

**LIFE INSURANCE COMPANY
OF ALABAMA**

INTERNAL AUDIT REPORT
AS OF DECEMBER 31, 2016



WILLIS BOATNER PUGH
CERTIFIED PUBLIC ACCOUNTANTS

**Internal Audit Report
Life Insurance Company of Alabama**

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**Internal Audit Report
Life Insurance Company of Alabama**

Listed below are the internal audit recommendations that were examined in the months of July through December. A summary of suggestions for improvement by control is included for your information. Management may wish to develop a letter of response to this report to detail how items are going to be implemented or that a change will not be placed into operation for a specific suggestion.

Controls tested	Observations by Risk		
	High	Medium	Low
1. Fixed Assets			X
2. Accounts Payable		X	
3. Cash Receipts		X	
4. Investments		X	
5. Company Name and Agent Search		X	
6. Company Website Search		X	
7. Travel and Entertainment		X	
8. New Policies	X		
9. Board of Directors' Minutes			X
10. Payroll		X	

The report includes our findings, suggestions for improvement and assessed level of risk. Below is the criteria used for the assessment of risk.

Assessment of Risk:

High (H) – Significant impact to the Company. Individually or aggregately material in terms of financial impact, external compliance violation, adverse publicity, significant or pervasive weakness in control environment, significant inefficiencies, etc.

Medium (M) – Moderate in terms of impact to the Company. Individual instance or an aggregate of low risk items considered moderate terms of financial impact, compliance violation, adverse publicity, weakness in control environment, efficiency, etc.

Low (L) – Low in terms of impact to the Company. Relatively immaterial in terms of financial impact, no external compliance violation, little adverse publicity, minor inefficiencies, etc.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Fixed Assets**

Observations by Risk		
H	M	L
		X

Background:

This test was an assessment of the internal controls related to fixed assets. It was included in the internal audit plan due to the importance of having proper capitalization or expensing procedures.

Scope and Approach:

Our evaluation included the following procedures related to fixed assets of the Company:

- Developed an understanding of the processes and controls in place for fixed assets by obtaining the Company's capitalization policy.
- Evaluated the accuracy and completeness of expenses incurred during 2016 as they related to fixed assets or repairs and maintenance and verified they were in compliance with the Company's policy. Evaluated the assets added to the fixed asset detail as being properly capitalized and that asset lives were in compliance with the Company's capitalization policy.
- Verified that the subsidiary ledger of fixed assets agreed to the general ledger.

Key Highlights:

- For the 2016 expenditures described above, no observations were noted.
- For the verification of the subsidiary ledger to the fixed asset schedule for the third and fourth quarter, no observations were noted.

Suggestions for Improvement or Observations Noted:

- During 2016 testing, we noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Accounts Payable**

Observations by Risk		
H	M	L
	X	

Background:

Accounts payable is a critical portion of the Company's financial records and can be subject to fraud without careful reconciliation and oversight. This test was an assessment of the internal controls related to accounts payable. It was included in the internal audit plan due to the importance of having proper controls over expenses incurred by the Company and proper payment and review procedures.

Scope and Approach:

Our evaluation included the following procedures related to the accounts payable of the Company:

- Developed an understanding of the processes and controls in place for accounts payable by obtaining the Company's cash disbursement policy. Developed an understanding of each key control the Company has over cash disbursements.
- Obtained a detail of all disbursements from account 112200 for the last six months of the 2016 year and sorted the detail by check type. Randomly selected 30 checks from each type of disbursement: general accounts payable expenses, LSP and HCP expenses to test for proper key control compliance.
- From the sample selected, each significant control area for general accounts payable was tested for proper compliance with the policy. Controls tested were as follows:
 - Two staff members approved the invoice.
 - Checks were filed in the electronic system with all required documentation to support the expense.
 - Checks were properly posted to the general ledger and general ledger account selected appeared to be appropriate.
 - Check amount posted to the general ledger agreed to the electronic system scanned file.
- From the sample selected, each significant control area for LSP disbursements was tested for proper compliance with the policy. Controls tested were as follows:
 - Approval of payment was noted.
 - Checks were filed in the electronic system with all required documentation to support the expense.
 - Checks were properly posted to the general ledger and general ledger account selected appeared to be appropriate.
 - Check amount posted to the general ledger agreed to the electronic system scanned file.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Accounts Payable - Continued**

Observations by Risk		
H	M	L
	X	

- From the sample selected, each significant control area for HCP disbursements was tested for proper compliance with the policy. Controls tested were as follows:
 - Check copy was located in the electronic system.
 - Documentation was in the electronic policy folder stating why there was a reimbursement and medical reports, if necessary, were included.
 - Payment was approved and agreed to policy application

Key Highlights:

- For the sample of general expenditures, LSP expenditures and HCP expenditures selected for the last six months of the 2016 year, no observations were noted.

Suggestions for Improvement or Observations Noted:

- During the last six months of the 2016 year testing, we noted no additional suggestions for improvements or observations.

Suggestions for Improvement or Observations Noted in Previous reports:

- During the third and fourth quarters of 2016 testing, we noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Cash Receipts**

Observations by Risk		
H	M	L
	X	

Background:

This test was an assessment of the internal controls related to accounts receivable/cash collections. It was included in the internal audit plan due to the importance of having proper controls over receipts that are deposited or mailed to the Company.

Scope and Approach:

Our evaluation included the following procedures related to cash receipts of the Company:

- Developed an understanding of the processes and controls in place for cash receipt by obtaining the Company's cash receipt policy. Developed an understanding of each key control the Company has over cash receipts.
- Obtained a detail of all receipts in account 112100 for the 2016 year. Randomly selected 60 receipts to test for proper key control compliance. The sample included both ACH and check deposits.
- From the sample selected, each significant control area for cash receipts was tested for proper compliance with the policy. Controls tested were as follows:
 - Deposit amount was agreed to supporting documentation and checks deposited were footed with a control tape.
 - Summary control slips were scanned for electronic filing, deposited into the bank account and recorded in the general ledger.
 - ACH and check deposit amounts were traced to clearing the bank statement.
 - For deposits that were only checks, checks were footed to the deposit total.
- Reviewed two months bank reconciliations for proper reconciliation and review.
- One day's deposit detail was received that listed each policy holders account number and amount paid. This detail was footed and agreed back to the deposited amount. Each policy holder's payment was traced to being properly applied to their account balance in the general ledger system.

Key Highlights:

- For the sample of cash receipts selected for the 2016 year, no observations were noted.
- During the review of the bank reconciliations there were no observations noted.
- During the testing of one day's deposit detail there were no observations noted.

Suggestions for Improvement or Observations Noted:

- During 2016 testing, we noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Investments**

Observations by Risk		
H	M	L
	X	

Background:

This test was an assessment of the internal controls related to investments. It was included in the internal audit plan due to the importance of having proper investment policies and procedures due to the value of the Company's balances.

Scope and Approach:

Our evaluation included the following procedures related to investments of the Company:

- Developed an understanding of the processes and controls in place for investments by obtaining the Company's investment policy.
- Agreed each month's postings from the brokerage statement activity to the general ledger from July 2016 to December 2016 and suggested any journal entries as necessary.

Key Highlights:

- There were no significant differences between the investment statements and the posting in the general ledger for the period from July 2016 until December 2016. Any monthly differences were timing differences that cleared the next month.

Suggestions for Improvement or Observations Noted:

- During the third and fourth quarters of 2016 testing, we noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Company Name and Agent Search**

Observations by Risk		
H	M	L
	X	

Background:

This test was included as an internal audit step to research no individual or company has filed for a name similar to Life Insurance Company of Alabama.

Key Highlights:

- Life Insurance Company of Alabama was registered in the following states:
 - Alabama - Lynn *Loer* listed as the registered agent
 - Georgia - Samuel Pierce, Jr. listed as registered agent, Clarence Daugette, III listed as CEO
 - Tennessee - No agent listed, dissolved; inactive
 - Arkansas - No agent listed
 - Florida - Steven Keck and Lynn Lowe listed as officers, Clarence Daugette, III listed as CEO
- Life Insurance Co. of Alabama was registered in the following state:
 - Alabama - J S Holleman listed as the incorporator.
- Alabama Life Insurance Company was registered in the following state:
 - Alabama - A L Welch listed as the registered agent, dissolved 2001
- LICOA Brokerage Services, Inc. was registered in the following state:
 - Alabama - Raymond Renfrow, Jr. listed as the registered agent.
- LICOA Employee Benefits, Inc.
 - Mississippi – Billy West listed as the registered agent, dissolved.
- LICOA, Inc.
 - Oklahoma - Kent Frates listed as the agent
- LICOA National, Inc.
 - Kentucky - Robert H. Davis listed as the incorporator, Inactive.

Suggestions for Improvement or Observations Noted:

- The audit committee or board should review the above list and determine if any additional inquires need to be made.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Company Website Search**

Observations by Risk		
H	M	L
	X	

Background:

This test was included as an internal audit step to research the domain name LICOA.com.

Key Highlights:

- The following was found during the search for the name LICOA.com:
 - Registrar: Wild West Domains, LLC
 - Registrant Name:
 - Server: whois.wildwestdomains.com
 - Registrant Organization: Life Insurance Company of Alabama
 - Registrant Email: jcasey@licoa.com
 - Admin: Clarence Daugette
 - Admin Organization: Life Insurance Company of Alabama
 - Tech Name: Clarence Daugette
 - Tech Organization: Life Insurance Company of Alabama
 - Tech email: jcasey@licoa.com
 - Expiration date: July 23, 2017
 - On the website www.whois.wildwestdomains.com Jeff Casey is listed as owner of the website

- Extensible Provisioning Protocol (EPP) domain status codes, indicate the status of a domain name registration. A particular domain may have more than one status code, but must have at least one. The status codes for the Company's domain, which were set by the domain's registrar are as follows:
 - clientTransferProhibited - This status code tells your domain's registry to reject requests to transfer the domain from your current registrar to another. If you do want to transfer your domain, you must first contact your registrar and request that they remove this status.
 - clientUpdateProhibited - This status code tells your domain's registry to reject requests to update the domain
 - clientRenewProhibited - This status code tells your domain's registry to reject requests to renew your domain. It is an uncommon status that is usually enacted during legal disputes or when your domain is subject to deletion.
 - clientDeleteProhibited - This status code tells your domain's registry to reject requests to delete the domain, name registration, which can prevent unauthorized deletions resulting from hijacking and/or fraud.

Suggestions for Improvement or Observations Noted:

We noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Travel and Entertainment Policy**

Observations by Risk		
H	M	L
X		

Background:

This test was an assessment of the internal controls related to travel and entertainment. It was included in the internal audit plan due to the importance of having proper controls over the Company's travel and entertainment expenses. This risk for this control is considered high because of the external compliance violations that could occur with the IRS and adverse publicity if the policy is not followed properly.

Scope and Approach:

Our evaluation included the following procedures related to the travel and entertainment policy of the Company:

- Developed an understanding of the processes and controls in place for travel and entertainment by obtaining the Company's Travel & Business Expense Reimbursement Policy.
- Obtained a detail of all disbursements from accounts 185-Travel, 818-Entertainment, 817-Meals and 816-Lodging for July 2016 to December 2016. All expenses posted to these accounts were tested for the following:
 - The expense was submitted for reimbursement no later than 30 days following the completion of a trip.
 - Overall documentation of the expense included names and identity of the individuals present, the business purpose, name and location of where the expense took place, exact amount and date of the expense and receipts for all expenditures
 - Mileage or gas reimbursement should include date and purpose of trip, location traveled to and from, mileage and receipts.
 - Meal reimbursement should include name and identity of individuals present, business purpose, name and location of where the meal took place, receipt and date of the expense.
 - Miscellaneous expense reimbursement should include a copy of the receipt, names and identity of individuals present, business purpose and type of expense.
 - An expense report should be submitted by each employee requesting reimbursement and the report should be reviewed and approved.
 - The expense was reviewed for the correct account charged and the expense appeared appropriate.

**Internal Audit Report
Life Insurance Company of Alabama**

Travel and Entertainment Policy (Continued)

Observations by Risk		
H	M	L
X		

Key Highlights:

- There were meal expenses without detailed receipts. Per Company policy, detailed receipts are required for all meal and entertainment expenses in excess of \$25.00. This policy is rarely followed.
- IRS guidelines state that golf outings must be directly before or after a business discussion that includes at least one potential or current business contact not associated with LICOA. One exception is that of Conferences in which golf is an included activity of the conference. Golf outings during LICOA sponsored trips are not considered business expenses and should be reimbursed by the employee.
- Some expenses listed under meals or entertainment upon closer inspection were actually personal items. These are personal expenses and should be reimbursed by the employee.

Suggestions for Improvement or Observations Noted:

- Evaluate the threshold of required detailed receipts for meals and action when a detailed receipt is not presented.
- Expenses should be more closely monitored by someone other than the employee upon submission as a business expense.
- Entertainment expenses should follow the IRS guidelines for proper business expense; otherwise they need to be reimbursed by the employee.

Additional Notes:

- It was also noted that some Regional Directors were not clearly operating within company policies in relation to company paid meals. It was noted the home office was aware of this and taking steps to reiterate the company policy when needed in a timely matter.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
New Policies or Changes to Policies Testing**

Observations by Risk		
H	M	L
	X	

Background:

This test was an assessment of the internal controls related to new or changed insurance policies. It was included in the internal audit plan due to the importance of proper documentation and set up of insurance policies.

Scope and Approach:

Our evaluation included the following procedures related to new or changes to insurance policies of the Company:

- Developed an understanding of the processes and controls in place for insurance policies.
- Developed an understanding of the different types of policies and changes
- Randomly selected one month to test new or changes to policies.

Key Highlights:

- Randomly selected the month of November 2016 to test certain insurance policies. The following types and number of policies were tested for the month of November 2016.
 - Policies issued and paid - 30 policies tested
 - Application was included in the file
 - Any changes in the policy between completing the application and the policy becoming effective was in the file, if necessary.
 - The face amount of life insurance policies agreed between the application and what was recorded.
 - Commission was properly set up for the agent(s).
 - Medical records or other types of verification was included in the file, if necessary.

Suggestions for Improvement or Observations Noted:

- During the month of November 2016, we noted no additional suggestions for improvements or observations. There were no exceptions noted during our testing.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Board of Directors' Minutes Review**

Observations by Risk		
H	M	L
		X

Background:

This test was a review of the minutes from the quarterly Board of Directors meetings. It was included in the internal audit plan due to the importance these meetings as well as the proper documentation of them.

Scope and Approach:

Our evaluation included reviewing the minutes from the quarterly Board of Directors' meetings.

Suggestions for Improvement or Observations Noted:

- During the 2016 review, we noted no additional suggestions for improvements or observations.

**Internal Audit Report
Life Insurance Company of Alabama**

**Internal Audit Summary Report
Payroll**

Observations by Risk		
H	M	L
	X	

Background:

This test was an assessment of the internal controls related to payroll. It was included in the internal audit plan due to the importance of having proper payroll policies and procedures. This is an area that can be subject to external audits from federal, state or local agencies.

Scope and Approach:

Our evaluation included the following procedures related to payroll of the Company:

- Developed an understanding of the processes and controls in place for payroll.
- Received a list of all employees employed as of November 2016 and selected 30 employees for testing (not selecting employees from previous reports testing).
- The following items were tested in the employee files for the 30 employees selected:
 - Salary was approved in the employee file or minutes
 - Employee evaluations were in the file, if required
 - An I-9 form was completed if the employee was hired after the date required
 - A copy of the employee's driver's license was in the file, if required
 - A copy of the employee's social security card was in the file, if required
 - A signed confidentiality agreement was in the file.
 - An application was in the file
 - E-verify was completed if the employee was hired after the requirement date
 - A new hire form was completed if hired after the requirement date
 - A form A-4 and W-4 was completed
- The following items were tested for the month of November 2016 payroll for the 30 employees selected:
 - The gross amount paid agreed to the approved payroll amount in the employee file
 - A time sheet was completed, signed by the employee, approved and hours agreed to the gross amount paid, if required
 - Any sick time or vacation time included in the payroll was approved
 - The total amount paid for the month of November 2016 agreed to the amount posted in the general ledger for November 2016
- The total amount paid, net of withholdings, in November was traced to the December bank statements as properly clearing the bank account.
- For the payroll dated November 30, 2016, the following items were recalculated for the 30 employees selected:
 - FICA
 - City of Gadsden withholding
 - 401(k) withholding amount

**Internal Audit Report
Life Insurance Company of Alabama**

Internal Audit Summary Report

Observations by Risk		
H	M	L
	X	

Payroll – Continued

- Obtained a detail of the accrued sick leave hours as well as the hourly rates of the corresponding employees.
- Attempted to obtain a detail of the sick leave taken by company executives over the last three years.

Key Highlights:

- There were no exceptions noted during the testing of the employee files.
- There were no exceptions noted while testing the month of November 2016 payroll.
- There were no exceptions noted while recalculating the tax returns examined.
- There were no exceptions noted while agreeing the net amount paid for February to the bank statements.
- There were no exceptions noted during the recalculation of the FICA amounts withheld.
- There were no exceptions noted during the recalculation of the City of Gadsden withholding.
- There were no exceptions noted during the recalculation of the 401(k) withholding amounts.
- The company has an accrued sick leave of approximately \$1.1 million, but no liability on the company's books.
- Per investigation, it was revealed that executives are not required to use personal time off, but they continue to accrue this time.

Suggestions for Improvement or Observations Noted:

- The company should develop a policy placing realistic limits on the amount of sick (personal) time that an employee may accrue.
- The company should develop a policy addressing the issue of accrued sick (personal) time for executives.
- A liability needs to be set up for the accrued sick (personal) leave.
- At the time of testing ideas were being considered to modify the current policies, but no final decisions had been made.

**Internal Audit Report
Life Insurance Company of Alabama**

Summary of Suggestions for Improvements

Fixed Assets

- During 2016 testing, we noted no additional suggestions for improvements or observations.

Accounts Payable

- During the third and fourth quarters of 2016 testing, we noted no additional suggestions for improvements or observations.

Cash Receipts

- During 2016 testing, we noted no additional suggestions for improvements or observations.

Investments

- During the third and fourth quarters of 2016 testing, we noted no additional suggestions for improvements or observations.

Company Name and Agent Search

- The audit committee or board should review the list and determine if any additional inquiries need to be made.

Company Website Search

- During 2016 testing, we noted no additional suggestions for improvements or observations.

Travel and Entertainment

- Evaluate the threshold of required detailed receipts for meals and action when a detailed receipt is not presented.
- Expenses should be more closely monitored by someone other than the employee upon submission as a business expense.
- Entertainment expenses should follow the IRS guidelines for proper business expense; otherwise they need to be reimbursed by the employee.

New Policies

- During the month of November 2016, we noted no additional suggestions for improvements or observations. There were no exceptions noted during our testing.

Board of Directors' Minutes

- During 2016 testing, we noted no additional suggestions for improvements or observations.

Payroll

- The company should develop a policy placing realistic limits on the amount of sick (personal) time that an employee may accrue.
- The company should develop a policy addressing the issue of accrued sick (personal) time for executives.
- A liability needs to be set up for the accrued sick (personal) leave.
- At the time of testing ideas were being considered to modify the current policies, but no final decisions had been made.