

CITIZENS PROPERTY INSURANCE CORPORATION  
TRANSCRIPT OF THE MINUTES OF THE  
AUDIT COMMITTEE MEETING HELD TUESDAY DECEMBER 6, 2016

A Board meeting of the Audit Committee of Citizens Property Insurance Corporation ("Citizens") was held at 1.00 pm on Tuesday December 6, 2016 in Maitland, FL.

The following members of the Audit Committee were present:

Juan Cocuy, Chairman  
Jim Henderson  
Bette Brown

The following Citizens staff members were present:

Jay Adams	Christine Ashburn
Steve Bitar	Violet Bloom
Kelly Booten	Bonnie Gilliland
Barry Gilway	Karen Holt
Spencer Kraemer	Paul Kutter
Joe Martins	Bruce Meeks
Jennifer Montero	Michael Peltier
John Rollins	Dan Sumner
Barbara Walker	David Woodruff
Andrew Woodward	

The following persons were present:

Brian Smith, Dixon Hughes Goodman  
Matt Church, Dixon Hughes Goodman  
Kapil Bhatia, Raymond James

The following persons attended by telephone:

Nancy Staff  
Becky Griffith  
Curt Overpeck  
Amy Chu  
Mark Casteel  
Amanda Smith

**Call Meeting to Order**

CHAIRMAN COCUY: Good afternoon, welcome, everybody. Juan Cocuy for the record, Chairman of the Audit Committee. Barbara, would you please call the roll call?

MS WALKER took the roll call and confirmed the Chairman had quorum.

CHAIRMAN COCUY: Thank you. We will begin the meeting with the approval of the prior Meeting Minutes.

**GOVERNOR BROWN proposed the motion and Governor Henderson seconded, to approve the minutes of the September 27, 2016 Audit Committee Meeting; all were in favor and the motion carried.**

CHAIRMAN COCUY: Minutes approved. Item number two is the report from the Office of the Internal Auditor, Joe Martins, please.

MR. MARTINS: Thank you, Mr. Chairman, for the record I am Joe Martins, Chief of Internal Audit. I would like to refer you to page 19 of your package, the Office of Internal Audit dashboard. On this page we first refer to an overview of the audit plan and secondly to plan changes. Every quarter and then basically every month we revisit the plan and re-examine the viability and whether anything is changing to confirm that it continues to provide the intended assurance. In the middle of the page you will see a graph that show where we spent our time in 2016. About 30 percent of our work was on insurance and operations, 34 percent in information technology, 14 percent in finance and accounting and the remainder on the rest of the organization. The right-hand graph looks at the audit plan by engagement type and there we focus on audit and advisory. For the last couple of years we have been moving slowly away from pure assurance audits to include advisory services and consulting work, and this year we managed 55 to 45 percent average between the two. At the bottom of the page we refer to changes to the plan. There were three canceled and one deferred engagement. Two of the canceled engagements were advisory work that, after assessment, it was determined that there was no specific need for us to assist the organization anymore. The second one, vendor management independent adjusters, is an audit that we canceled. Here we reassessed our approach for next year with Claims; had a discussion with the Chief Claims Officer and decided that this specific audit would probably not add that much value to the organization. There is some other advisory work that we will be doing for the claims environment. Another audit was deferred, third party access audit, that audit is currently in progress. We deferred it because that audit will be completed early next year. On page 20 I referred to the progress against plan. There you will see that 94 percent of the plan or 31 of the 33 projects are either completed or in draft format. We have two audit products that are currently in progress, both are advisory work. We refer to the IT governance advisory piece that we are currently busy with, as well as building consolidation monitoring. As you know we have already completed the building consolidation. The only piece that is still remaining there is our review of the management of the financial transactions associated to that project. In the middle of the page we highlight the work that we completed, there were four audits (assurance engagements) that we completed as well as five advisory engagements. With the audits we completed work on change management, administrative and executive expenses, legislative and federal change compliance and lastly, reinsurance. All of these audits resulted in a satisfactory rating. The administrative and executive expense audit is one that we do annually to assess executive expenses as well as how we manage our administrative expenses, and this year we confirmed that they have a mature controlling infrastructure in place managing the admin expenses.

Our year to date audit ratings highlight our results for the year, and you will see that 69 percent of the work that we have done was really satisfactory or needs minor improvement with the remainder as needs improvement. And a little bit later when you look at the control efficiency resolutions you will see that these are being managed quite well. On page 21 we highlight the work that we are doing in the internal control framework and the progress that we are making there. We have 47 total engagements of which we completed 26 with four currently in progress. At the bottom of the page is a graph showing the way we spend our time and which of these engagements have been done. We completed the reviews in HR, finance and accounting. There are three that are remaining that we haven't started with yet, and then legal and underwriting that we need to finalize as well. The majority of the work that is currently needing to be done is in IT and the reason that we have not completed that work is because we were recruiting for an IT specialist that has current knowledge and experience, and we haven't been that successful in finding the appropriate person for that role. What we have done this year after we had numerous attempts and about three years search, we have chosen to transfer one of our IT staff to that role and to reduce the audit staff next year by one, transferring one of those staff to work full time on this project and help

us complete those engagements. On page 22 we focus on control deficiency resolution and the first graph on that page is showing a slow digression of the number of open items quarter on quarter. We started off Q4 2015 with 16, this year around we are ending at nine and we expect that by the end of this year we will only have one open deficiency that hasn't been finalized yet. That excludes the work that we are still finalizing. The item that will remain refers to access to claimants' medical records and there is a system change that needs to take place in the Claims Center. They are currently assessing the ability of the Claims Center to restrict access to these medical records and put it in place, and it is foreseen that that this will be finalized by February 2017.

On page 23 we mention staffing and we highlight in the graph on the left-hand side that there are three vacancies at the moment. One is in internal audit and refers to the Forensic Audit Manager that we are recruiting, and then we have two vacancies in Enterprise Risk Management: a director as well as one staff, and we are working at finding those people.

I would like to refer you to page 25, which is the Office of the Internal Audit 2017 Audit Strategy and Plan. In this document, on page 28, we focus on the audit plan and process, and I will just briefly go through that. For this year we followed a detailed annual planning process which is regularly revisited throughout the year and adjusted to accommodate the changes in the organization, risk opportunity and profile. We define for the audit universe and I will mention the universe a little bit later, and we prioritize our work to determine whether Citizens' network of risk and opportunity management internal control and governance processes as designed and presented by management, are adequate and functioning as expected. The risk factors considered while reviewing the units in the universe included the control environment, business exposure, compliance requirements, reputational image factors, organizational change with growth, and management of the internal audit discretion. We realize that pure assurance activities are not the only solution to accomplish our goals and offer other services to add value to the company. Instead of pure audits we will try next year to have about a 50/50 exposure towards audit and advisory services to the business. Apart from consulting advisory we will also do project audits for specific projects next year. One of the specific ones that we will focus on is the ERP implementation. We do compliance audits and there are a couple in the plan. Forensic audits, investigations were needed, we also do training and education to the organization with respect to controls and control management and then risk assessments. In developing the audit plan and approach we consulted with other internal assurance providers and here we specifically refer to the compliance office, ERM, the internal control function and we also consulted with the Inspector General and with the external auditors. We shared the audit schedule with the external auditors and we will continue our discussions with them as the year progresses and adjust our plan where appropriate in order to provide opportunity for them to rely on the Office of Internal Audit's work where they see fit. On page 31 I would like to highlight the organization and administration, and specifically looking at the organization chart of the Office of the Internal Auditor. There we have three areas that we focus on: Enterprise Risk Management, internal audit and internal controls function. The ICF team consists of three staff. At the moment two of those staff are provided by audit, the manager as well as the COBIT IT specialist, and one staff is provided by finance.

I would like to go to the specific audits and the audit areas that we are going to focus on. The first area is finance and ops and on page 36 we provide a listing of the audit work that we plan to do in 2017. In underwriting and agency services we intend to audit automated underwriting and the Call Center and in Claims we plan to do legal billing and litigation vendor management, claims payment process, vendor management, specifically focused towards the management repair program and the acuity system functionality. In accounting and finance we intend to continue with the CenterPoint project, the ERP project engagement. For Human Resources we are going to focus on self-funded benefit plan and in

Legal: we currently are executing a procurement audit. Advisory engagements will include claims adjuster resource validation, recruiting practices, water claims handling, expense ratio analysis benchmarking, self-service strategy, independent adjuster authority limits, non-automated personal lines underwriting, audit advisory engagement on FMAP, agency quality assurance and vendor management office processes. On page 38 we show the IT audits and you will see that the way IT audits work for 2017, we intend to focus more on the advisory rather than pure audit engagements. The audit engagement we have in place is a network assessment that we intend to complete during the middle of the year. The IT audit security function every year performs some sort of a network assessment. This year we will partner with them and at the same time do an assessment ourselves to provide some assurance that there is sufficient management at this time. The advisory engagements we intend to complete in 2017, include data retention, end user computing, IT compliance program, IT security logging, shared storage and third-party access. On page 39 we highlight the compliance audit work that we intend to do, and specifically with the compliance audit we align closely with the Inspector General and give the Inspector General an opportunity to provide staffing and we co-source with the Inspector General to complete some of this work. We have the Office of Foreign Access Control, policyholder disbursements, privacy, special pay programs, and advisory engagements we have legislative change compliance and own risk solvency assessment. We are aware that from an audit perspective we are not legally required to be compliant, but I think there is value in assessing what benefit there may be for Citizens to apply some of the best practices or leading practices. On page 41 we highlight the internal control assessments that we plan to complete including two in legal and compliance, three in finance and accounting, two in agency and consumer services. We will also commence with a COBIT assessment in IT during next year. And we will also be assisting the organization in completing the self-assessments closer to the end of the year.

CHAIRMAN COCUY: So you consider these hours audit or advisory?

MR. MARTINS: These hours are actually not included in the audit plan, per se, these are separated. We include in the plan to show it, but we haven't added that to the audit hours. We actually separated in the plan, separated risks as well as the internal control framework work from the audit work. So if we add it in it will be viewed as advisory, instead of field audit work, but it is not included in the number of hours that we added to the plan. But it would be advisory.

CHAIRMAN COCUY: The previous pages are weighted more towards audit engagements.

MR. MARTINS: Correct. On page 42 we have presented the 2017 financial budget. I think you will find that the budget is relatively aligned with the 2015 and 2016 budgets, and I want to highlight two specific areas. The first one is contingent staffing and the second is professional services. These two, really for our purposes work hand in hand with each other and the reason we have budgeted in those specific areas is that we feel that we may need some support, specifically when we look at the advisory work that we are doing and how we do these advisory engagements, in respect of external help and identification of what the leading practices are out there. Sometimes when you do the audit work and research for leading practices it is not that evident. We currently are using a service provider to help us with the IT governance audit where we completed the assessment of standards and guidelines that are out there, compared that with current business practice, but when we compared business practice to leading practice to assess what the world has out there, and how the world out there is applying the standards and the practices, we didn't find that much and we are using one of the external suppliers to provide us some guidance in terms of what they see in the market. I expect that we will do more of that next year to provide some guidance to the organization in respect of what is leading practice. It is easy for Audit to say

this is leading practice, but I think we need to back that up with something as well and that is what we will be doing there.

GOVERNOR BROWN: Joe, may I ask you a question? What is a technology charge back?

MR. MARTINS: That is really the computer equipment that we use. It is telephone services, the computer equipment, and the space that we utilize on the servers. It is also the support that we get from the IT function. So IT is one of the units within Citizens that started first with a charge back, and I think overtime we will probably increase that to some other functions that provide a support function to the organization as well.

CHAIRMAN COCUY: So they allocate a certain amount of expenses?

MR. MARTINS: And they allocate a certain amount.

CHAIRMAN COCUY: Why would you anticipate that it is going to decrease by \$98,000, 50 percent?

MR. MARTINS: One of the reasons was that we used to use a server for our administrative system. And we changed it actually during this year to web based environment and we are not utilizing the support that we used to have in the upgrades of the local system. So the support and the space utilization has decreased and that is why I expect to have a smaller footprint from IT.

CHAIRMAN COCUY: I'm sure you checked with Kelly to make sure then? She is okay with that, right?

MR. MARTINS: It doesn't make it cheaper. I think you will find that that cost really goes into the operating expenses now. So it is just a move a couple of lines up, but it does make a change. Any other questions on the budget?

CHAIRMAN COCUY: I guess something that I am thinking about is depop. With the depopulation we are shrinking, but we are anticipating a five percent increase in our costs. How do we reconcile or justify that?

MR. MARTINS: I think what we don't see is that included in the cost that we have is staff that we provide and services which we provide on behalf of other organizations as well. One of them would be the staff member that we transferred to ICF. Originally the intention was that that member would be provided by finance, and the cost of that member would be served through finance. Given that we couldn't find the resource for that function, Audit is carrying that cost during the period of us providing the advisory or consulting out for the implementation of the ICF project. So that carries some of the extra costs that we probably would not have had to carry this year.

The last piece that I wanted to mention was on page 45. It is just a quick overview of the audit universe. And what we have done there is we also have color coded where we see and how we viewed as audit, how we view the risk within the organization, the specific universe areas. And there is a legend in there that shows low risk, medium risk and high and we basically use the standard methodology for the assessment of that which is the one that we utilize in identifying high, medium and low impact issues, and it is attached to every audit report that we produce. You will see, if you compare the yellow and the reds to the work that we are doing, most of the work that we are executing against would be against the areas that we have identified as medium or high risk for the organization.

That is really all I have in my presentation, sir. If there are no further questions on the plan, itself, I would like to request approval for the 2017 audit strategy and plan which includes the

2017 budget from the committee.

GOVERNOR HENDERSON: I notice on the classification of the employee base that, I guess maybe a little bit of bias on my part there, about the number of CPAs you have on staff. I know you have certified internal auditors and that it is a much respected designation. Is that just in terms of how the market goes or strategy or not? There are some amazing training that we and others pull out of the CPA firms that help so much on their perspective of audit and depth there; what are our feelings about that?

MR. MARTINS: I think when I look at the finance and accounting area, specifically towards the CPA, I personally agree with you in terms of the CPA qualification and the knowledge and experience that we get from that. It is the availability of the resources and the area of expertise that we are looking for. A large piece of the work that we are doing is in insurance and insurance operations, and in the IT area. And so from a CPA perspective I think we are well served if we have at least one strong qualified public accountant to help us with the finance and accounting work that we are doing. But we need to also bring in staff that are skilled in insurance operations and in IT, and those staff that we did bring in, although they may not have CPAs, they also don't have the CPCU. They have many years of experience in auditing in insurance environments and those were the staff that we could find that joined the organization. And so when we balance this out I think I agree with you that a CPA has a breadth of experience that they gather through the exposure that they get in being in one of the large accounting firms and the type of work that they do there, but it is not that easy to specifically find them all the time and we don't exclude that when we advertise. That is one of the titles that we put in there. We don't always look for CIAs, we are saying CPA or CIA or years of experience.

CHAIRMAN COCUY: Do you have a number of staff that are both CPA and CIAs?

MR. MARTINS: I have one CPA, and most of the staff are CIA.

CHAIRMAN COCUY: I think the other thing to note is great progress on becoming more of an advisory organization. I think that is really helpful to Citizens rather than just pure auditing and working towards a 50/50 goal. I think that is really good. And I also want to commend you on the progress of the internal control framework. I think we are making some headway there.

MR. MARTINS: Thank you, sir. The only item that is remaining is to approve the plan and the budget.

CHAIRMAN COCUY: Do we have a motion for the plan?

**GOVERNOR HENDERSON motioned to approve the Plan and Budget and Governor Brown seconded. All were in favor and the motion was accepted.**

CHAIRMAN COCUY: Thank you very much. Okay, we will move on now to item three of our agenda, the Chief Financial Officer report, Jennifer Montero, please.

MS. MONTERO: Good afternoon. If you will turn to tab three, and you have before you the financial statements for the period ending September 30th, 2016, along with the quarterly financial analysis the QFA, and a one page summary addressing litigated water claims. While depopulation activity and administrative expenses have appeared to stabilize, we continue to observe substantial period over period declines in written premium and upward trends in loss activity, particularly within the personal lines account. Direct written premium of \$768 million marks a decrease of 24 percent or \$237 million as compared to the same

period last year, primarily as a result of the absence of renewal business on policies depopulated in prior reporting periods. Depopulation activity as measured by ceded premium written decreased 80 percent or \$76 million. As of September 30th, 2015, a total of \$95 million of ceded premiums were reported. As of September 30th, 2016, only \$19 million of ceded premium was reported. The decrease in the depopulation activity is presumed to be driven by the depletion of the attractive policies in addition to trends and adverse loss experience on litigated water losses. Through September 30th, 2016, net premium earned a 506 million decrease, 19 percent or 122 million, as compared to a year ago. Net losses and loss adjustment expense, LAE, decreased nine percent or 33 million for the period ending September 30th, as compared to a year ago. However, over the same period the net loss in LAE ratio increased by eight percentage points on a combined basis. By account attritional loss in LAE ratios was 71 percent, 11 percent and 21 percent for the PLA, the CLA and the coastal accounts respectively. The PLA non-sinkhole, non-catastrophe results continue to deteriorate due to the number of claims entering litigation. Based on current trends the expectation within the PLA is that accident year 2016, will ultimately have close to 50 percent of all non-sinkhole and non-catastrophe claims ending up in litigation. Assignment of benefit and representation at first notice of loss continue to be extremely strong indicators as to whether a claim will end up in litigation. With respect to hurricane losses, the ultimate losses in LAE related to Hurricane Hermine are projected to be about 4.5 million. Administrative and underwriting expenses of 114 million decreased approximately 14 percent, or 32 million relative to the same period a year ago. The expense ratio of 25 percent through the third quarter of 2016, remains flat as compared to the prior quarter, and an increase of three percent as compared to the year ago period. The three percent increase is largely the result of a decrease of \$237 million of direct written premium, outpacing the related decrease in underwriting and administrative expenses of \$32 million. However, year over year administrative expenses excluding underwriting expenses decreased by \$7 million through September 30th. In response to the decrease in premium base, the expense ratio is two percent below the budget estimated of 27 percent and is anticipated to remain flat at 25 percent across the remainder of the calendar year 2016. Policyholder surplus increased by \$109 million over the nine months ended September 30th. Policies in force of 491,779 at September 30th, 2016, reflects a decrease of 14,000 or 82,308 policies as compared to September 2015. However, policies in force have increased since January 2016, by 223 policies. The policies serviced, which includes both policies in force and policies that have been assumed but have not been renewed by their respective take-out carriers decreased by 25 percent or 170,471 policies over the same period. And if there are no questions that concludes my report.

CHAIRMAN COCUY: Just to clarify, for the numbers, they are in millions, right?

MS. MONTERO: Yes.

CHAIRMAN COCUY: The policy data is the actual numbers?

MS. MONTERO: Yes, that is correct.

CHAIRMAN COCUY: And this report and the one that is on page 2 is for nine months ended?

MS. MONTERO: Yes, September 30th.

CHAIRMAN COCUY: Okay. Any questions?

GOVERNOR HENDERSON: Thank you, Jennifer, just a note, I know the Board meeting tomorrow and comments on personal lines are definitely under stress.

MS. MONTERO: Yes.

GOVERNOR HENDERSON: We have been told several times we are aware of that, but it is proof in the pudding, if you will. So obviously the attention to the rate changes to try to deal with a smaller population and really some tough accounts, too, and obviously water. Good report.

CHAIRMAN COCUY: Okay, moving on to the report of the external auditors, the audit plan for 2016, the gentlemen from Dixon Hughes, welcome.

MR. CHURCH: Thank you for having us today, as always. I am Matt Church, the lead engagement partner on the audit of Citizens and the audit of FMAP and with me is Brian Smith, who is the senior manager on both of those entities. You should have in your materials the audit plan. We will go through it relatively quickly and we will get to a timeline and that will sort of explain where we are in the process. I will go through engagement scope and then I will hand it over to Brian to talk about our audit process and also the significant risk areas based on sort of the 9-30 numbers and where we are and we will update that as we move through our interim work set. With that turn over to slide four, our engagement scope for the current year is to audit the financial statements of Citizens Property Insurance Corporation on both a statutory basis and a GAAP basis, the GAAP financial statement is on a GASB basis. So it is a governmental accounting which falls under GAAP. We will also audit the financial statements for the Florida Market Assistance Plan. If you flip to page 5, what you will get from that will be the independent auditor's reports on –

CHAIRMAN COCUY: The Florida Market Assistance Plan is on a GAAP basis for commercial?

MR. CHURCH: Yes, good point. So on page 5 we will issue independent audit reports for all three statements. We will issue the communication of those charts with governance report which is the SAS 114 letter. And last year the way we did that and I want to make sure that the committee is comfortable with this approach again, is we combine the two bases of accounting for Citizens in the one letter that had both statutory and GASB components and then we issued a separate letter for FMAP. It seemed to work well last year. I think that would be our preferred path this year as well versus having three separate letters. We will also issue the communication of internal control related matters which is the SAS 115 letter, an acknowledgment letter for the Florida OIR. This says we are aware of the provisions of the Florida Insurance Code, and a letter of qualifications that will be filed at the end of the audit and will be delivered with the audited financial statements and then any reporting requested by the Audit Committee thereto. So going over to slide six we will talk about where we are in the process. We started planning; because of some of the events in the September, October time frame we kind of deferred really planning until we got through some of that to kind of see where things were going to be. We started our interim field work in Tallahassee this past Monday, so yesterday, so we will be there this week and then next week as needed, the team will be there. And predominantly working on controls, walk-throughs, things of that nature, looking at reinsurance contracts that have been entered into during the year and we will do the bulk of our premium and claim testing on transactions that have happened year to date. Next week we will be in between Tallahassee and local. So back in the office trying to shut down accounting policy, things like that, and just wrapping up those interim procedures. We plan to begin our field work which we plan to be in Tallahassee for four weeks, April 3rd of '17, and that would run through 04/28 of '17. And then one thing that worked really well last year I think is we, as part of wrapping up and doing the financial reporting aspect we actually spent a couple of days in Tallahassee with the finance team working through any comments, changes, anything like that to the financial

statements. It seemed to work better than just scanning copies back and forth. So we will plan to probably do that again this year with an estimated completion date of May 15, 2017. Any questions on the timeline and where we are to date?

CHAIRMAN COCUY: So with that completion date will you report on the final on the June quarter? With Audit Committee Board meetings?

MR. CHURCH: Yes. And I will give it to Brian to talk about our audit approach.

MR. SMITH: Brian Smith, team manager with the engagement team. I will walk through the audit approach here starting on slide eight. On the left-hand side you will see a table that shows the key steps. This is really a highlight of the audit approach we put into place starting with the risk assessment which we started last week and are still in the process of completion. That is a tailored approach, not only looking at scoping accounts but also scoping inherent risk to accounts and disclosures. Next is working on understanding controls. The team is in the field this week working on that. Just a reminder, the scope of our audit is not to provide an opinion on controls, but to obtain and understand the controls for the purpose of scoping our risk to engagement. The third bullet point that you will see is audit areas of focus. These are really the more significant areas that we are going to spend most of our time in. These are areas of more management estimates and assumptions. We will talk about those in a little bit more detail in a second. We will also look at significant transactions during the year, we will target those specifically and make sure we look at appropriate evaluation of accounting policy but also looking at the transactions to make sure we have evidence that supports those transactions. From there we will use audit technology, look at fraud risk assessments and also at the end of the report we will take all of our findings and conclusions and report back to the committee. So if you go on to the next couple of slides here, significant risk areas. Certainly stop me if you have questions on any of these, but these are areas we have scoped and made the assumption that these are areas that are significant to the company. The first one being IBNR. So you will see on the left-hand side the area of focus, the middle objective and then our response. The risk here is the amount of detail of assumptions and methods used by the actuaries in the IBNR calculation determination. To respond to this DHG has hired a third party actuary with Merlinos & Associates which we have engaged to work with Citizens' actuaries. The purpose of that is to challenge, understand and ultimately conclude with the actuaries that the IBNR method assumptions are appropriate. Also items we will look at is if there are certain areas of disaggregation that we need to consider due to AOB risk or due to catastrophe risk that may have occurred during the year. We will also look at testing the details that go into those calculations. So also getting into the claims and the reserves that support those IBNR case reserves. We will look through a look back analysis to see if there are any large losses that were paid after year end, pay analyze if we need to go back to the actuaries for consideration. We will also look at the range of the reserves to make sure that the range is consistent with prior years but also appropriate when applying materiality. Premiums is the next item. With any company there is a presumption of fraud risk with premium recognition. That applies here with Citizens as well. The risk we have looked at for premium recognition is really the risk of cut off and appropriate cancellation of premiums as they are canceled, make sure they are timely. We will target specific procedures to address that within our detail audit approach. Also recalculate premiums and also to target the procedures on take out policies. The next area is on the next page, page 11, or slide 11. This is investments. The risk with investments is valuation. The company has a large portfolio. We will use DHG's internal valuation specialist on a sample basis to go through and recalculate and take the valuation securities back to fair market value. We will also look at impairment if anything is necessary for that. We will confirm the portfolio with third parties, and also test purchase and sales of securities. The next item is reinsurance. The risk with reinsurance is really appropriate accounting policies. Reinsurance terms can have significant terms within those

agreements. We will read and evaluate those agreements, apply appropriate accounting policy, ultimately challenge the company's conclusion on reinsurance. Conclusions for accounting and risk transfer. We will also evaluate the appropriate holdings of those balances at the end of the year through confirmations to prove the existence, also admissibility under statutory accounting. And the last item on slide 12, this is management risk of override. Every company has a risk of management override controls. To target that risk we will evaluate significant assumptions and estimates. We will also look at journal entry testing to analyze specific fraud risk to the company and report back if we have any identified management override controls.

CHAIRMAN COCUY: So last year was obviously a learning curve. Specifically like in the area of IBNR, you probably learned a lot last year, you have got it all documented, you pretty much know our folks and their expertise. And how confident are you in what you have learned last year and the steps that we have now that those calculations and our processes are strong?

MR. SMITH: I think they are strong. I think you have a process in place that is consistent with the industry. When looking at IBNR it really starts from the bottom up, you want to make sure your data that is being provided to your actuaries is accurate from the start. That is really where the detail work comes in. We did not identify anything in the prior year that would say, well, maybe the data needs to be looked at differently. The challenge going forward is you have a new year, there is hurricane risks out there, and there is also AOB that is an issue, making sure that not only your actuaries, but the actuaries that you have hired are rethinking in the case of disaggregation that is used for that data. So to answer your question I think historically from last year they are strong but always open to challenge going forward.

CHAIRMAN COCUY: Okay, thanks.

MR. CHURCH: The last few slides that are included are really just bios of the engagement team, just so everybody has contact information for Brian, myself, concurring review partner and also the senior manager, over our IT testing. So if anybody has any specific questions to any of us, there is our contact information there. So with that we will take any questions that the committee may have.

GOVERNOR HENDERSON: What is the total hours of the engagement for the firm?

MR. SMITH: They are around 1,400 hours.

GOVERNOR BROWN: Brian, I have a quick question. You were talking about the key steps and I am just curious, you talked about understanding controls and I assume that if you find anything that in the area of controls or otherwise that if you have a question you would talk to Joe about it immediately, is that how that works?

MR. SMITH: Correct. And for our scopes so you understand, we will not provide an opinion on controls. If you were, say, an SEC filer under PCB rules you would be required to. Under the AICPA rules, we are not, however, we are required to understand those controls. So there is two ways you could come about a control deficiency. One would be going in and looking at the controls in place and identifying that there is a gap in the control or maybe a control was written to be performed this way and we go through and do a walk through and it is just not functioning the way it should. The other way is if we find an error within our system testing, there is always the question that should there have been a control deficiency if we find in this statement. So either of those situations we would go back to not only the company, because they are the owner of the control, but also evaluate it with Joe's team.

GOVERNOR BROWN: Super, thank you.

CHAIRMAN COCUY: And obviously, if you find areas for improvement you will report those in the management letter to us, correct?

MR. SMITH: Correct, correct.

CHAIRMAN COCUY: All right. Any other questions from the committee?

GOVERNOR HENDERSON: None here, thank you.

GOVERNOR BROWN: Thank you.

CHAIRMAN COCUY: Thank you, gentlemen. Item number five is, for information only, and other than that, that is the business that we have planned. Do we have any new business? Seeing none.

**GOVERNOR HENDERSON: Motion for adjournment, Governor Brown seconded, all in favor and the meeting adjourned.**

DRAFT