

June 24, 1980

SUBJECT: INSURANCE

WITHDRAWN

Circular Letter No. 6

TO: ALL DOMESTIC INSURERS

RE: CONTROL OF BOND PURCHASES AND SALES

The Department has become aware of a method of securities trading which has the effect of deferring or avoiding capital losses and overstating the value of the bond portfolio. It involves the purchase and sale of bonds at prices in excess of actual market values and is accomplished by means of the use of fictitious brokers advices which set forth such excess prices. The practice is known as "overtrading" or "parking a loss".

The Board of Directors of an insurer has a grave obligation to exercise more than ordinary care in the discharge of its investment function. It follows, therefore, that there is a duty to actively oversee the performance of those to whom the task of effectuating purchases and sales of securities has been delegated.

It is requested that each domestic insurer institute formal procedures to assure that the purchase and sale of securities are adequately monitored. Such procedures should consist of the following:

1. A procedure to test the validity of market values at which purchases and sales are negotiated, including the use of recognized securities rating organizations in instances where market values are difficult to obtain.
2. A review of the purchases and sales of bonds, in terms of the volume negotiated through various brokers.
3. The inclusion of this area in the scope of the audit by the Certified Public Accounting firm retained by the insurer.
4. The inclusion of this area in the program of the internal audits of the insurer.
5. The preparation of a clear and concise format for the report in which securities transactions are presented to the Board of Directors. Such format should include the yield to maturity of bonds purchased or sold.
6. The preparation and distribution to appropriate personnel, of a list of securities dealers approved by the Board of Directors.
7. The preparation for the Board of Directors of a periodic listing of the amount of commissions paid to individual securities dealers.

Kindly acknowledge receipt of this letter to:

Mr. George L. Gould,  
Chief-Examinations Bureau  
New York State Insurance Department  
2 World Trade Center  
New York, NY 10047

Very truly yours,

[SIGNATURE]

ALBERT B. LEWIS

Superintendent of Insurance