control over derivative transactions as defined in Section 1401(a) of the Law, and Section 178.6(b) of Regulation No. 163 during the year ended December 31, 20XX. Management of ABC Insurance Company is responsible for maintaining effective internal control over derivative transactions. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of ABC Insurance Company. Consequently, we make no representation regarding the sufficiency of the procedures described in the attached Appendix either for the purpose for which this report has been requested or for any other purpose.

The procedures performed and the findings are included in the attached Appendix.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on the internal control over derivative transactions of ABC Insurance Company for the year ended December 31, 20XX. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the management and Board of Directors of ABC Insurance Company and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

APPENDIX B

Agreed-Upon Procedures for Testing Internal Control Over Derivative Transactions

The following table lists the types of derivative transactions permitted by the New York Derivative Law (the Law). We inquired of management of the insurance company as to whether the insurance company used the type of derivative addressed by each section, and marked the column entitled “Is the Section Applicable?” either *Yes* or *No* based on management’s response to the inquiry. For each type of derivative with a *Yes* response, we performed the procedures in the applicable section and attached the section to the report. For each type of derivative with a *No* response, we did not perform procedures nor did we attach the applicable section to the report. We compared the types of derivative reported by the insurance company in its “Schedule of Derivative Transactions” included in the Annual Statement with the types of derivatives listed in the following table and found that the types of derivatives included in the schedule were marked *Yes* in the table.

Attachments to the Report		
Section of the Agreed-Upon Procedures		Is the Section Applicable?
No.	Type of Derivative	Yes or No
1	All Derivative Types	Yes
2	Cap Contracts	
3	Collar Contracts	
4	Floor Contracts	
5	Forward Contracts	
6	Future Contracts	
7	Option Contracts	
8	Swap Contracts	
9	Swaption Contracts	
10	Warrant Contracts	

Section 1—All Derivative Types

Procedures	Findings		
	No Exception	Exception	N/A

The following procedures were performed to test controls applicable to all derivative transactions. The procedures were applied to the internal control over derivative transactions in existence during the year ended December 31, 20XX.

Documentation of Controls, Policies, and Procedures

1. Read the insurance company’s derivative use plan (DUP), amendments thereto, and its documentation of controls, policies, and procedures that describe internal control over derivative transactions and found that the DUP and the documentation of controls, policies, and procedures include a description of controls that address the following:
 - a. Systems or processes for the periodic valuation of derivative transactions including mechanisms for compensating for any lack of independence in valuing derivative positions (Valuation)
 - b. Systems or processes for determining whether a derivative instrument used for hedging or replication has been effective (Effectiveness)
 - c. Credit risk management systems or processes for over-the-counter (OTC) derivative transactions that measure credit risk exposure using the counterparty exposure amount and policies for the establishment of collateral arrangements with counterparties (Credit Risk Management)
 - d. Management assessment of the adequacy and technical expertise of personnel associated with derivative transactions and systems to implement and control investment practices

_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
involving derivatives (Professional Competence)	_____	_____	_____
e. Systems or processes for regular reports to management, segregation of duties, and internal review procedures (Reporting)	_____	_____	_____
f. Procedures for conducting initial and ongoing legal reviews of derivative transactions including assessments of contract enforceability (Legal Reviews)	_____	_____	_____

Nontransaction-Specific Procedures

- | | | | |
|--|-------|-------|-------|
| 2. Read the minutes of meetings of the board of directors and found an indication that the board of directors of the insurance company approved the DUP and any amendments thereto. | _____ | _____ | _____ |
| 3. Inquired of management as to whether the DUP and any amendments thereto were approved by the New York State Insurance Department and was advised that the DUP and any amendments thereto were approved. | _____ | _____ | _____ |
| 4. Read the minutes of meetings of the board of directors and found an indication that the board of directors of the insurance company approved the commitment of financial resources determined by management to be sufficient to accomplish the objectives of the insurance company's DUP. | _____ | _____ | _____ |

This procedure does not provide an assessment of or assurance about the adequacy of the resources determined by management to be sufficient to accomplish the objectives of the DUP.

In performing the following procedures, the practitioner should be aware that management frequently will have designated and

(continued)

Procedures	Findings		
	No Exception	Exception	N/A

will have in place limits, controls, or procedures that are more restrictive than those approved for use in the DUP.

5. For the year ended December 31, 20XX, inquired of management and was advised that —

a. There was monitoring of derivative transactions by a control staff, such as internal audit or other internal review group, that is independent of derivatives trading activities.

b. There were procedures in place for derivative personnel to obtain, prior to exceeding limits prescribed by management, at least oral approval from members of senior management who are independent of derivatives trading activities.

c. There were procedures in place for senior management to address excesses related to management-established limits and divergences from management-approved derivative strategies, and that such management has authority to grant exceptions to derivatives limits.

d. There were procedures in place requiring that management be informed when limits prescribed in the DUP were exceeded and for management to approve corrective action(s) in such circumstances.

e. There were procedures in place for the accurate transmittal of derivatives positions to the risk measurement systems when management had implemented risk management systems.

f. There were procedures in place for the performance of appropriate reconciliations to ensure data integrity

Procedures	Findings		
	No Exception	Exception	N/A
across the full range of derivatives, including any new or existing derivatives that may be monitored apart from the main processing networks.	_____	_____	_____
g. There were procedures in place for risk managers and senior management to define constraints on derivative activities to ensure compliance with the DUP and to justify excesses with respect to specified management limits.	_____	_____	_____
h. There were procedures in place for senior management, an independent group, or an individual that management designated to perform at least an annual assessment of the identified controls and financial results of the derivative activities to determine that controls were effectively implemented and that the insurance company's business objectives and strategies were achieved.	_____	_____	_____
i. There were procedures in place for a review of limits in the context of changes in strategy, risk tolerance of the insurance company, and market conditions.	_____	_____	_____
Reporting to the Board of Directors or Committee Thereof			
The Law contains provisions regarding management oversight of derivative and replication transactions.			
6. Read the minutes of the board of directors meetings or committees thereof and found an indication that the board of directors or committee thereof received, at least quarterly, a report regarding derivative and replication transactions.	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
7. Read one quarterly report referred to in procedure 6 and found that the report contained—			
a. A list, or appropriate summaries, of the following:			
i. Derivative transactions during the period	_____	_____	_____
ii. Derivative transactions outstanding at the end of the period	_____	_____	_____
iii. Unrealized gains or losses on open derivative positions	_____	_____	_____
iv. Derivative transactions closed during the period	_____	_____	_____
b. A summary of the performance of the derivatives in comparison to the objective of the derivative transactions	_____	_____	_____
c. An evaluation of the risks and benefits of the derivative transactions	_____	_____	_____
d. A summary of the amount, type, and performance of replication transactions	_____	_____	_____
8. If the report referred to in the preceding procedure was received, reviewed, and approved by a committee of the board of directors, read the minutes of the board of directors meeting and found an indication that a report of such committee was reviewed at the next board of directors meeting.	_____	_____	_____
9. Read the board of directors minutes and found an indication that the board of directors received a report during the year describing the level of knowledge and experience of individuals conducting, monitoring, controlling, and auditing derivative and replication transactions.	_____	_____	_____

Findings

Procedures	No Exception	Exception	N/A
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Derivative and Replication Limitations

The Law contains limits on hedging and replication transactions. An insurance company may enter into hedging or replication transactions if, as a result of and after giving effect to the transaction, the derivative investments and replication investments do not exceed certain specified percentages of admitted assets. The following procedures were performed using one analysis per quarter prepared by the insurance company to monitor compliance with the limitations.

10. Obtained and read the insurance company's analysis used to test limitations on investments in derivatives and replication transactions and found that the amounts shown in the analysis indicated that—

a. The aggregate statement value of options, swaptions, caps, floors, and warrants purchased was not in excess of seven and one-half percent of the insurance company's admitted assets, per the last annual statement.

b. The aggregate statement value of options, swaptions, caps, and floors written was not in excess of three percent of admitted assets.

c. The aggregate potential exposure of collars, swaps, forwards, and futures entered into and options, swaptions, caps, and floors written was not in excess of six and one-half percent of admitted assets.

d. The aggregate statement value of all assets being replicated did not exceed ten percent of the insurance company's admitted assets.

e. The extent of derivative transactions did not exceed the insurance com-

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
pany's internal limitations or that any excess had been specifically authorized by management.	_____	_____	_____
11. Inquired of the preparer of the analysis read in procedure 10 and was advised that the analysis excluded transactions entered into to hedge the currency risk of investments denominated in a currency other than United States dollars.	_____	_____	_____
12. Obtained and read the insurance company's analysis used to test limitations on counterparty exposure, as defined in section 178.3 (e) of the Regulation, and found that the report indicated that—			
a. The counterparty exposure under one or more derivative transactions for any single counterparty, other than a "qualified counterparty," was not in excess of one percent of the insurance company's admitted assets.	_____	_____	_____
b. The counterparty exposure under one or more derivative transactions for all counterparties, other than qualified counterparties, was not in excess of three percent of the insurance company's admitted assets.	_____	_____	_____
13. If the insurance company required collateral arrangements with the counterparties, obtained and read the insurance company's analysis used to monitor the adequacy of the collateral held in accordance with the terms of the arrangement and found that the amount of the collateral held as shown on the analysis was equal to or in excess of the amount to be held.	_____	_____	_____

Description of Exceptions if Any

Procedure Number

Description of Exception

Section 2—Cap Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected cap contracts to test internal control over cap transactions. Selected five percent of each type of cap transaction (that is, purchases [premium disbursements], sales [premium receipts], and closeouts [closings and settlements of the position]), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all the transactions of that type.</p>			
Reporting			
1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to enter into cap contracts.	_____	_____	_____
2. For each cap selected for testing, read management's documentation describing the intended use of the cap and performed the following procedures, as applicable.	_____	_____	_____
For caps used as a hedge—			
3. Determined that the documentation described the following:			
a. The risk hedged	_____	_____	_____
b. How the hedge was consistent with the overall risk management strategy	_____	_____	_____
c. How the cap was expected to be effective in offsetting the exposure	_____	_____	_____
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the cap as a hedge	_____	_____	_____
b. The terms of the cap, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the cap hedged	_____	_____	_____
d. Evidence that the cap continued to be an effective hedge	_____	_____	_____
e. Evidence that the cap was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures, for entering into hedge transactions; for example, the notional amount or underlying	_____	_____	_____
If the cap was an exact offset to an outstanding cap—			
5. Read documentation indicating that the cap offset an outstanding cap previously purchased or sold by the insurance company and that the cap was an exact offset of the market risk of the cap being offset.	_____	_____	_____
For caps used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the cap was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
d. The approach for assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the cap, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected caps including those that are a part of a replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof, who had the authority to authorize cap transactions. Compared the name of the individual who authorized the cap transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount or strike price exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>non-qualified</i> counterparties, approved by the board of directors or a committee			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
thereof. Compared the name of the counterparty involved in the cap transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or a committee thereof to trade cap contracts. Compared the name of the individual who executed the purchase, sale, or closeout of the cap with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve payments relating to caps. Compared the name of the individual who approved any payment relating to the cap with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the cap with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the cap with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the purchase, sale, or closeout of the cap and found that the purchase,			

Procedures	Findings		
	No Exception	Exception	N/A
sale, or closeout was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade caps and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the cap contract, as stated on the deal ticket and confirmation, with the terms of the cap contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period (for example, monthly or quarterly), indicating that the insurance company determined that its accounting records for caps tested in procedure 18, agreed with or reconciled to the related control account; for example, the subsidiary ledger to the general ledger.	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the cap agreement. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
21. Compared the terms of the cap agreement recorded in the insurance company's accounting records with the terms shown in the executed copy of the cap agreement and found them to be in agreement.	_____	_____	_____
22. Obtained documentation for one reporting period (for example, monthly or quarterly), indicating that the insurance company physically inventoried the cap agreements.	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
23. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the cap agreement with the names of individuals authorized to execute purchases, sales, or closeouts of cap contracts and found that the name of the individual was not on the list.	_____	_____	_____
24. Compared information regarding the cap, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
25. If the cap should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the cap, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
26. Read accounting documentation indicating that the insurance company monitored periodic cash settlements related to the cap tested, meaning, the insurance company had controls in place to determine that periodic cash settlements, if any, were received.	_____	_____	_____
Effectiveness of Caps Used As Hedges and in Replication Transactions			
27. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the cap as a hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
28. If the cap was no longer effective as a hedge or replication, compared the ac-	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
tion taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.			
Legal Review			
29. Read documentation indicating that the legal department reviewed the cap agreement to assess contract compliance with the DUP and enforceability.			
30. Read documentation indicating that the legal department updated its assessment of agreement enforceability at least annually.			
Valuation			
31. Obtained the insurance company's policies and procedures for valuing caps and found that the insurance company determined the fair value of the cap in accordance with the policy described in the insurance company's procedures for the valuation of caps.			
32. Read documentation supporting the fair value of the cap and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized person.			

Description of Exceptions if Any

Procedure Number	Description of Exception
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(continued)

Section 3—Collar Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected collar contracts to test internal control over collar transactions. Selected five percent of each type of collar transaction (that is, executions [entering into a collar transaction in which the net position at inception may result in either no cash outlay, cash received, or cash disbursed] and close-outs [closings and settlements of the position]), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all the transactions of that type.</p>			
<p>Reporting</p> <ol style="list-style-type: none"> 1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to enter into collar contracts. 	_____	_____	_____
<ol style="list-style-type: none"> 2. For each collar selected for testing, read management's documentation describing the intended use of the collar and performed the following procedures, as applicable. <p>For collars used as a hedge—</p>	_____	_____	_____
<ol style="list-style-type: none"> 3. Determined that the documentation described the following: <ol style="list-style-type: none"> a. The risk hedged 	_____	_____	_____
<ol style="list-style-type: none"> b. How the hedge was consistent with the overall risk management strategy 	_____	_____	_____
<ol style="list-style-type: none"> c. How the collar was expected to be effective in offsetting the exposure 	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____
4. Determined that the following items were documented:			
a. The purpose(s) of the collar as a hedge	_____	_____	_____
b. The terms of the collar, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the collar hedged	_____	_____	_____
d. Evidence that the collar continued to be an effective hedge	_____	_____	_____
e. Evidence that the contract was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures, for entering into hedge transactions; for example, the notional amount or underlying	_____	_____	_____
If the collar was an exact offset of an outstanding collar—			
5. Read documentation indicating that the collar offset an outstanding collar previously purchased or sold by the insurance company and that the collar was an exact offset of the market risk of the collar being offset.	_____	_____	_____
For collars used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
c. How the collar was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the collar, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected collars including those that are a part of a replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof, who had the authority to authorize collar transactions. Compared the name of the individual who authorized the collar transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount or strike price exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and			

Procedures	Findings		
	No Exception	Exception	N/A
found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>nonqualified</i> counterparties approved by the board of directors or a committee thereof. Compared the name of the counterparty involved in the collar transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or a committee thereof to trade collar contracts. Compared the name of the individual who executed the execution or closeout of the collar contract with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve payments relating to collars. Compared the name of the individual who approved any payment relating to the collar with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the collar with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the collar with the name of the individual who entered	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the execution or closeout of the collar and found that the execution or closeout was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade collars and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the collar contract, as stated on the deal ticket and confirmation, with the terms of the collar contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period (for example, monthly or quarterly), indicating that the insurance company determined that its accounting records for collars, tested in procedure 18, agreed with or reconciled to the related control account; for example, the subsidiary ledger to the general ledger.	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the collar agreement. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
21. Compared the terms of the collar agreement recorded in the insurance company's accounting records with the terms shown in the executed copy of the collar agreement and found them to be in agreement.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
22. Obtained documentation for one reporting period (for example, monthly or quarterly), indicating that the insurance company physically inventoried the collar agreement.	_____	_____	_____
23. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the collar contracts with the names of individuals authorized to enter into trades, executions, or closeouts of collar contracts and found that the name of the individual was not on the list.	_____	_____	_____
24. Compared information regarding the collar, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
25. If the collar should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the collar, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
26. Read accounting documentation indicating that the insurance company monitored periodic cash settlements related to the collar tested, meaning, the insurance company had controls in place to determine that periodic cash settlements, if any, were received.	_____	_____	_____
Effectiveness of Collars Used As Hedges and in Replication Transactions			
27. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A

the effectiveness of the collar as a hedge or replication in accordance with the policies regarding effectiveness.

28. If the collar was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.

Legal Review

29. Read documentation indicating that the legal department reviewed the collar agreement to assess contract compliance with the DUP and enforceability.

30. Read documentation indicating that the legal department updated its assessment of agreement enforceability at least annually.

Valuation

31. Obtained the insurance company's policies and procedures for valuing collars and found that the insurance company determined the fair value of the collar in accordance with the policy described in the insurance company's procedures for the valuation of collars.

32. Read documentation supporting the fair value of the collar and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.

Description of Exceptions if Any

Procedure Number

Description of Exception

Section 4—Floor Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected floor contracts to test internal control over floor transactions. Selected five percent of each type of floor transaction (that is, purchases [premium disbursements], sales [premium receipts], and closeouts [closings and settlements of the position]), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all the transactions of that type.</p>			
Reporting			
1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to enter into floor contracts.	_____	_____	_____
2. For each floor selected for testing, read management's documentation describing the intended use of the floor and performed the following procedures, as applicable.	_____	_____	_____
For floors used as a hedge—			
3. Determined that the documentation described the following:			
a. The risk hedged	_____	_____	_____
b. How the hedge was consistent with the overall risk management strategy	_____	_____	_____
c. How the floor was expected to be effective in offsetting the exposure	_____	_____	_____
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the floor as a hedge	_____	_____	_____
b. The terms of the floor, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the floor hedged	_____	_____	_____
d. Evidence that the floor continued to be an effective hedge	_____	_____	_____
e. Evidence that the floor was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures for entering into hedge transactions; for example, the notional amount or underlying	_____	_____	_____
If the floor was an exact offset of an outstanding floor—			
5. Read documentation indicating that the floor offset an outstanding floor previously purchased or sold by the insurance company and that the floor was an exact offset of the market risk of the floor being offset.	_____	_____	_____
For floors used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the floor was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the floor, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected floors including those that are a part of a replication transaction—			
8. Obtained a list of individuals approved by the board of directors or a committee thereof who had the authority to authorize floor transactions. Compared the name of the individual who authorized the floor transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount or strike price exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>non-qualified</i> counterparties, approved by the board of directors or a committee			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
thereof. Compared the name of the counterparty involved in the floor transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or a committee thereof to trade floor contracts. Compared the name of the individual who executed the purchase, sale, or closeout of the floor with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve payments relating to floors. Compared the name of the individual who approved any payment relating to the floor with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the floor with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the floor with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the purchase, sale, or closeout of the floor and found that the purchase,			

Procedures	Findings		
	No Exception	Exception	N/A
sale, or closeout was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade floors and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the floor contract, as stated on the deal ticket and confirmation, with the terms of the floor contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period (for example, monthly or quarterly), that the insurance company determined that its accounting records for floors, tested in procedure 18, agreed with or reconciled to the related control account; for example, the subsidiary ledger to the general ledger.	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the floor agreement. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
21. Compared the terms of the floor agreement recorded in the insurance company's accounting records with the terms shown in the executed copy of the floor agreement and found them to be in agreement.	_____	_____	_____
22. Obtained documentation for one reporting period (for example, monthly or quarterly), indicating that the insurance company physically inventoried the floor agreements.	_____	_____	_____

(continued)

Findings

Procedures	No Exception	Exception	N/A
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- | | | | |
|---|-------|-------|-------|
| <p>23. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the floor agreement with the names of individuals authorized to execute purchases, sales, or closeouts of floor contracts and found that the name was not on the list.</p> | _____ | _____ | _____ |
| <p>24. Compared information regarding the floor, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.</p> | _____ | _____ | _____ |
| <p>25. If the floor should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the floor, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.</p> | _____ | _____ | _____ |
| <p>26. Read accounting documentation indicating that the insurance company monitored periodic cash settlements related to the floor tested, meaning, the insurance company had controls in place to determine that periodic cash settlements, if any, were received.</p> | _____ | _____ | _____ |

Effectiveness of Floors Used As Hedges and in Replication Transactions

- | | | | |
|---|-------|-------|-------|
| <p>27. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the floor as a hedge or replication in accordance with the policies regarding effectiveness.</p> | _____ | _____ | _____ |
| <p>28. If the floor was no longer effective as a hedge or replication, compared the ac-</p> | _____ | _____ | _____ |

Procedures	Findings		
	No Exception	Exception	N/A
tion taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____
Legal Review			
29. Read documentation indicating that the legal department reviewed the floor agreement to assess contract compliance with the DUP and enforceability.	_____	_____	_____
30. Read documentation indicating that the legal department updated its assessment of agreement enforceability at least annually.	_____	_____	_____
Valuation			
31. Obtained the insurance company's policies and procedures for valuing floors and found that the insurance company determined the fair value of the floor in accordance with the policy described in the insurance company's procedures for the valuation of floors.	_____	_____	_____
32. Read documentation supporting the fair value of the floor and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.	_____	_____	_____

Description of Exceptions if Any

Procedure Number	Description of Exception
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(continued)

Section 5—Forward Contracts

Procedures	Findings		
	No Exception	Exception	N/A

Performed the following procedures on selected forward contracts to test internal control over forward transactions. Selected five percent of each type of forward transaction, with the selections distributed throughout the year. These are, (1) forward contracts entered into to make delivery, (2) forward contracts entered into to take delivery, (3) forward contracts settled by making delivery, (4) forward contracts settled by taking delivery, (5) forward contracts settled by cash. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all of the transactions of that type.

Reporting

1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to enter into forward contracts.
2. For each forward selected for testing, read management's documentation describing the intended use of the forward and performed the following procedures, as applicable.

_____	_____	_____
_____	_____	_____

For forward contracts used as a hedge—

3. Determined that the documentation describes the following:
 - a. The risk hedged
 - b. How the hedge was consistent with the overall risk management strategy
 - c. How the forward was expected to be effective in offsetting the exposure

_____	_____	_____
_____	_____	_____
_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____
4. Determined that the following items were documented:			
a. The purpose(s) of the forward as a hedge	_____	_____	_____
b. The terms of the forward, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the forward hedged	_____	_____	_____
d. The specific forward contract used in the hedge	_____	_____	_____
e. Evidence that the forward continued to be an effective hedge	_____	_____	_____
f. Evidence that the forward was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures, for entering into hedge transactions; for example, the notional amount or underlying	_____	_____	_____
If the forward was an exact offset of an outstanding forward—			
5. Read documentation indicating that the forward offset an outstanding forward previously purchased or sold by the insurance company and that the forward was an exact offset of the market risk of the forward being offset.	_____	_____	_____
For forwards used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the forward was expected to be effective in replicating the investment characteristic of the replicated investment	_____	_____	_____
d. The approach for assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the forward contract, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected forwards, including those that are a part of the replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof who had the authority to authorize forward transactions. Compared the name of the individual who authorized the forward transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the			

Procedures	Findings		
	No Exception	Exception	N/A
transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>nonqualified</i> counterparties, approved by the board of directors or a committee thereof. Compared the name of the counterparty involved in the forward transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or committee thereof to trade forward contracts. Compared the name of the individual who executed the purchase or sale of the forward with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve settlements or payments related to forward contracts. For the purchase and any transaction subsequent to purchase, compared the name of the individual who approved any payment or settlement of funds in connection with the forward contract with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any settlement or payment relating to the forward with the name of the individual who approved en-	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
tering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the forward with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the purchase or sale of the forward contract and found that the purchase or sale was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade forwards and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the forward contract, as stated on the deal ticket and confirmation, with the terms of the forward contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period, (for example, monthly or quarterly), that the insurance company determined that its accounting records for forwards, tested in procedure 18, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the forward contract. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
21. For one reporting period, (for example, monthly or quarterly), obtained the insurance company's documentation of the existence of the forward contract and found that the insurance company either (a) obtained a statement from the custodian confirming the existence of the forward contract, (b) physically inventoried the forward contract, or (c) obtained a statement from the counterparty acknowledging the existence of the forward contract	_____	_____	_____
22. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the forward with the names of individuals authorized to execute purchases and sales of forwards and found that the name was not on the list.	_____	_____	_____
23. Compared information regarding the forward, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
24. If the forward should have been included in the monitoring analysis separately tested in step 10 within section 1, "All Derivative Types," compared information regarding the forward, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
Effectiveness of Forward Contracts Used As Hedges and in Replication Transactions			
25. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the forward as a			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
26. If the forward was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____
Legal Review			
27. Read documentation indicating that the legal department reviewed the forward contract to assess contract compliance with the DUP and enforceability.	_____	_____	_____
28. Read documentation indicating that the legal department updated its assessment of contract enforceability at least annually.	_____	_____	_____
Valuation			
29. Obtained the insurance company's policies and procedures for valuing forwards and found that the insurance company determined the fair value of the forward in accordance with the policy described in the insurance company's procedures for valuation of forwards.	_____	_____	_____
30. Read documentation supporting the fair value of the forward contract and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.	_____	_____	_____

Description of Exceptions if Any

Procedure Number

Description of Exception

Section 6—Futures Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected futures contracts to test internal control over futures transactions. Selected five percent of each type of futures transactions with the selections distributed throughout the year. These are purchases, sales, and cash settlements (closeouts of a position). If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all of the transactions of that type.</p>			
Reporting			
1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to trade futures.	_____	_____	_____
2. For each futures transaction selected for testing, read management's documentation describing the intended use of the futures and performed the following procedures, as applicable.	_____	_____	_____
For futures used as a hedge—			
3. Determined that the documentation describes the following:			
a. The risk hedged	_____	_____	_____
b. How the hedge was consistent with the overall risk management strategy	_____	_____	_____
c. How the futures position was expected to be effective in offsetting the exposure	_____	_____	_____
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the futures as a hedge	_____	_____	_____
b. The terms of the futures transaction and the name of the exchange and firm(s) handling the trade	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the futures transaction hedged	_____	_____	_____
d. Evidence that the futures contract continued to be an effective hedge	_____	_____	_____
e. Evidence that the futures position was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures for futures transactions; for example, the notional amount or underlying	_____	_____	_____
For futures transactions that were an exact offset of an outstanding futures transaction—			
5. Read documentation indicating that the futures transaction offset an outstanding futures position previously purchased or sold by the insurer and that the futures transaction was an exact offset of the market risk of the futures position being offset.	_____	_____	_____
For futures used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
c. How the futures position was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the futures transaction and the name of the exchange and the firm(s) handling the trade	_____	_____	_____
c. The specific futures contract used in the replication	_____	_____	_____
For all selected futures including those that are a part of the replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof, who had the authority to authorize futures trades. Compared the name of the individual who authorized the futures transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
support and found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of individuals authorized by the board of directors or committee thereof to trade futures contracts. Compared the name of the individual who executed the purchase or sale of the futures contract with the names on the list and found the name of the individual on the list.	_____	_____	_____
11. Obtained a list of individuals authorized to approve settlements or disbursements related to futures transactions. For purchases and transactions subsequent to purchase or sale of the futures contract, compared the name of the individual who approved any settlement of funds relating to the futures with the names on the list and found the name of the individual on the list.	_____	_____	_____
12. Compared the name of the individual who approved any payment relating to the futures with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
13. Compared the name of the individual who received cash or other consideration in connection with the futures with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
14. Obtained the deal ticket and confirmation for the purchase, expiration, or sale of the futures contracts and found that the purchase, sale, or expiration of the futures contract was confirmed by the deal ticket and confirmation.	_____	_____	_____
15. Compared the terms of the futures transaction, as stated on the deal ticket and confirmation, with the terms of the	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
transaction recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
16. Obtained documentation for one reporting period, (for example, monthly or quarterly), that the insurance company determined that its accounting records for futures, tested in procedure 15, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
17. For one reporting period, (for example, monthly or quarterly), obtained the insurance company's documentation of the existence of the futures contracts and found that the insurance company obtained statements from the futures counterparty(ies) or broker(s) confirming the futures transactions and positions.	_____	_____	_____
18. Compared information regarding the futures contract, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
19. If the futures position should have been included in the monitoring analysis separately tested in procedure 10 within section 1, " All Derivative Types," compared information regarding the futures contract, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
Effectiveness of Futures Used As Hedges and in Replication Transactions			
20. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
the effectiveness of the futures position as a hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
21. If the futures position was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the company policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____

Valuation

22. Obtained the insurance company's policies and procedures for valuing positions and found that the insurance company determined the valuation of the futures contract in accordance with the policy described in the insurance company's procedures for valuation of futures.	_____	_____	_____
23. Read documentation supporting the market price of the futures contract and found that the market price was obtained from an independent source.	_____	_____	_____

Description of Exceptions if Any

Procedure Number	Description of Exception
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Section 7—Option Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected option contracts to test internal control over option transactions. Selected five percent of each type of option transaction (that is, purchases, sales, expirations, and exercises), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all of the transactions of that type.</p>			
Reporting			
1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to trade or enter into option contracts.	_____	_____	_____
2. For each option selected for testing, read management's documentation describing the intended use of the option and performed the following procedures, as applicable.	_____	_____	_____
For options used as a hedge—			
3. Determined that the documentation described the following:			
a. The risk hedged	_____	_____	_____
b. How the hedge was consistent with the overall risk management strategy	_____	_____	_____
c. How the option was expected to be effective in offsetting the exposure	_____	_____	_____
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the option as a hedge	_____	_____	_____
b. For over-the-counter (OTC) options, the terms of the option, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. For exchange-traded options, the term of the option, the name of the exchange, and the name of the firm(s) handling the trade	_____	_____	_____
d. The assets or liabilities (or portion thereof) that the option hedged	_____	_____	_____
e. For OTC and exchange-traded options, the specific option used in the hedge	_____	_____	_____
f. Evidence that the option continued to be an effective hedge	_____	_____	_____
g. Evidence that the option was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures, for entering into hedge transactions; for example, the notional amount, or underlying	_____	_____	_____
If the option transaction was (a) for income generation and was for the sale of a call option on securities or (b) an exact offset to an outstanding option—	_____	_____	_____
5. Read the documentation supporting the transaction which indicated that the insurance company was holding or could immediately acquire through the exercise of options, warrants, or conversion rights already owned, the underlying securities during the entire period the option was outstanding.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
6. Read documentation indicating that the option offset an outstanding option previously purchased or sold by the insurance company and that the option was an exact offset to the market risk of the option being offset.	_____	_____	_____
For options used in a replication transaction—			
7. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the option was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
8. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The specific option used in the replication	_____	_____	_____
c. For OTC options, the terms of the option, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
d. For exchange-traded options, the name of the exchange and the firm(s) handling the trade	_____	_____	_____
For all selected options, including those that are a part of a replication transaction—			

(continued)

Findings

Procedures	No Exception	Exception	N/A
9. Obtained a list of individuals, approved by the board of directors or a committee thereof, who had the authority to authorize option transactions. Compared the name of the individual who authorized the option transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
10. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____
11. Obtained a list of <i>qualified</i> and <i>non-qualified</i> counterparties, approved by the board of directors or a committee thereof. Compared the name of the counterparty involved in the option transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
12. For OTC options, determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 11.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
13. Obtained a list of individuals authorized by the board of directors or committee thereof to trade option contracts. Compared the name of the individual who executed the purchase, sale, or exercise of the option with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Obtained a list of individuals authorized to approve payments relating to options contracts. Compared the name of the individual who approved any payment relating to the option with the names on the list and found the name of the individual on the list.	_____	_____	_____
15. Compared the name of the individual who approved any payment relating to the option with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
16. Compared the name of the individual who received cash or other consideration in connection with the option with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
17. Obtained the deal ticket and confirmation for the purchase, sale, or exercise of the option and found that the purchase, sale, or exercise of the option was confirmed by the counterparty or firm handling the transaction.	_____	_____	_____
18. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade options and found that the name was not on the list.	_____	_____	_____
19. Compared the terms of the option contract, as stated on the deal ticket and confirmation, with the terms of the op-	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
tion contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
20. Obtained documentation for one reporting period, (for example, monthly or quarterly), indicating that the insurance company determined whether its accounting records for options, tested in procedure 19, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
21. Obtained the accounting record documenting modifications, if any, to the option transaction. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
22. Obtained documentation for one reporting period, (for example, monthly or quarterly), indicating that the insurance company obtained a statement from the counterparty confirming the existence of the option position.	_____	_____	_____
23. Using the list of authorized traders obtained in procedure 13, compared the name of the individual who had custody of or access to the option documentation with the names of individuals authorized to purchase, sell, or exercise the option and found that the name was not on the list.	_____	_____	_____
24. Compared information regarding the option, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
25. If the option should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the option, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
Effectiveness of Options Used As Hedges and in Replication Transactions			
26. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the option as a hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
27. If the option was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____
Legal Review			
28. Read documentation indicating that the legal department reviewed the option agreement to assess contract compliance with the DUP and enforceability.	_____	_____	_____
29. Read documentation indicating that the legal department updated its assessment of legal enforceability of the OTC option agreement at least annually.	_____	_____	_____
Valuation			
30. Obtained the insurance company's policies and procedures for valuing options and found that the insurance company determined the fair value of OTC options and the market price of exchange-			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
traded options, in accordance with the policy described in the insurance company's procedures for the valuation of options.	_____	_____	_____
31. Read documentation supporting the fair value for OTC options and the market price of exchange-traded options and found that the fair value or market value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.	_____	_____	_____

Description of Exceptions if Any

Procedure Number	Description of Exception
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Section 8—Swap Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected swap contracts to test internal control over swap transactions. Selected five percent of each type of swap transaction (that is, executions [purchases] and close-outs [sales]), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in fewer than four items, selected four or fewer items that represented all the transactions of that type.</p>			
Reporting			
<p>1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to enter into swap agreements.</p>	_____	_____	_____
<p>2. For each swap agreement selected for testing, read management's documentation describing the intended use of the swap agreement and performed the following procedures, as applicable.</p>	_____	_____	_____
For swaps used as a hedge—			
<p>3. Determined that the documentation describes the following:</p>			
<p>a. The risk hedged</p>	_____	_____	_____
<p>b. How the hedge was consistent with the overall risk management strategy</p>	_____	_____	_____
<p>c. How the swap was expected to be effective in offsetting the exposure</p>	_____	_____	_____
<p>d. The approach in assessing the effectiveness of the hedge</p>	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the swap as a hedge	_____	_____	_____
b. The terms of the swap, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the swap hedged	_____	_____	_____
d. Evidence that the swap continued to be an effective hedge	_____	_____	_____
e. Evidence that the swap was consistent with the insurance company's parameters, as specified in the DUP or applicable policies and procedures, for entering into swap agreements; for example, the notional amount or underlying	_____	_____	_____
For swaps that were an exact offset of an outstanding swap—			
5. Read documentation that indicated that the swap offset a swap previously purchased or sold, and that the swap was an exact offset to the market risk of the swap being offset.	_____	_____	_____
For swaps used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the swap was expected to be effective in replicating the investment characteristic of the replicated investment	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the swap, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected swaps including those that are a part of a replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof who had the authority to authorize swap transactions. Compared the name of the individual who authorized the swap transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transactions tested; for example, a transaction in which the notional amount exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>non-qualified</i> counterparties, approved by the board of directors or a committee thereof. Compared the name of the			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
counterparty involved in the swap agreement with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or committee thereof to trade swap contracts. Compared the name of the individual who executed the swap with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve settlements or disbursements related to swaps. For purchases and any interim settlements or closeouts of the swap subsequent to purchase, compared the name of the individual who approved any settlement of funds relating to the swap with the names on the list and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the swap with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the swap with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the purchase, execution, or	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
closeout of the swap and found that the purchase, execution, or closeout of the swap was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade swaps and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the swap contract, as stated on the deal ticket and confirmation, with the terms of the swap contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period, (for example, monthly or quarterly), that the insurance company determined whether its accounting records for swaps, tested in procedure 18, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the swap agreement. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
21. Compared the terms of the swap agreement recorded in the insurance company's accounting records with the terms shown in the executed copy of the swap agreement and found them to be in agreement.	_____	_____	_____
22. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the swap agreement with	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
the names of individuals authorized to execute swap agreements and found that the name was not on the list.	_____	_____	_____
23. Compared information regarding the swap, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
24. If the swap should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the swap, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
25. Read accounting documentation indicating that the insurance company monitored periodic cash settlements related to swap transactions, meaning, the insurance company had controls in place to determine that periodic cash settlements, if any, were received.	_____	_____	_____
Effectiveness of Swaps Used As Hedges and in Replication Transactions			
26. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the swap as a hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
27. If the swap was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
Legal Review			
28. Read documentation indicating that the legal department reviewed the swap agreement to assess contract compliance with the DUP and enforceability.	_____	_____	_____
29. Read documentation indicating that the legal department updated its assessment of the enforceability of the swap agreement at least annually.	_____	_____	_____
Valuation			
30. Obtained the insurance company's policies and procedures for valuing swaps and found that the insurance company determined the fair value of the swap in accordance with the policy described in the insurance company's procedures for valuation of swaps.	_____	_____	_____
31. Read documentation supporting the fair value of the swap and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.	_____	_____	_____

Description of Exceptions if Any

Procedure Number	Description of Exception
------------------	--------------------------

(continued)

Section 9—Swaption Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected swaption contracts to test internal control over swaption transactions. Selected five percent of each type of swaption transaction with the selections distributed throughout the year. These are executions (purchases) and closeouts (sales). If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all the transactions of that type.</p>			
<p>Reporting</p>			
<p>1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to buy or sell swaptions.</p>	_____	_____	_____
<p>2. For each swaption contract selected for testing, read management's documentation describing the intended use of the swaption and performed the following procedures, as applicable.</p>	_____	_____	_____
<p>For swaptions used as a hedge—</p>			
<p>3. Determined that the documentation describes the following:</p>			
<p>a. The risk hedged</p>	_____	_____	_____
<p>b. How the hedge was consistent with the overall risk management strategy</p>	_____	_____	_____
<p>c. How the swaption was expected to be effective in offsetting the exposure</p>	_____	_____	_____
<p>d. The approach in assessing the effectiveness of the hedge</p>	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
4. Determined that the following items were documented:			
a. The purpose(s) of the swaption as a hedge	_____	_____	_____
b. The terms of the swaption, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
c. The assets or liabilities (or portion thereof) that the swaption hedged	_____	_____	_____
d. Evidence that the swaption continued to be an effective hedge	_____	_____	_____
e. Evidence that the swaption was consistent with the insurance company's parameters, as specified in the DUP or applicable policies and procedures, for entering into swaption agreements; for example, the notional amount or underlying	_____	_____	_____
For swaptions that were an exact offset of an outstanding swaption—			
5. Read documentation indicating that the swaption offset an outstanding swaption and that the swaption was an exact offset of the market risk of the swaption being offset.	_____	_____	_____
For swaptions used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____
c. How the swaption was expected to be effective in replicating the investment			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
characteristic of the replicated investment	_____	_____	_____
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The terms of the swaption, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected swaptions including those that are a part of a replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof, who had the authority to authorize swaptions. Compared the name of the individual who authorized the swaption transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transactions tested; for example, a transaction in which the notional amount exceeded a limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support and found evidence of approval of the transaction tested.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
10. Obtained a list of <i>qualified</i> and <i>nonqualified</i> counterparties, approved by the board of directors or a committee thereof. Compared the name of the counterparty involved in the swaption transaction with names on the list and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. Determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or committee thereof to trade swaption contracts. Compared the name of the individual who executed the swaption with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve settlements or disbursements related to swaption agreements. Compared the name of the individual who approved settlements and disbursements relating to the swaption with the names on the list and found the name on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the swaption with the name of the individual who approved entering into the contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the swaption with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
16. Obtained the deal ticket and confirmation for the purchase, sale, modification, or closeout of the swaption and found that the purchase, sale, modification, or closeout was confirmed by the counterparty.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade swaptions and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the swaption contract, as stated on the deal ticket and confirmation, with the terms of the swaption contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period, (for example, monthly or quarterly), that the insurance company determined whether its accounting records for swaptions, tested in procedure 18, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the swaption agreement. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual who approved the modification on the list.	_____	_____	_____
21. Compared the terms of the swaption agreement recorded in the insurance company's accounting records with the terms shown in the executed copy of the swaption agreement and found them to be in agreement.	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
22. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody or access to the swaption agreement with the names of individuals authorized to execute swaption agreements and found that the name was not on the list.	_____	_____	_____
23. Compared information regarding the swaption, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
24. If the swaption should have been included in the monitoring analysis separately tested in procedure 10 within section 1, "All Derivative Types," compared information regarding the swaption, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____
Effectiveness of Swaptions Used As Hedges and in Replication Transactions			
25. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the swaption as a hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
26. If the swaption was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A

Legal Review

- | | | | |
|--|-------|-------|-------|
| 27. Read documentation indicating that the legal department reviewed the swaption agreement to assess contract compliance with the DUP and enforceability. | _____ | _____ | _____ |
| 28. Read documentation indicating that the legal department updated its assessment of the enforceability of the swaption agreement at least annually. | _____ | _____ | _____ |

Valuation

- | | | | |
|---|-------|-------|-------|
| 29. Obtained the insurance company's policies and procedures for valuing swaptions and found that the insurance company determined the fair value of the swaption in accordance with the policy described in the insurance company's procedures for valuation of swaptions. | _____ | _____ | _____ |
| 30. Read documentation supporting the fair value of the swaption and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual. | _____ | _____ | _____ |

Description of Exceptions if Any

Procedure Number	Description of Exception
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Section 10—Warrant Contracts

Procedures	Findings		
	No Exception	Exception	N/A
<p>Performed the following procedures on selected warrant contracts to test internal control over warrant transactions. Selected five percent of each type of warrant transaction (that is, purchases, sales, expirations, and exercises), with the selections distributed throughout the year. If five percent of a given type of transaction exceeded 40, the number of items selected for that type of transaction was limited to 40. If five percent of a type of transaction resulted in less than four items, selected four or fewer items that represented all of the transactions of that type.</p>			
Reporting			
1. Read the insurance company's derivative use plan (DUP) and any amendments thereto and found that the DUP permits the insurance company to trade or enter into warrant contracts.	_____	_____	_____
2. For each warrant selected for testing, read management's documentation describing the intended use of the warrant and performed the following procedures, as applicable.	_____	_____	_____
For warrants used as a hedge—			
3. Determined that the documentation described the following:			
a. The risk hedged	_____	_____	_____
b. How the hedge was consistent with the overall risk management strategy	_____	_____	_____
c. How the warrant was expected to be effective in offsetting the exposure	_____	_____	_____
d. The approach in assessing the effectiveness of the hedge	_____	_____	_____
4. Determined that the following items were documented:			

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
a. The purpose(s) of the warrant as a hedge	_____	_____	_____
b. For exchange-traded warrants, the term of the warrant, the name of the exchange, and the name of the firm(s) handling the trade	_____	_____	_____
c. For over-the-counter (OTC) warrants, the terms of the warrant, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
d. The assets or liabilities (or portion thereof) that the warrant hedged	_____	_____	_____
e. Evidence that the warrant continued to be an effective hedge	_____	_____	_____
f. Evidence that the warrant was consistent with the insurance company's parameters, as specified in the DUP or applicable company policies and procedures for entering into hedge transactions; for example, the notional amount or underlying	_____	_____	_____
If the warrant transaction was an exact offset of an outstanding warrant—			
5. Read documentation indicating that the warrant transaction offset an outstanding warrant previously purchased or sold by the insurance company and that the warrant was an exact offset of the market risk of the warrant being offset	_____	_____	_____
For warrants used in a replication transaction—			
6. Determined that the documentation described the following:			
a. The investment type and characteristics replicated	_____	_____	_____
b. How the replication was consistent with the overall management investment strategy	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
c. How the warrant was expected to be effective in replicating the investment characteristics of the replicated investment	_____	_____	_____
d. The approach in assessing the effectiveness of the replication transaction	_____	_____	_____
7. Determined that the following items were documented:			
a. The instruments used in the replication and the investment type and characteristics replicated	_____	_____	_____
b. The specific warrant used in the replication	_____	_____	_____
c. For exchange-traded warrants, the name of the exchange and the firm(s) handling the trade	_____	_____	_____
d. For OTC warrants, the terms of the warrant, the name of the counterparty, and the counterparty exposure amount	_____	_____	_____
For all selected warrants including those that are part of a replication transaction—			
8. Obtained a list of individuals, approved by the board of directors or a committee thereof who had the authority to authorize warrant transactions. Compared the name of the individual who authorized the warrant transaction with the names on the list and found the name of the individual on the list.	_____	_____	_____
9. Based on the details of the transaction identified in procedure 2 and company policy, compared the terms of the transaction with the insurance company's policy regarding the requirement for the board of directors or a committee thereof to authorize the specific transaction tested; for example, a transaction in which the notional amount exceeded a			

(continued)

Findings

Procedures	No Exception	Exception	N/A
limit requiring additional approval. If the board of directors or a committee thereof was required to approve the transaction, read minutes of the board of directors or a committee thereof or other appropriate support, and found evidence of approval of the transaction tested	_____	_____	_____
10. Obtained a list of <i>qualified</i> and <i>nonqualified</i> counterparties, approved by the board of directors or a committee thereof. Compared the name of the counterparty involved in the warrant transaction with names on the list, and found the name of the counterparty on the respective qualified or nonqualified list.	_____	_____	_____
11. For OTC warrants, determined that the counterparty was listed as qualified or nonqualified in the analysis used for monitoring the insurance company's limitations on counterparty exposure, consistent with the classification in the listing obtained in procedure 10.	_____	_____	_____
12. Obtained a list of individuals authorized by the board of directors or committee thereof to trade warrant contracts. Compared the name of the individual who executed the purchase, sale, or exercise of the warrant with the names on the list and found the name of the individual on the list.	_____	_____	_____
13. Obtained a list of individuals authorized to approve payments related to warrant contracts. Compared the name of the individual who approved any payment relating to the warrant with the names on the list, and found the name of the individual on the list.	_____	_____	_____
14. Compared the name of the individual who approved any payment relating to the warrant with the name of the individual who approved entering into the	_____	_____	_____

Procedures	Findings		
	No Exception	Exception	N/A
contract and found that the names were different.	_____	_____	_____
15. Compared the name of the individual who received cash or other consideration in connection with the warrant with the name of the individual who entered into the contract and found that the names of the individuals were different.	_____	_____	_____
16. Obtained the deal ticket and confirmation for the purchase, sale, or exercise of an exchange-traded warrant and found that the purchase, sale, or exercise was confirmed by the firm handling the transaction.	_____	_____	_____
17. Compared the name of the individual who received the deal ticket and confirmation with the names on a list of individuals authorized to trade warrants and found that the name was not on the list.	_____	_____	_____
18. Compared the terms of the warrant contract, as stated on the deal ticket and confirmation, with the terms of the warrant contract recorded in the insurance company's accounting records and found them to be in agreement.	_____	_____	_____
19. Obtained documentation for one reporting period, (for example, monthly or quarterly), that the insurance company determined whether its accounting records for warrants, tested in procedure 18, agreed with or reconciled to the related control account, (for example, the subsidiary ledger to the general ledger).	_____	_____	_____
20. Obtained the accounting record documenting modifications, if any, to the warrant transaction. Compared the name of the individual who approved the modification with a list of individuals authorized to approve modifications and found the name of the individual	_____	_____	_____

(continued)

Procedures	Findings		
	No Exception	Exception	N/A
who approved the modification on the list.	_____	_____	_____
21. For one reporting period, (for example, monthly or quarterly), obtained the insurance company's documentation of the existence of the warrant contract and found that the insurance company either (a) obtained statements from the custodian confirming the existence of the warrant contracts or (b) physically inventoried the warrant contracts.	_____	_____	_____
22. Using the list of authorized traders obtained in procedure 12, compared the name of the individual who had custody of or access to the warrant contracts with the names of individuals authorized to execute purchases, sales, or exercises of warrants and found that the name was not on the list.	_____	_____	_____
23. Compared information regarding the warrant, such as type of derivative, notional amount, and fair value, with the comparable information included in the report to the board of directors or appropriate committee thereof and found them to be in agreement.	_____	_____	_____
24. If the warrant position should have been included in the monitoring analysis separately tested in procedure 10 of section 1, "All Derivative Types," compared information regarding the warrant, such as type of derivative, notional amount, and fair value, with the comparable information in the monitoring analysis and found them to be in agreement.	_____	_____	_____

Effectiveness of Warrants Used As Hedges and in Replication Transactions

25. Read the insurance company's documentation of effectiveness and found that the insurance company evaluated the effectiveness of the warrant as a

Procedures	Findings		
	No Exception	Exception	N/A
hedge or replication in accordance with the policies regarding effectiveness.	_____	_____	_____
26. If the warrant was no longer effective as a hedge or replication, compared the action taken by the insurance company with the action required by the accounting policies and procedures and found that the action taken was consistent with the accounting policy.	_____	_____	_____
Legal Review			
27. Read documentation indicating that the legal department reviewed a nonexchange traded warrant agreement to assess contract compliance with the DUP and enforceability.	_____	_____	_____
28. Read documentation indicating that the legal department updated its assessment of enforceability of the nonexchange traded warrant agreement at least annually.	_____	_____	_____
Valuation			
29. Obtained the insurance company's policies and procedures for valuing warrants and found that the insurance company determined the fair value of the warrant in accordance with the policy described in the insurance company's procedures for the valuation of warrants	_____	_____	_____
30. Read documentation supporting the fair value of warrants and found that the fair value was either (a) obtained from an independent source, (b) checked against an independent source, or (c) calculated internally by an authorized individual.	_____	_____	_____

Description of Exceptions if Any

Procedure Number

Description of Exception

APPENDIX C

Illustrative Management Representation Letter

[Responsible Party's Letterhead]

[Date]

[CPA Firm's Name and Address]

In connection with your engagement to apply the agreed-upon procedures enumerated in the American Institute of Certified Public Accountants' Statement of Position 01-03, *Performing Agreed-Upon Procedures Engagements that Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law*, which were agreed to by management of ABC Insurance Company, solely to assist us in complying with the requirements of Section 1410 (b)(5) of the New York State Insurance Law, as amended (the Law), which addresses the assessment of internal control over derivative transactions as defined in Section 1401 (a) of the Law and Section 178.6 of Regulation No. 163 during the year ended December 31, 20XX, we confirm, to the best of our knowledge and belief, the following representations made to you during your engagement:

1. We are responsible for establishing and maintaining effective internal control over derivative transactions in accordance with the Law.
2. During the year ended December 31, 20XX, the internal control over derivative transactions was functioning in accordance with the policies and procedures set forth in the Company's derivative use plan (DUP) and related accounting policies and procedures. There have been no errors or fraud that would indicate a weakness in the internal control over derivative transactions.
3. We have disclosed to you all significant deficiencies in the design or operation of the internal control over derivative transactions that would adversely affect the Company's ability to function in accordance with the Company's DUP.

4. There have been no communications from regulatory agencies, internal auditors, or other practitioners or consultants relating to the internal control over derivative transactions, including communications received between December 31, 20XX and the date of this letter.
5. We have made available to you all information that we believe is relevant to the internal control over derivative transactions.
6. We have responded fully to all inquiries made to us by you during the engagement.

To the best of our knowledge and belief, no events have occurred subsequent to December 31, 20XX and through the date of this letter that would require adjustment to or modification of the findings of the agreed-upon procedures.

[*Signature*]

[*Title*]

[*Signature*]

[*Title*]

Reporting on Controls Over Derivative Transactions at Insurance Entities Task Force

Albert J. Reznicek, Chair

Edward F. Bader

Darryl Briley

Ben B. Korbly

Edward J. Metzger

David A. Nachman

Paula C. Panik

Robert M. Solitro

Mary Todd Stocker

Deborah H. Whitmore

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AICPA Staff

Charles E. Landes

Director

Audit and Attest Standards

Judith M. Sherinsky

Technical Manager

Audit and Attest Standards