



# STATE OF NORTH CAROLINA

**SPECIAL REVIEW**

**NORTH CAROLINA DEPARTMENT OF INSURANCE  
REGULATORY ACTIONS DIVISION (RAD) TRUST**

**RALEIGH, NORTH CAROLINA**

**SEPTEMBER 2005**

**OFFICE OF THE STATE AUDITOR**

**LESLIE W. MERRITT, JR., CPA, CFP**

**STATE AUDITOR**

**SPECIAL REVIEW**

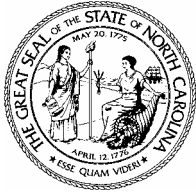
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STATE OF NORTH CAROLINA  
Office of the State Auditor

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**LETTER OF TRANSMITTAL**

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September 19, 2005

The Honorable Michael F. Easley, Governor  
Members of the North Carolina General Assembly

Ladies and Gentlemen:

Pursuant to General Statute §147-64.6(c)(16), we have completed our special review into allegations concerning the Department of Insurance and the Regulatory Actions Division (RAD) Trust. The results of our review, along with recommendations for corrective actions, are contained in this report.

General Statute §147-64.6(c)(12) requires the State Auditor to provide the Governor, the Attorney General, and other appropriate officials with written notice of apparent instances of violations of penal statutes or apparent instances of malfeasance, misfeasance, or nonfeasance by an officer or employee. In accordance with that mandate, and our standard operating practice, we are providing copies of this report to the Governor, the Attorney General and other appropriate officials.

Respectfully submitted,

*Leslie W. Merritt, Jr.*

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor



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## **INTRODUCTION**

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The Office of the State Auditor received allegations that Department of Insurance (DOI) personnel and Regulatory Actions Division (RAD) Trust management mismanaged the assets of London Pacific Life & Annuity Company, an insurance company in receivership due to financial problems. Allegations included the improper disposal of assets, unnecessary purchases, wasteful expenditures, and lack of required reporting to the Wake County Superior Court. In addition, the Department of Insurance received similar allegations in June 2004. In a letter to the Office of the State Auditor dated June 23, 2004, the Commissioner of Insurance wrote, “we do not believe that any of the allegations in the letter are true.” However, DOI conducted an internal investigation of the allegations. On November 26, 2004, the DOI general counsel drafted a letter to the Commissioner of Insurance summarizing the results of the internal investigation. On March 17, 2005, the Commissioner of Insurance wrote a letter requesting that the State Auditor undertake an audit to answer unresolved allegations that warrant a review by an independent outside auditor. In April 2005, our office began a special review of the allegations. Additional issues arose during the course of the special review.

To conduct this review, we performed the following procedures:

- Interviews with employees of DOI, RAD Trust, and London Pacific;
- Examination of relevant documents and records of DOI, RAD Trust, London Pacific, and other companies in receivership (estates) including review of invoices, travel reimbursement forms, check registers, bank statements, purchase orders, and asset listings;
- Review of policies and procedures;
- Interviews with individuals external to DOI, RAD Trust, and the companies in receivership;
- Examination of documents from the DOI internal investigation.

This report presents the results of our special review. The review was conducted pursuant to General Statute § 147-64.6(c)(16) rather than as a financial audit. The Department of Insurance is subject to financial audit procedures within the Office of the State Auditor’s audit of the State’s Comprehensive Annual Financial Report. An independent public accounting firm conducts annual cash receipts and disbursements audits of RAD Trust, London Pacific, and other companies in receivership.



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## BACKGROUND

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The Commissioner of Insurance is responsible for overseeing the financial solvency of all insurance companies operating within the State of North Carolina. When DOI financial analysts and financial examiners discover that a company domiciled<sup>1</sup> in North Carolina is becoming insolvent, the Commissioner is empowered by North Carolina General Statute (NCGS) §58-30 to place the company into receivership. Once a company enters receivership, the Commissioner is vested authority of the company, the Commissioner makes all management decisions (including employment decisions, entering contracts or authorizing loans) and controls all the assets. DOI attempts to rehabilitate the company's financial viability to enable it to continue business or liquidate the company by selling its insurance policies and assets to another insurance company. In all receiverships, the goal of the Commissioner is to protect the policyholders of the company and attempt to ensure that policyholders and creditors receive as much of the residual funds as possible. This responsibility for companies in receivership exists in all 50 states, although each state's operations and methods for handling companies in receivership may differ.

As more companies became insolvent in the early 1990's, DOI received approval from the Wake County Superior Court (via court order on June 22, 1992) to maintain a centralized bank account through which operations of all companies in receivership could maintain deposits and use those deposits to pay obligations. Afterward, DOI realized that management of companies in receivership could more economically be managed through the creation of a trust to oversee the operations.

On July 5, 1995, a court order ("Declaration of Trust for the Regulatory Actions Divisions Group Master Trust") of the Wake County Superior Court created RAD Trust. The trust document named the Commissioner of Insurance, "in his official capacity," as grantor of companies in receivership (estates) and outlined the powers, duties, and responsibilities of the Commissioner for these estates. The Commissioner was to designate a Special Deputy Commissioner as trustee of the estates. The declaration of trust enumerated responsibilities of the grantor as follows:

- a. Take possession of assets of the companies in receivership and administer them under the general supervision of the Superior Court of Wake County;
- b. Provide accountings to the Superior Court of Wake County;
- c. Deposit in one or more bank accounts amounts required for meeting current administrative expenses and dividends for the companies in receivership;

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<sup>1</sup> An insurance company's domiciled state is the state in which the insurer is incorporated or organized.

## **BACKGROUND (CONTINUED)**

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- d. Charge the costs for administering the estates against the assets of the insurers or against the deposits made.

Further, the trust document gave the Commissioner of Insurance power to create one centralized operational bank account, obtain a lease for office and storage space for the administration of the estates, and purchase supplies, equipment and furnishings to carry out the responsibilities and allocate those costs to the estates based on their usage. The trustee was required to perform functions for the estates in accordance with General Statutes and “pursuant to standards of ethical behavior and professional conduct applicable to employees and officers of the State of North Carolina.” Functions of the trustee noted in the trust document include:

- Creation of a centralized operational bank account;
- Provision of payroll accounting services;
- Employment of personnel and independent contractors to assist in administering the companies in receivership;
- Leasing office space, storage space, and equipment to administer the estates;
- Purchasing supplies, equipment, and furnishings for the administration of the estates;
- Obtaining or providing printing, shipping, copier, facsimile, and other services for the companies in receivership;
- Management and allocation of employees’ and independent contractors’ travel and other expenses incurred for services to the estates;
- Advertising for, processing, and paying claims against the companies in receivership.

Subject to control of the Commissioner of Insurance, the trustee also maintained powers to acquire and retain investments, sell or dispose of estate property, manage property of the companies, borrow or lend money on behalf of the estates, employ advisors, and purchase insurance coverage. If the trustee was removed by the Commissioner of Insurance or resigned, the successor trustee “shall be a Deputy Commissioner of Insurance and an employee of the Insurance Department of the State of North Carolina.”

## **BACKGROUND (CONTINUED)**

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### **Funding:**

RAD Trust operates on deposits received from the estates. RAD Trust does not receive appropriations from the State; however, the salaries and benefits of DOI personnel overseeing the estates are fully funded by state appropriations. When a company enters receivership, RAD Trust places a designated amount into the RAD Trust bank account to cover its expenses as well as those of the estates. As of June 30, 2005, RAD Trust managed seven insurance companies through deposits on hand as noted in the table below:

<b>DEPOSITS ON HAND FROM COMPANIES IN RECEIVERSHIP AS OF JUNE 30, 2005</b>	
London Pacific Life & Annuity Company	\$294,000
Commercial Casualty Insurance Company of North Carolina	73,000
The Investment Life Insurance Company of America	5,000
Twentieth-Century Life Insurance Company	13,000
Nationwide Truckers Association Self Insurers Fund of North Carolina	5,000
State Capital Insurance Company	5,000
National Workers Compensation Fund of North Carolina	5,000
Total	\$400,000
Source: RAD Trust	

RAD Trust expends funds to operate these companies as well as to maintain its own operations. As such, typical expenses include rent, utilities, salaries and benefits, tax and audit services, consulting services, and purchase of assets. Each company continues to maintain its own checking account to pay policy benefits as well as some general expenses. Therefore, purchases for an individual company may either be paid directly through the estates' checking accounts or through the RAD Trust account. For all purchases for a specific estate made through the RAD Trust banking account, a monthly billing from RAD Trust to each estate is maintained. In addition, this billing includes a monthly charge of each estate's share of RAD Trust operating expenses. The billing is based on an established allocation method that is developed by RAD Trust each year.

### **Facilities:**

RAD Trust maintains administrative offices at 401 Glenwood Avenue near downtown Raleigh, North Carolina. Originally, DOI entered into a lease for the office space in this location in August 1993, prior to the creation of RAD Trust. At the time, the receivership operations occupied only a portion of the building. In March 1996, RAD Trust entered into a lease for the same building with the landlord. Over time, RAD Trust and DOI

## **BACKGROUND (CONCLUDED)**

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became the sole tenants of the building. RAD Trust remained the lessee while DOI paid RAD Trust for office space through a “services agreement.” Currently, RAD Trust maintains offices on the bottom floor of the building along with remaining employees of London Pacific. As of March 1, 2005, RAD Trust sub-leases the top two floors of the building to DOI staff that oversee estate operations or perform financial statement analysis of North Carolina licensed insurance entities.

### **Organizational Structure:**

The DOI Special Deputy Commissioner appointed as trustee is the executive officer of RAD Trust. In addition, the DOI Deputy Commissioner for Financial Analysis oversees RAD Trust financial operations while a DOI Financial Analyst acts as RAD Trust operations manager. RAD Trust employs individuals in the following positions: a controller, two accounting clerks, a research and accounting analyst, and a research assistant/legal analyst. These five positions are not state employees but are employees of the trust with separate salary and benefit plans. Other DOI employees assist with overseeing operations of the estates. Usually, a DOI employee acts as “examiner-in-charge” of the daily operations of an individual estate. In some instances, services of outside contractors are acquired to administer the operations of an estate as in the case of Commercial Casualty Insurance Company.

## FINDINGS AND RECOMMENDATIONS

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### 1. RAD TRUST HAS OPERATED OUTSIDE THE RULES AND REGULATIONS OF THE STATE EVEN THOUGH IT IS A FUNCTION AND RESPONSIBILITY OF THE COMMISSIONER OF INSURANCE.

RAD Trust was formally created by court order of the Wake County Superior Court on July 5, 1995. Since its creation, RAD Trust has operated as a non-state entity. As such, RAD Trust management has formulated its own rules, policies, and procedures rather than following state rules and regulations. For example, RAD Trust employs and terminates employees at will outside the State Personnel System. Further, RAD Trust created its own financial reporting systems. RAD Trust has received an annual cash receipts and disbursements audit rather than a full-scope audit including analysis of fixed assets and compliance with regulations.

RAD Trust operations are managed by State employees. The DOI Senior Deputy Commissioner oversees all operations, a DOI Deputy Commissioner is responsible for financial operations, and another DOI employee administers the day-to-day operations of the companies in receivership. Additionally, a DOI financial examiner usually oversees the individual companies in receivership as an “examiner-in-charge.” These DOI employees’ salaries are paid exclusively by the State with no reimbursement from either RAD Trust or the estates.

The trust document that created RAD Trust notes that the trustee (Senior Deputy Commissioner) shall carry out functions “*in a manner consistent with the provisions of Article 5 of Chapter 58 of the North Carolina General Statutes, the provisions of the Liquidation Act, the regulations of the North Carolina Department of Insurance, and pursuant to standards of ethical behavior and professional conduct applicable to employees and officers of the State of North Carolina.*” Further, the trust document gives complete control of all operations of the trust and the estates to the Commissioner of Insurance, “in his official capacity,” and his designee as “trustee.” In fact, the Commissioner actually is empowered to take possession of assets of the companies in receivership. In all respects, the Commissioner of Insurance and departmental employees managing, administering, and operating RAD Trust and the estates act in official capacities as State officials and employees and do not relinquish their titles, responsibilities, or duties as State employees and officials when working on trust and estate operations.

Further, the Office of the State Controller (OSC) in consultation with the Office of the State Auditor (OSA) determined that RAD Trust should be included within the North Carolina Comprehensive Annual Financial Report<sup>2</sup> (CAFR) as a “component unit.”<sup>3</sup>

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<sup>2</sup> Comprehensive Annual Financial Report is the State’s annual financial statement.

<sup>3</sup> “Component unit” is a legally separate entity for which the State is financially accountable. Financial accountability is based upon the ability of the State to impose its will on the entity.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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Literature from the Governmental Accounting Standards Board (GASB) provides guidelines for determining whether an entity should be considered a function and responsibility of the State for inclusion in the CAFR. RAD Trust qualified, at a minimum, as a component unit based upon: (1) possession of corporate powers including recognition by the IRS, ability to contract in its own name, and sue or be sued in its own name, and (2) the State's ability to impose its own will through the control of all aspects of the organization (both the trust and estates) including day-to-day operations and hiring and firing employees. Furthermore, the Department of Insurance has a fiduciary responsibility which classifies RAD Trust as a "private purpose trust fund."<sup>4</sup>

DOI and RAD Trust management said that RAD Trust and the estates are an entity separate from State government. Management repeatedly noted that the Commissioner of Insurance and his designees "wear a different hat" when handling trust and estate responsibilities. In a memo on the history and legal status of the entity, RAD Trust management said, "The Commissioner's legal capacities as regulator and as receiver are separate and distinct." However, RAD Trust management acknowledge that they do not surrender their status as State officials and employees when handling the RAD Trust function. Further, DOI and RAD Trust officials believe the operations should remain outside the auspices of State government due to establishment by court order, case law indicating that the State is not subject to legal action in cases against the insurer, and their belief that the intent of the original legislation was to keep the functions separate. However, in a letter to OSC and OSA, management agreed that, "the Commissioner holds legal title and possession of the insurer's assets for the beneficial owners of the property, the creditors and policyholders, subject to the supervision of the Court." Finally, DOI and RAD Trust management cited the ability to hire employees (whom have not been considered State employees), sign leases, obtain property, and execute contracts as well as the separate Federal Identification Number from the IRS, annual filings of separate income tax returns, and classification as a "Court Settlement Fund" for tax purposes.

In summary, the Commissioner of Insurance and DOI employees control all aspects of RAD Trust and estate operations, the Commissioner has ownership of estate assets, the Commissioner and his designees act in official capacities while overseeing the trust and estates, the trust document specifies that Department of Insurance regulations should be followed, and financial reporting standards recognize the State's ability to impose its will

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<sup>4</sup> GASB 34.72 and GASB Codification paragraph 1300.112 define "private purpose trust fund" as "all other trust arrangements under which principal and income benefit individuals, private organizations, or other governments."

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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on RAD Trust. Therefore in our opinion, RAD Trust should operate as a division of the Department of Insurance and should follow State rules and regulations in all aspects of its operations where practical.

### **RECOMMENDATION**

RAD Trust should comply with the trust document by following regulations of the Department of Insurance. As such, RAD Trust should follow State rules and regulations regarding purchasing, personnel, cash receipts and disbursements, contracting, and use of other governmental services.

#### **2. RAD TRUST DID NOT FILE QUARTERLY REPORTS FOR THE TRUST AS REQUIRED IN THE DECLARATION OF TRUST.**

The July 5, 1995, Declaration of Trust required the trustee to “furnish to Grantor and file with the Superior Court of Wake County, North Carolina, on a quarterly basis, accounts of receipts and disbursements of trust property.” Our review of the quarterly report filings revealed that RAD Trust filed quarterly reports for the individual estates but did not file quarterly reports for the trust itself until the quarter ended June 30, 2004. Therefore, RAD Trust did not comply with the terms of the Declaration of Trust. Management stated they did not understand that they had to file separately for RAD Trust because they had filed individual quarterly reports for each estate. However, the trust document states that filings of “trust property” are necessary, not just property of the estates.

### **RECOMMENDATION**

RAD Trust should comply with the terms of the July 7, 1995, Declaration of Trust. Management should continue filing quarterly reports for both RAD Trust and the individual estates.

#### **3. RAD TRUST MANAGEMENT DID NOT MAINTAIN ADEQUATE DOCUMENTATION FOR THE DISPOSAL OF ESTATE ASSETS.**

The original complainant alleged that RAD Trust management gave away, threw away, or sold serviceable computers, monitors, servers, and other computer components of London Pacific. RAD Trust management and staff as well as estate employees confirmed that computers, office furniture, and other items were disposed of through sales to estate employees, DOI employees, vendors, and other individuals and companies external to the



## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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trust and estates. RAD Trust management offered employees who were being terminated the option of purchasing the computer that they used. In addition, other computer items, furniture, equipment, and other items such as art were offered for sale to existing employees of RAD Trust and DOI employees overseeing the estate. RAD Trust management arbitrarily set prices with employees making offers and management either accepted, refused, or negotiated the amount offered.

NCGS §58-30-85(a)(7), (9) permits the Department of Insurance, in its role as either rehabilitator or liquidator of companies in receivership, to “conduct public and private sales of the property of the insurer” as long as the sales are “at its market value” and prices “are fair and reasonable.” However, there is no documentation to support that assets were sold at market values to ensure a fair and reasonable process.

RAD Trust purchased large amounts of computer equipment for the trust and London Pacific. Some of these purchases resulted in excess equipment that was also sold to employees and vendors. One particular sale appeared unusual. In August 2003, two excess servers were sold to a DOI employee working in the Financial Examinations Division. This employee operated a private business in his home and he purchased items to furnish his home office. However, due to estate employee complaints about outsiders purchasing items, this individual did not directly purchase the servers; rather, a London Pacific employee paid for the items and resold them to the individual. However, the amount paid to the estate was \$100 less than the amount London Pacific paid for the two servers. The London Pacific employee charged an installation fee for the servers and, instead of charging the person to whom the servers were sold, he shorted the estate by \$100. To remedy this shortfall, the former RAD Trust director paid the \$100 difference in December 2004.

RAD Trust management confirmed the sales and said that estate information technology systems were outdated and required upgrades. Management further stated the method of selling items to employees was used to improve employee morale as well as receive a higher sales price than prices received through prior auctions or from State Surplus Property. Interviews also indicated that sales of assets to employees had occurred with earlier estates including the Investment Life Insurance Company of America.

RAD Trust management does not take a physical inventory of fixed assets when taking over estate operations. Rather, RAD Trust relies on the company’s existing inventory and instead concentrates on securing the building to prevent theft. RAD Trust management stated that fixed asset values were inconsequential relative to the values of estate investments. As a result, management focused its efforts on investments rather than equipment. Current RAD Trust accounting policies adopted March 2005 require that “as soon as practicable after a receivership order is approved by the Court, fixed assets housed at an estate’s office location will be inventoried.” The May 2002 policies only required

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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inventory of estate assets “prior to the transfer of assets to the RAD Trust location.”

In addition, documentation supporting the sales was inadequate. After some of the initial sales, estate employees began preparing a list to attempt to identify all sales of assets and the proceeds received. However, RAD Trust was unable to verify whether all sales were documented since no inventory was taken and reconciled and some payments were made in cash. See Appendix A for a listing of assets sold that we were able to document. In addition, payments from some vendors may have been obscured through reductions on future invoices.

### **RECOMMENDATION**

RAD Trust should discontinue the practice of selling estate assets directly to employees. Management should pursue the feasibility of holding auctions or public sales to ensure that all persons have equal opportunity to purchase items and to maximize receipts. Further, the method for determining prices should be adequately documented. RAD Trust should establish procedures for taking an inventory of assets upon a company entering receivership, how sales of assets will be managed, and determining sales prices for disposition of assets. Finally, all sales of assets should be adequately documented.

#### **4. ASSETS OF THE ESTATES ARE CO-MINGLED WITH ASSETS OF RAD TRUST AND THE DEPARTMENT OF INSURANCE.**

We received an allegation that estate assets were transferred to either the Glenwood facility or the Dobbs building for use by DOI employees. Our observation of facilities, inquiry of employees, and review of fixed asset listings confirmed that estate assets were located throughout the Glenwood building and had been transferred to the Dobbs building at one point. Furniture and equipment of companies in receivership occupy space throughout the Glenwood facility. For example, the conference room table from the London Pacific board of directors is currently located in the 2<sup>nd</sup> floor conference room at Glenwood for use by RAD Trust, estate, and DOI employees, including those who do not work on estate operations. Further, DOI employees working on estate operations and employees performing financial analysis of other insurance companies utilize several laptop computers and desks purchased by estates. The inventory list properly notes who owns the assets and assets are tagged with stickers indicating which entity purchased the asset.

When the former Special Deputy Commissioner (who was the trustee) was relocated to the Dobbs building following his promotion within DOI, office furniture and computer equipment of estates were moved with him. Following the receipt of allegations, those items were subsequently returned to Glenwood. The prior director of RAD Trust and a former employee of London Pacific who was hired by DOI also admitted that they took their laptop computers with them to DOI until DOI provided them with computer equipment months later.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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There has been no reimbursement from RAD Trust or DOI to the estates for use of these assets through purchase or rental agreements. RAD Trust management said the shared use of furniture and equipment is more cost-effective for the various entities by sharing assets rather than each entity purchasing its own. Further, RAD Trust management believes that any DOI employee who performs any functions for estates may use equipment purchased with estate funds.

### **RECOMMENDATION**

DOI should provide its employees with necessary computers, office equipment, and furniture through the normal purchasing process. Estate operations should not be an alternative source for these items for DOI employees. Items not needed for estate operations should be sold at fair market values. If certain assets are needed for operations of estates, RAD Trust, and DOI, DOI should pay a rental amount of its fair share for the use of the items.

#### **5. EXCESSIVE PURCHASES OF COMPUTER ITEMS WERE MADE USING ESTATE AND RAD TRUST FUNDS.**

Our finding related to the disposition of assets (finding #3) noted that RAD Trust purchased new computer items to replace the assets sold to employees and vendors. We reviewed invoices, fixed asset listings, check registers, trial balances, and purchase orders for the period July 2002 through May 2005. During that time, London Pacific funds were used to purchase 17 servers, 23 printers, 17 monitors, eight personal computers, and three scanners. According to the London Pacific trial balance, \$200,688.86 in computer hardware and component purchases were made during this period. In addition, RAD Trust purchased nine servers, 23 printers, 11 monitors, 16 personal computers, and two scanners during the same period. Total RAD Trust expenses for computer purchases amounted to \$183,174.31 between July 2002 and May 2005.

RAD Trust management stated the purchases were necessary to upgrade London Pacific computer equipment to enable compatibility and connectivity between the London Pacific-Sacramento office, the London Pacific-Raleigh office, and RAD Trust facility at Glenwood Avenue. For example, one invoice included the notation, "Citrix server to handle DOI employees at LP."

The former RAD Trust director and a former London Pacific information technology employee acknowledged that excess computer equipment was purchased. In one instance, extra servers were purchased because RAD Trust was able to acquire servers at a low price on a "good deal." The excess equipment was kept in case existing equipment needed repair or replacement. When a vendor noticed the excess equipment, the items were sold to the vendor and other servers were sold to a former DOI employee. (See finding #3) As of June 2005, some excess equipment remains at the Glenwood location.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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For example, observation of the warehouse at the Glenwood facility revealed three London Pacific printers, seven RAD Trust printers, seven London Pacific monitors, four RAD Trust monitors, and one RAD Trust scanner in addition to other computer components.

In addition, some of the computer equipment purchased using estate funds was for DOI employees. Specifically, \$27,079.02 was spent to purchase laptop computers for the Senior Deputy Commissioner, the Deputy Commissioner for Financial Analysis, and other DOI employees overseeing estate operations. Also, personal digital assistants were purchased at a total cost of \$963.87 for the former Senior Deputy Commissioner, current Senior Deputy Commissioner, and current Deputy Commissioner for Financial Analysis. RAD Trust management said the laptops and personal digital assistants were purchased using estate funds due to their need for overseeing estate operations, specifically when traveling between RAD Trust offices and estate locations in other states. However, use of these items is not limited to their responsibilities for the estates.

### **RECOMMENDATION**

RAD Trust should adequately justify the purchase of all computer equipment. Large purchases of computer items for companies in receivership should be avoided except in extreme circumstances. In addition, DOI should furnish its employees computer equipment necessary to perform their jobs. Estates should not be charged (whether directly or indirectly through the monthly billings) for assets purchased for the long-term use of DOI employees. Any excess or surplus equipment should be sold for the benefit of the estates.

#### **6. RAD TRUST ENTERED INTO AN EXCLUSIVE BUSINESS RELATIONSHIP WITH ADVANTEC GLOBAL SERVICES, INC.**

In the fall of 2003, the London Pacific network administrator attended a training session on Citrix servers taught by the owner of Advantec Global Services, Inc. The employee was impressed with the knowledge and expertise of the instructor and informed his supervisor, the former RAD Trust director, of his impressions. After the final day of the training session, the London Pacific network administrator arranged for a meeting between the course instructor (owner of Advantec) and the former RAD Trust director. In the course of conversation, it was verbally agreed that Advantec could provide information technology services to RAD Trust and the estates. Advantec offered to set up a Citrix server for RAD Trust and provide technical support.

Advantec began providing technical support to RAD Trust and the estates in October 2003. During the initial stages of support, Advantec also sold software, hardware, and maintenance agreements to RAD Trust at competitive prices. Soon thereafter, the Advantec sales manager asked the former RAD Trust director to “sole source” Advantec

## FINDINGS AND RECOMMENDATIONS (CONTINUED)

for information technology products. The former RAD Trust director and the London Pacific network administrator said Advantec offered to sell equipment to RAD Trust or the estates at cost plus a five-percent markup. RAD Trust management agreed verbally to this offer though the former RAD Trust director said he also checked with other companies to ensure prices were competitive and occasionally purchased items from other vendors.

Our review of invoices from Advantec revealed no evidence of bids or quotes for any equipment purchased from Advantec. In fact, RAD Trust Purchase Order #3193 noted “Advantec is now our major supplier of networking equipment and management software. They also supply most of our network services.” During the period November 2003 through April 2005, RAD Trust and London Pacific paid the following amounts to Advantec for equipment, software, and services:

<b>ANALYSIS OF PAYMENTS TO ADVANTEC GLOBAL SERVICES, INC.</b>				
<b>YEAR</b>	<b>CATEGORY</b>	<b>RAD TRUST</b>	<b>LONDON PACIFIC</b>	<b>TOTAL</b>
2003	Equipment and maintenance agreements	\$38,591.34	\$12,515.80	\$51,107.14
	Software	8,320.85	22,588.05	30,908.90
	Services	62,297.06	66,806.32	129,103.38
	<b>Total</b>	<b>\$109,209.25</b>	<b>\$101,910.17</b>	<b>\$211,119.42</b>
2004	Equipment and maintenance agreements	35,869.12	1,495.48	37,364.60
	Software	7,608.09	3,314.06	10,922.15
	Services	201,550.94	19,520.01	221,070.95
	<b>Total</b>	<b>\$245,028.15</b>	<b>\$24,329.55</b>	<b>\$269,357.70</b>
2005	Equipment and maintenance agreements	281.71	0.00	281.71
	Software	0.00	0.00	0.00
	Services	30,917.47	0.00	30,917.47
	<b>Total</b>	<b>\$31,199.18</b>	<b>0.00</b>	<b>\$31,199.18</b>
	<b>GRAND TOTAL</b>	<b>\$385,436.58</b>	<b>\$126,239.72</b>	<b>\$511,676.30</b>

Source: Invoices, check registers, detailed vendor listings, analysis of payments

In addition, DOI purchased \$115,954.73 in equipment from Advantec during May and June 2004. Many of the above billings for services included reimbursement for employee meals and lodging without supporting receipts and meals were reimbursed at actual costs rather than a per-diem rate.

No written contract existed between Advantec and RAD Trust until March 2004 although Advantec began providing services and equipment in October 2003. The contract required that Advantec provide consulting services for a desktop support engineer for 40 hours per week at an agreed-upon rate of \$63.75 per hour. Prior to the contract, Advantec was providing these services at \$85 per hour. Billings subsequent to the contract include the notation, “discount per agreement.” The contract also required RAD Trust to provide working space for Advantec.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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Advantec is based in Charlotte, NC, and was in the process of attempting to open a Raleigh district office. As the agreement progressed, RAD Trust offered to rent two offices to Advantec for \$300 per month in lieu of Advantec charging for travel costs. Advantec's website lists the 401 Glenwood Avenue, Raleigh, NC location as its "Raleigh, NC office" and internet and telephone book listings still show this location. However, in January 2005, RAD Trust terminated the contract with Advantec as of February 28, 2005.

### **RECOMMENDATION**

RAD Trust should not enter into exclusive agreements with vendors for services or equipment. Further, any purchase agreements should be in writing. Management should ensure that RAD Trust adheres to contracting policies in all instances. RAD Trust should not authorize payment for contract services provided prior to the approval of a signed contract.

#### **7. RAD TRUST ROUTINELY PAID FOR LUNCHEONS, BREAKFAST ITEMS, CHRISTMAS PARTIES, AND SOFT DRINKS FOR ESTATE EMPLOYEES.**

We received allegations that RAD Trust catered luncheons for London Pacific employees using estate funds and that State employees also attended the luncheons. We interviewed staff and reviewed invoices and check registers for the period July 2002 through May 2005. Our interviews and analysis confirmed that management paid for luncheons attended by estate and State employees, lunch at various meetings, Christmas parties for London Pacific employees, breakfast items for estate employees, and soft drinks and snacks for estate employees. Examples of items questioned include the following:

- \$389.15 in accumulated reimbursements to a DOI employee for purchases of doughnuts for London Pacific employees on 36 occasions.
- \$317.40 for a takeout order from Chili's as a "morale booster" lunch meeting.
- Eight other employee lunches for estate employees costing \$2,792.85.
- \$1,103.55 for Christmas luncheons for employees of London Pacific at Angus Barn in Raleigh, NC and Ambrosia Fine Foods in Sacramento, CA.
- Lunch meetings with contractors, vendors, and potential buyers of estate business.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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- \$4,362.56 for purchases of soft drinks for London Pacific employees over a two-year period as a fringe benefit for employees.

In total, we questioned 21 items for \$1,417.98 for RAD Trust and 70 items for \$7,904.99 for London Pacific. See Appendix B for a detailed listing of all food purchases questioned.

RAD Trust management stated these expenses were intended to improve morale after the company entered receivership. With regard to Christmas luncheons and soft drink purchases, RAD Trust management said they were continuing business practices of the estate. Management said lunch meetings were necessary to continue business on short deadlines and to closely resemble business practices in the corporate world. In our opinion the practice of purchasing meals and food items for employees, including DOI employees, is incompatible with the responsibility with which RAD Trust was vested pursuant to the court order.

### **RECOMMENDATION**

RAD Trust management should re-examine its role in protecting the interests of policyholders and revise, where necessary, policies and procedures to ensure the prudent use of trust and estate resources. RAD Trust should discontinue the practice of purchasing meals and food items for DOI, trust, or estate employees. RAD Trust should establish procedures to ensure all expenditures are necessary and proper.

#### **8. RAD TRUST AND DOI EMPLOYEES TRAVELED EXTENSIVELY ON ESTATE BUSINESS WITH MINIMAL ADVANCE TICKET PURCHASES AND SOME FIRST-CLASS TICKET PURCHASES.**

We received allegations that DOI employees' travel expenses were reimbursed using estate funds rather than State funds. Our review of all travel reimbursements, check registers, and all payments to travel agents for the period July 2002 through May 2005 revealed substantial travel costs. During the period reviewed, DOI, RAD Trust, and estate employees charged \$234,510.46 in travel costs. Of that amount, \$81,878.40 was for airline tickets with at least \$4,305 in travel agent and airline ticket change fees. While the trust and estates did pay for DOI employee travel, those payments were justified since the employees were traveling on official business of the trust and the associated estates. Most of the travel was for on-site visits to estates in locations outside North Carolina. However, we did note the following problems with travel:

- Of the 136 trips with airline ticket purchases, 22 did not include documentation showing the date of purchase. Of the remaining 114 trips, the average length of time between purchase and departure was only 11.12 days. Only one purchase was made over 30 days in advance and only 25.44% were made at least two weeks in advance of travel.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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- \$12,178 for DOI employees traveling via first-class airfare on 12 occasions. These charges were paid through the RAD Trust account but allocated 100% to London Pacific.
- \$10,105.13 for two employees to attend an information technology security conference in Orlando, FL. Costs incurred were for rental of a house (\$999.60), conference tuition (\$7,245), airfare and baggage (\$790.40), rental car and associated costs (\$345.63), meals (\$554.50), and books (\$170). Expenses for the RAD Trust Director were charged to RAD Trust (\$5,974.68) while expenses for the London Pacific IT employee were directly charged to London Pacific (\$4,130.45).
- In total we questioned 14 items totaling \$20,126.28 for RAD Trust and three items for \$4,130.45 for London Pacific. See Appendix C for a detailed listing.

RAD Trust management said the trips were necessary to oversee estate operations but it is unclear whether all trips were required. Management and staff indicated trips could be planned in advance to take advantage of airline ticket discounts and no one recalled any emergency travel circumstances.

Management claimed to be unaware of any travel via first-class airfare and speculated that upgrades were provided free-of-charge by the airlines or through use of frequent flyer miles. However, documentation was not available to support those claims.

The travel authorization form for the trip to Orlando, FL, indicated the conference was “related to state security audit” and the purchase order for the trip showed it was “in response to state IT security audit.” Given the stated purpose of the trip, we question the need for an estate employee to attend the conference and the associated expenses. Further, costs associated with State requirements would more properly be charged to DOI rather than RAD Trust and allocated to the estates.

### **RECOMMENDATION**

Given the financial solvency problems of the estates, RAD Trust management should ensure expenses are minimal in all respects. Management should implement procedures to ensure airline tickets are booked in advance to receive discount prices. In addition, management should review all airline ticket purchases to prevent first-class airfare purchases or adequately document when airlines offer upgrades or employee frequent flyer miles are used for upgrades. Finally, RAD Trust management should evaluate the cost-benefit of all travel related to estate management.



## FINDINGS AND RECOMMENDATIONS (CONTINUED)

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**9. THE LEASE FOR OFFICE SPACE IS NOT ECONOMICAL AND RAD TRUST DID NOT HAVE A WRITTEN SUB-LEASE WITH THE DEPARTMENT OF INSURANCE FOR OFFICE SPACE.**

RAD Trust offices are located at 401 Glenwood Avenue, Raleigh, NC. On August 4, 1993, DOI entered into a lease agreement for 3,000 square feet of office space on the top floor of the building at an initial annual cost of \$29,700. On March 31, 1996, RAD Trust took over the lease for expanded office space to encompass the entire building (21,200 square feet) at an annual cost of \$211,801.68. Subsequently, the lease has been amended three times: on August 4, 1998; December 16, 1998; and April 12, 1999. The current lease has been extended through June 30, 2009. The current annual lease for the building is \$377,889 with a final installment of \$459,326.40.

The initial lease for building space was at a rate of \$9.90 per square foot. The building was originally selected due to its proximity to downtown Raleigh and the relative cost of the space. It should be noted that the Glenwood South area in which the office is located had not been revitalized at the time of the original lease agreement. As the area became a preferred location within Raleigh, the associated rents increased. Currently, RAD Trust is paying \$17.82 per square foot for office space and that amount will escalate to \$21.67 by 2009, the final year of the lease. We obtained lease information for all property leased by State agencies in Wake County from the State Property Office. The table below shows the average rental rates for space in Wake County rented by State agencies.

<b>AVERAGE RENTAL RATES PER SQUARE FEET</b>	
Overall rate per square foot	\$12.87
Rate per square foot for office space	13.80
Rate per square foot for office space in Raleigh	13.78
Source: Department of Administration, State Property Office	

Thus, RAD Trust is paying 29% more per square foot than the average to rent office space.

The Department of Insurance also rents office space within the Glenwood facility. Currently, DOI employees who oversee RAD Trust and estate operations are located within the building in addition to personnel in the Financial Analysis Division which is responsible for performing financial statement analysis of all NC licensed insurance entities. During the course of the lease arrangement, other sections within DOI have occupied office space within the Glenwood facility including the Financial Examination Division. Throughout that time, no sub-lease existed between RAD Trust and DOI. Rather, a series of services agreements were signed by which DOI would be billed by RAD Trust for its share of office space and support services. In the agreement, support

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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services were defined as “whatever support may be required the Department in order to supervise and direct RAD’s operations including, but not limited to, the use of office furniture, copy machines, fax machines, telephones, computers, and whatever other equipment and office supplies may be needed by the Department.” Costs were capped at an amount rising from \$60,000 in 1996 to \$300,000 by 2001. The services agreements did not specify the amount of space designated to DOI. After discussions between RAD Trust, DOI, the State Property Office, and the Division of Purchase and Contract, it was determined a sub-lease was necessary. As a result, a sub-lease agreement was finally reached in 2005. On March 1, 2005, the Council of State approved a sub-lease between RAD Trust and DOI for 14,436 square feet (including office and storage) at an annual cost of \$156,000 (\$10.81 per square foot).

### **RECOMMENDATION**

In consultation with the State Property Office, RAD Trust management should seek an alternative office space arrangement that is more economical. Since the current lease is effective through 2009, a cost-benefit analysis should be performed to determine whether it is economical to terminate the lease, pay any penalty, and lease other office space. If the long-term costs to break the lease are not economical, RAD Trust management should seek other, less costly office space at the end of the current lease. Finally, RAD Trust and DOI should ensure that a sub-lease exists at all times for any space rented by RAD Trust to DOI.

#### **10. RAD TRUST ALLOCATED TO THE ESTATES THE COSTS OF LEASEHOLD IMPROVEMENTS AT ITS GLENWOOD OFFICE LOCATION.**

We received allegations that RAD Trust charged the estates for leasehold improvements to the Glenwood Avenue offices. Our review of the lease agreement, check registers, and invoices confirmed that RAD Trust charged the estates and DOI through the monthly allocation and billing process for building improvements. Specifically, we discovered the following leasehold improvements incurred and charged to estates and DOI:

- \$17,724 for demolition, drywall, acoustical ceiling, paint, and electrical costs for a new ceiling in the lower level of the Glenwood building and renovation of three lower level offices directly charged to London Pacific.
- \$44,655 to replace carpet in the Glenwood facility.
- \$3,243 for painting and new sheet rock for hallways as well as other offices throughout the Glenwood building. A note attached to the invoice states “(Senior Deputy Commissioner) said to have RAD pay and allocate accordingly.”

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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RAD Trust management said these expenses were necessary to accommodate the moving of estates into the Glenwood facility. We question charging the costs of leasehold improvements that will benefit future estates, RAD Trust, and DOI beyond the life of the estate charged. The Glenwood building office space is adequate for the number of trust and estate employees and only becomes limited due to DOI employees occupying space within the building.

### **RECOMMENDATION**

RAD Trust management should limit expenses for office improvements, especially given the financial position of companies in receivership. Management should refrain from charging estates for leasehold improvements that will provide benefits extending beyond the life of those estates. Each estate or agency should pay its fair share for the use of office improvements during its time within the building.

#### **11. RAD TRUST USED PRIVATE MOVERS RATHER THAN THE SERVICES OF CORRECTION ENTERPRISES.**

We received allegations that RAD Trust paid moving expenses for DOI employees and used private movers rather than Correction Enterprises staff in violation of NCGS §148-70 that requires State agencies to give preference to Department of Corrections products and services. Review of check registers and invoices revealed private vendors were paid to move items from estate offices to RAD Trust offices, between the RAD Trust/DOI offices at Glenwood and the DOI offices at Dobbs, and within the RAD Trust offices. Specifically, we discovered the following:

- Thrifty Office Furniture moved DOI, RAD Trust, and estate employees to, from, and within the Glenwood building on 20 occasions at a cost of \$20,746.25.
- TROSA Moving re-arranged offices within the Glenwood building in preparation for London Pacific employees moving into the building at a one-time cost of \$301.
- On April 29, 2004, Thrifty Office Furniture moved the former RAD Trust director's office to the Dobbs building which should be a DOI expense.
- Thrifty Office Furniture twice moved furniture to State Surplus Property. Those items were not identified as DOI, RAD Trust, or estate property for billing purposes.
- Supporting documentation does not indicate which staff was moved within the Glenwood building.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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RAD Trust management said they were unaware that Correction Enterprises could be used for these moves and that they believed a private mover must be utilized. We question the hiring of outside movers, especially for re-arranging offices within the Glenwood facility. The use of private moving services to move DOI employees violated NCGS §148-70.

### **RECOMMENDATION**

RAD Trust should comply with NCGS §148-70 and utilize Corrections Enterprises when available to provide more cost-effective moving services. In any situation in which DOI employees are moved, Correction Enterprises must be given preference. Further, due to the financial insolvency of the estates, RAD Trust management should only pay for moving services when absolutely necessary as moving items within the Glenwood facility appears to be a questionable use of funds.

### **12. RAD TRUST PAID FOR PERSONAL ITEMS FOR EMPLOYEES.**

We received allegations that RAD Trust employees purchased personal items using trust and estate accounts and credit cards. Our review of check registers and invoices for the period July 2002 through May 2005 revealed the following purchases of personal items through the RAD Trust and estate accounts:

- Plants and flowers were purchased from Fowler's Nursery for the former Senior Deputy Commissioner, former RAD Trust director, and current RAD Trust manager costing \$461.25. RAD Trust management stated the vendor would not accept credit cards at the time of delivery. Therefore, the flowers were billed to and paid for by RAD Trust. The individual employees were later billed for their purchases. Employees reimbursed RAD Trust for the flowers and shrubs.
- The former Senior Deputy Commissioner purchased a sofa for his office using RAD Trust funds at a cost of \$1,132.06 in May 2003. After questions about this transaction arose, he reimbursed RAD Trust for this purchase in July 2004 and moved the sofa to a personal residence.
- Advantec Global Services, Inc. charged RAD Trust \$1,419.09 for a refurbished computer and monitor purchased for the former Senior Deputy Commissioner (see finding #6). After receiving the bill, RAD Trust was reimbursed for the cost. Computer memory in the amount of \$149.80 was also purchased and reimbursed for the same individual through a similar process.
- Employees routinely shipped personal items using RAD Trust UPS, DHL, Airborne Express, and Federal Express accounts as well as the London Pacific UPS account. We noted 12 instances totaling \$325.90.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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RAD Trust management allowed personal items to be purchased through RAD Trust and/or estate accounts as well as personal use of phones, postage machine, and shipping charges as a method to ensure honesty. They said employees were more likely to report personal use of items and pay for them if given the opportunity.

Further, the former Senior Deputy Commissioner stated his purchase of the sofa was necessary to furnish his office. He said he simply paid for the sofa himself to prevent questions as to whether the initial purchase was needed. As to the computer and monitor purchase, the former Senior Deputy Commissioner stated the vendor accidentally ran the purchase through the RAD Trust account rather than billing him personally.

After determining the widespread use of RAD Trust and estate accounts and equipment for personal purposes, we decided to examine deposits and receipts to quantify the total amount. Our review revealed:

- \$1,596.22 in employee reimbursements for postage/telephone usage. Employees were permitted to use the postage machine and long distance telephone as long as they reimbursed RAD Trust for the usage. Employees were assigned a code that they keyed into the postage machine and/or telephone so they would be charged for their personal usage. RAD Trust management allowed this practice because they believed it kept the employees “honest.”
- \$4,635.49 in employee reimbursements for RAD Trust and DOI employee purchases of software, cables, and other computer-related items originally billed to RAD Trust. Also, computers were refurbished and billed to RAD Trust. These purchases were subsequently billed to the individuals who reimbursed RAD Trust. Also, employees purchased computers from the estates and/or RAD Trust. (See finding # 3)
- \$1,559.63 in employee reimbursement for miscellaneous purchases (batteries, moving boxes, sofa).

RAD Trust management did not provide any written policies and procedures regarding employee reimbursement for usage of postage/telephone, personal purchases in name of RAD Trust, etc. Management allowed these practices because they believed the employees were honest about the usage and subsequent reimbursement. They did not see a problem with these practices.

### **RECOMMENDATION**

The practice of allowing RAD Trust and DOI employees to use the postage machine, long distance telephone, and make personal purchases using RAD Trust accounts and credit cards should be discontinued. RAD Trust management should develop policies and procedures to address these practices.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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### **13. RAD TRUST PURCHASED ADDITIONAL ITEMS THAT DO NOT APPEAR REASONABLE AND NECESSARY FOR ESTATE OPERATIONS.**

Based on allegations from the original complaints as well as information gathered in interviews, we reviewed invoices, check registers, and bank statements for RAD Trust and the estates for the period July 2002 through May 2005 for items related to food purchases (finding #7), computer purchases (finding #5), travel reimbursements (finding #8), payments to selected vendors (findings #6 and #11), leasehold improvements (finding #10) and other expenditures. Based on our review, we found other purchases that appear to be a questionable use of RAD Trust and estate funds. For the purpose of this report, we classified the questionable expenses into three categories as follows:

1. Magazine and newspaper subscriptions that do not appear necessary for RAD Trust or estate operations.
2. Certification dues and examination fees paid for employees of DOI, RAD Trust, and the estates with unclear benefit to the estates.
3. Other miscellaneous questioned costs.

The following are some examples of questioned expenses that do not appear reasonable and necessary. See Appendix D for a detailed list of the \$30,033.32 in additional questioned costs.

1. Magazine and newspaper subscriptions
  - Two-year subscription to *The Wall Street Journal* for \$319 paid twice (\$638 total) during the period reviewed.
  - \$860.03 for annual subscriptions for three years for *Lawyers Weekly* for Department of Justice Deputy Attorney General assigned to DOI. In addition, RAD Trust paid \$277.25 for a “Bankruptcy Practice Manual” for one of the deputy attorney generals assigned to DOI.

RAD Trust management believes the newspaper subscriptions were necessary to maintain awareness of business activities and check investment valuations and “stock pricing.” We question whether that information could be obtained online through free services on the web. Further, we question why the Department of Justice would not pay for materials for its employees to perform their jobs.

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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### 2. Certification dues and examination fees

- \$250 paid in annual dues for the former Senior Deputy Commissioner to maintain Certified Fraud Examiner (CFE) credentials for a two-year period.
- \$223.14 for a study guide and examination fee for the Computing Technology Industry Association (CompTIA) examination for former RAD Trust Director and \$175 for security certification examination for London Pacific information technology employee.

RAD Trust management said the CFE certification was paid by the Trust to provide more respect for testimony in court against insurers. In addition, management believed paying for certifications provided a benefit to the estates. It should be noted that DOI does not routinely pay for certification dues and examination fees for employees.

### 3. Other miscellaneous questioned costs.

- \$3,280 for consulting services in which dates on an invoice were changed to allow payment to the contractor rather than having the invoice designated “Class 5” and not be paid until after all other creditors of the estate.
- \$40.45 for a weather radio for RAD Trust.
- \$143.94 for a new cellular phone for a London Pacific employee only five months prior to the scheduled shutdown of operations.
- \$3,475 for training for three employees for “character-building for low self-esteem employees” provided by Legacy Center, a company that purchased office equipment from the London Pacific estate.
- \$13,000 candidate placement fee paid to an employment company to assist in hiring a new RAD Trust controller. The fee was reimbursed on a pro-rata basis by the firm because the controller did not maintain employment for 90 days.

We asked RAD Trust management for explanations for items questioned above. Management noted that RAD Trust attempted to make “prudent” decisions to ensure policyholders received the highest value on their policies. However, current and prior management and staff acknowledged that some mistakes may have been made and that some expenses could appear strange to outsiders. Henceforth, RAD Trust management stated they will try to follow State guidelines where appropriate.

Our extensive review of expenditures, reported in this finding and previous findings, indicates that staff and management operated under a belief that RAD Trust and the estates could operate outside restrictions and limitations of State government allowing freedom to purchase whatever items they deemed necessary. However, the trust

## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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document creating RAD Trust notes the trustee shall carry out functions “consistent with the regulations of the Department of Insurance” and “pursuant to standards of ethical behavior and professional conduct applicable to employees and officers of the State of North Carolina.” Further, the trustee has a fiduciary responsibility to manage the estates well and spend resources wisely, especially given the precarious financial position of insolvent insurance companies.

### **RECOMMENDATION**

We recommend RAD Trust management re-examine its role in protecting the policyholders and revise, where necessary, policies and procedures to ensure the prudent use of trust and estate resources. RAD Trust management should discontinue the practice of using estate assets for employee expenses such as professional dues, certification fees, and professional subscriptions. Further, management should examine all expenses to ensure the reasonableness and necessity of each disbursement of trust or estate funds.

#### **14. RAD TRUST DID NOT HAVE ADEQUATE WRITTEN POLICIES AND PROCEDURES.**

We reviewed existing policies and procedures for RAD Trust as well as former policies and procedures. In addition, we examined personnel files, invoices, purchase orders, contracts, and other financial documentation to determine whether policies and procedures were in place.

In November 2004, RAD Trust updated their “Employee Personnel Guide.” This guide outlines policies on attendance, standard of conduct, conflicts of interest, time reporting, expense reporting, travel reimbursement, use of equipment, and purchase of RAD Trust or estate assets. Prior to the November 2004 version, no policy existed to prevent employees from purchasing assets of RAD Trust or the estates. (See finding #3).

In March 2005, RAD Trust updated the “Accounting Policy and Procedures Manual” (previous revision May 2002). The manual provides guidance on cash receipts, bank reconciliations, purchasing, contract services, cash disbursements, inventory, financial reports, time reporting, allocation of RAD Trust expenses to the estates, and fixed assets. Several RAD Trust employees and DOI employees overseeing estates admitted that formal, written policies for many activities did not exist prior to the past year.

Our review of invoices, purchase orders, and contracts revealed inadequate documentation to support several purchases. Current accounting policy requires a purchase order for purchases in excess of \$100, two quotes in writing or by telephone for purchases over \$500, and three written quotes for purchases in excess of \$2,000. However, no policies



## **FINDINGS AND RECOMMENDATIONS (CONTINUED)**

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requiring bids or quotes existed prior to March 2005. We discovered:

- 18 instances totaling \$45,590.18 of items purchased without bids or quotes. (See Appendix E)
- All equipment and software purchases from Advantec Global Services, Inc. showed no evidence of bids or quotes. (See finding #6)
- Nine occurrences totaling \$34,000.13 lacked a purchase order despite policies requiring them for purchases in excess of \$100. (See Appendix E)

We also discovered contracts were not in place for recurring services. Current RAD Trust accounting policy states, “All contract services require prior approval by the CSG Senior Deputy Commissioner” while the prior procedures required “All contract services, such as legal and consulting, require an approved contract signed by a Deputy Commissioner or the Senior Deputy Commissioner.” However, Advantec Global Services, Inc. began providing information technology support services as well as selling equipment to RAD Trust and the estates in October 2003 though no signed contract was in place until March 24, 2004. Further, the firm of Bode, Call, and Stroup, LLP provided legal services to RAD Trust and the estates for years without a written contract. During the period of our review, RAD Trust and the estates paid Bode, Call, and Stroup, LLP \$278,383.82 in legal services without a contract. In April 2005, RAD Trust initiated attempts at formulating a written contract between the legal firm and RAD Trust and an e-mail from the Senior Deputy Commissioner regarding representation of the London Pacific estate notes that RAD Trust will “follow state bid and contracting requirements.”

Finally, our review of invoices revealed five payments totaling \$13,572.57 in which payments were made for items without proper supporting documentation in the form of receipts, packing slips, purchase requests, et al. (See Appendix F) Some of these payments were supported through hand-written notes by RAD Trust or estate employees.

### **RECOMMENDATION**

RAD Trust should implement and follow all necessary accounting policies and procedures to adequately support payments. RAD Trust management should not authorize payment for purchases exceeding the required dollar thresholds that do not have bids or quotes attached. Further, no amounts should be paid for services prior to the signing of a contract. Finally, management should not pay for items without receipts, packing slips, and other documentation that adequately support payment.

## **FINDINGS AND RECOMMENDATIONS (CONCLUDED)**

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### **15. CHECK-WRITING PROCEDURES AND PERFORMANCE OF BANK RECONCILIATIONS DID NOT ADEQUATELY DETECT ERRORS.**

RAD Trust maintains an operating bank account, an interest-bearing investment deposit account, and a payroll account. The “Accounting Policy and Procedures Manual” requires the accounting staff to perform monthly bank reconciliations for the estates and RAD Trust accounts. Further, the policies require the examiner-in-charge to review the reconciliations for his/her estate and the Financial Analysis Division Deputy Commissioner to review the reconciliations for the RAD Trust bank accounts. The policy states, “The reviews should include an evaluation of the cleared and outstanding checks for propriety.”

For the period July 1, 2002, through May 31, 2005, we reviewed check registers, bank statements, bank reconciliations, and cancelled checks for large and/or unusual payments, missing checks, etc. Based upon our review, we noted the following problems:

- Check registers showed that checks were not written in sequential order through January 2004;
- 57 checks were numbered incorrectly on the check registers;
- 11 check numbers were voided and re-used;
- One check was written to a specific person per the check register but to a different person per the actual check;
- Unable to locate three checks or identify these checks on the check register;
- Check numbers were assigned to electronic transfers (payroll and payroll taxes) to aid in reconciling bank statements (numbers were later voided).

The monthly reviews did not identify and correct the problems. Failure to establish controls over check writing increases the likelihood that erroneous or improper transactions are processed.

### **RECOMMENDATION**

RAD Trust management should implement specific accounting policies and procedures to prevent and detect errors. These policies and procedures should address such issues as writing checks in sequential order, voiding check numbers, identifying all checks (including voided checks) on the check register, and a detailed, thorough review of the monthly bank reconciliations. A system for distributing and updating these procedures should also be implemented. Once the procedures are in place, management should enforce strict adherence to the procedures in all areas.

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## CONCLUSION

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Our review of the operations of RAD Trust and the estates indicates that RAD Trust management operated under a belief that RAD Trust and the estates could operate outside restrictions and limitations of state government. As such, RAD Trust management engaged in business practices and made purchases in whatever manner they deemed necessary despite the financial position of the estates. However, the trust document creating RAD Trust notes the trustee shall carry out functions “consistent with...the regulations of the Department of Insurance” and “pursuant to standards of ethical behavior and professional conduct applicable to employees and officers of the State of North Carolina.” Further, the trustee has a fiduciary responsibility to manage the estates well and spend resources wisely, especially given the precarious financial position of insolvent insurance companies.

RAD Trust management should focus their efforts on cutting expenses of insolvent companies in an effort to maximize payouts for policyholders and creditors. Given the Commissioner of Insurance’s responsibility as grantor and the Senior Deputy Commissioner’s responsibility as trustee for companies facing insolvency, the officials from the Department of Insurance have an even greater duty to protect the policyholders through prudent use of estate assets and management of operations.

The responsibility for managing insurance companies in receivership exists in all 50 states although operations and methods for managing the estates differ. Therefore, the Department of Insurance should seek guidance from other states as well as the National Association of Insurance Commissioners on best practices for this responsibility.

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**APPENDIX A  
DOCUMENTED ASSET SALES TO EMPLOYEES AND VENDORS**

Employee/ Vendor	Item(s) Bought	Amt Paid	Employee/ Vendor	Item(s) Bought	Amt Paid
LP Empl #1	Desk, monitor, cabinet/bookcase, desk chair	\$ 120	LP Empl #26	Computer, chair, table	160
LP Empl #2	Computer, monitor, 3 chairs, 3 pictures, desk, table	425	LP Empl #27	Computer, scanner	230
LP Empl #3	Fax, refrigerator	80	LP Empl #28	Picture	25
LP Empl #4	Computer, monitor	110	LP Empl #29	Monitor, 2 shelves, 2 tables	85
LP Empl #5	Chair, file cabinet	45	LP Empl #30	TV, TV cabinet, file cabinet, unknown item	190
LP Empl #6	Shelving	40	LP Empl #31	Printer	25
LP Empl #7	Picture	30	LP Empl #32	Chairs, cabinets, table, computer	350
LP Empl #8	Computer, printer	200	LP Empl #33	Computers	230
LP Empl #9	Computer, chair, calculator	150	LP Empl #34	Computer, monitor	220
LP Empl #10	3 chairs, 2 cabinets	115	LP Empl #35	Computer	75
LP Empl #11	Laptop, computer	600	LP Empl #36	Computer, unknown items	235
LP Empl #12	Bookcase, chair	50	LP Empl #37	2 cabinets, cubicle	200
LP Empl #13	File cabinet, 3 bookcases	70	LP Empl #38	Computer	100
LP Empl #14	Laptop	75	LP Empl #39	Computer	130
Legacy Center	Projector, plants, mail shelves, whiteboard, metal credenza, bookcases, printer	535	LP Empl #40	Computer	130
Wallace	13 racks	325	LP Empl #41	Computer, table, 2 chairs	165
DOI Empl #1 (paid by LP Empl #15)	Servers	4,400	LP Empl #42	Computer	65
LP Empl #15	Printer, computer, 2 monitors, end table, desk, cordless phone	1,700	LP Empl #43	2 chairs	50
LP Empl #16	Table, chair, file cabinet, computers, monitor	175	LP Empl #44	2 bookcases, picture	125
LP Empl #17	Love seat, 2 chairs, 2 tables, hutch, 2 stools, 2 carts	440	LP Empl #45	Laptop, pictures	500
LP Empl #18	2 chairs, file cabinet, large picture, 2 computers	280	Exquisite Entertainment	2 cubicles, file cabinet, panels	250
LP Empl #19	Fax machine, 2 shelves	75	Mourier Land Investment Corp	2 conference room tables and chairs	2,500
LP Empl #20	Zip drive, computer, monitor	125	KBM Workspace	Furniture, chairs, tables, desks, conference table, credenzas book cases, shelving	8,000
LP Empl #21	2 chairs, oil painting	45	Palmer & Swanson	Furniture	10,000
LP Empl #22	Computer, misc. office furniture	485	LP Empl #46	Cubicle, 3 cabinets	225
LP Empl #23	Camcorder, chair, scanner, monitor	70	DOI Empl #2	Computer	125
LP Empl #24	Computer	140	Total Documented		\$35,345
LP Empl #25	End table	50			

Source: London Pacific files, invoices, receipts, bank statements, deposits

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**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
8/30/2002	2650	Joe Holloway	2	1, 2	RAD Trust	\$ 53.12	doughnuts from Krispy Kreme on 8/9, 8/16, 8/23, 8/30	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
9/30/2002	2688	Joe Holloway	2	1, 2	RAD Trust	53.12	doughnuts from Krispy Kreme on 9/6, 9/13, 9/20, 9/27	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
10/31/2002	2719	Joe Holloway	2	1, 2	RAD Trust	55.04	doughnuts from Krispy Kreme on 10/4/, 10/11, 10/18, 10/25	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
11/29/2002	2766	Joe Holloway	2	1, 2	RAD Trust	54.61	doughnuts from Krispy Kreme on 11/1, 11/8, 11/15, 11/22	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
11/29/2002	2767	Boyce Oglesby	1	1, 2	RAD Trust	68.43	lunch at Carver's Creek for five Boyce and Dan Henderson "re: phone tel HYBR deal"	Wasteful expenditure to purchase lunch for employees and persons external to trust and estates.
12/31/2002	2801	Joe Holloway	2	2, 3	RAD Trust	13.98	doughnuts from Krispy Kreme on 12/13/02	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
2/13/2003	2863	Joe Holloway	2	1, 2	RAD Trust	26.91	doughnuts from Krispy Kreme on 1/3, 1/7,1/31	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
3/5/2003	2899	Joe Holloway	2	1, 2	RAD Trust	28.83	doughnuts from Krispy Kreme on 2/7, 2/14, 2/28	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
4/2/2003	2960	Joe Holloway	2	1, 2	RAD Trust	19.22	doughnuts from Krispy Kreme on 3/7, 3/28	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
4/2/2003	2966	Joyce Stevens	2	electronic pymt	RAD Trust	28.06	bagels for London Pacific from Panera Bread	Wasteful expenditure to purchase breakfast for employees
5/7/2003	3056	Joe Holloway	2	electronic pymt	RAD Trust	9.61	doughnuts from Krispy Kreme on 4/11	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
6/18/2003	3115	Joe Holloway	4	electronic pymt	RAD Trust	19.22	doughnuts from Krispy Kreme on 5/23, 5/30	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
6/18/2003	3118	Joyce Stevens	1	electronic pymt	RAD Trust	119.84	Miscellaneous coffee order from Larry's Beans	Wasteful expenditure to purchase gourmet coffee for employees.
7/16/2003	3146	Joe Holloway	4	electronic pymt	RAD Trust	19.22	doughnuts from Krispy Kreme on 6/13, 6/20	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
8/13/2003	3197	Joe Holloway	4	electronic pymt	RAD Trust	9.61	doughnuts from Krispy Kreme on 7/10	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
9/19/2003	3250	Joyce Stevens	2	electronic pymt	RAD Trust	81.00	11 coffees from Larry's Beans	Wasteful expenditure to purchase gourmet coffee for employees



**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
9/30/2003	3280	Joe Holloway	4	electronic pymt	RAD Trust	\$ 16.00	doughnuts from Krispy Kreme on 9/5, 9/12, 9/19	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
10/15/2003	3307	Joe Holloway	4	electronic pymt	RAD Trust	10.66	doughnuts from Krispy Kreme on 8/22, 8/29	Wasteful expenditure to purchase doughnuts for employees on a weekly basis
2/26/2004	electronic pymt	Joyce Stevens	2	electronic pymt	RAD Trust	317.40	lunch for "business meeting", to go order from Chili's	Wasteful expenditure to purchase lunch for employees
5/19/2004	3627	Sharon Holt	2	2, 4	RAD Trust	272.55	"lunch for Hartford meetings" to make progress on LP-Hartford exchange, drinks and ice from Harris Teeter, sandwich boxed lunches from Carolina Café, sandwiches and chips from Sunflower's, email as if training seminar for justification	Wasteful expenditure to purchase lunch for employees and persons external to trust and estates, False justification used since this was not a training seminar.
6/4/2004	3661	BB&T Bankcard	4	2, 4	RAD Trust	141.55	lunches from Carolina Café, drinks from Harris Teeter for meeting with LP, Hartford, and NOHLGA to discuss notification package--3 DOI employees, 2 LP employees, 1 outside attorney (Lane Wharton), 1 from Ernst & Young, 4 from Hartford, 6 from NOHLGA, 1 from CA Life & Health Guaranty Assoc, 1 counsel to CAL&HGA	Wasteful expenditure to purchase lunch for employees and persons external to trust and estates.
9/5/2002	714156	George Nicholson	6	5	London Pacific	226.06	Lunch at Outback for Mass Mutual meeting (\$66.68), lunch at Carver's Creek with Mass Mutual employees for due diligence meeting (\$119.68), lunch at Carver's Creek with Basic Capital Mgmt for due diligence meeting (\$39.70)	Wasteful expenditure to purchase lunch for employees and persons external to trust and estates.

**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
9/12/2002	715582	Capitol One Source	7	5	London Pacific	\$ 9.79	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/20/2002	717421	Capitol One Source	7	5	London Pacific	88.13	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/27/2002	719427	Capitol One Source	7	5	London Pacific	107.71	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/4/2002	720918	Capitol One Source	7	5	London Pacific	95.47	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/4/2002	720922	Capitol One Source	7	5	London Pacific	67.32	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/4/2002	720923	Capitol One Source	7	5	London Pacific	37.43	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/7/2002	721249	Capitol One Source	7	5	London Pacific	88.13	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/11/2002	722970	Capital Creations	5	5	London Pacific	229.52	pizza for employee luncheon	Wasteful expenditure to purchase lunch for employees
10/14/2002	722973	Costco Retail Services	3	5	London Pacific	61.40	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/17/2002	723917	Capitol One Source	5, 7	5	London Pacific	97.92	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/21/2002	727070	Adorno's Catering	3	5	London Pacific	266.19	employee appreciation luncheon for 26	Wasteful expenditure to purchase lunch for employees
10/23/2002	725426	Capitol One Source	5, 7	5	London Pacific	58.75	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/28/2002	726330	Capitol One Source	5, 7	5	London Pacific	29.38	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
11/8/2002	729779	Red Hot & Blue	5	5	London Pacific	457.83	barbecue luncheon for 30	Wasteful expenditure to purchase lunch for employees at cost >\$15 per person
11/8/2002	cash	Back Forty Texas BBQ	3	5	London Pacific	485.00	barbecue luncheon for 27	Wasteful expenditure to purchase lunch for employees at cost >\$17 per person
11/13/2002	731304	Costco Retail Services	3, 5	3	London Pacific	111.49	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees

**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
12/6/2002	737849	Capitol One Source	5, 7	3	London Pacific	\$ 401.48	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
12/6/2002	737866	Costco Retail Services	3, 5	3	London Pacific	205.87	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
12/6/2002	737875	Vincent's Pizza	8	3	London Pacific	108.22	"lunch Raleigh office"	Wasteful expenditure to purchase lunch for employees
12/17/2002	800725	George Nicholson	5	3	London Pacific	475.00	Christmas luncheon at Angus Barn for 18	Wasteful expenditure to pay for employee Christmas party at cost >\$26 per person
12/30/2002	803714	Ambrosia Fine Foods	3	3	London Pacific	628.55	Christmas luncheon for 28	Wasteful expenditure to pay for employee Christmas party at cost >\$22 per person
1/3/2003	805043	Capitol One Source	5, 9	3	London Pacific	48.92	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
1/13/2003	807246	Capitol One Source	5, 9	3	London Pacific	117.50	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
1/21/2003	809148	Capitol One Source	5, 9	3	London Pacific	29.38	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
1/22/2003	809577	Capitol One Source	5, 9	3	London Pacific	48.96	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
2/3/2003	811962	Capitol One Source	5, 9	3	London Pacific	88.13	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
2/3/2003	811975	Round Table Pizza	3, 5	3	London Pacific	142.54	employee recognition luncheon	Wasteful expenditure to purchase lunch for employees
2/19/2003	815185	Capitol One Source	5, 9	3	London Pacific	88.74	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
2/21/2003	816268	Costco Retail Services	5, 10	3	London Pacific	219.84	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
3/11/2003	820436	Capitol One Source	5, 9	3	London Pacific	78.95	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
3/21/2003	822917	Capitol One Source	5, 9	3	London Pacific	49.27	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
3/27/2003	824085	Capitol One Source	5, 9	3	London Pacific	19.74	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees

**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
4/3/2003	825588	Capitol One Source	5, 9	3	London Pacific	\$ 29.68	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
4/8/2003	826453	Capitol One Source	5, 9	3	London Pacific	69.16	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
4/8/2003	826460	Costco Retail Services	5, 10	3	London Pacific	191.99	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
4/21/2003	829116	Capitol One Source	5, 9	3	London Pacific	59.21	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
4/24/2003	830257	Capitol One Source	5, 9	3	London Pacific	39.47	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
4/28/2003	831146	Capitol One Source	5, 9	3	London Pacific	69.00	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
5/8/2003	833823	Capitol One Source	5, 9	3	London Pacific	49.27	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
5/16/2003	835845	Capitol One Source	5, 9	3	London Pacific	29.84	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
5/20/2003	836195	Capitol One Source	5, 9	3	London Pacific	29.84	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
5/27/2003	837697	Capitol One Source	5, 9	3	London Pacific	39.51	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
6/11/2003	841344	Capitol One Source	5, 9	3	London Pacific	40.32	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
6/11/2003	841353	Costco Retail Services	5, 10	3	London Pacific	8.34	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
6/18/2003	842886	Capitol One Source	5, 9	3	London Pacific	19.58	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
7/1/2003	845402	Capitol One Source	5, 9	3	London Pacific	78.94	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
7/10/2003	847818	Costco Retail Services	5, 10	3	London Pacific	79.19	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
7/23/2003	850593	Capitol One Source	5, 11	3	London Pacific	39.47	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees

**APPENDIX B  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
7/31/2003	852292	Capitol One Source	5, 11	3	London Pacific	\$ 59.21	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
8/8/2003	854331	Capitol One Source	5, 11	3	London Pacific	9.99	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
8/8/2003	854337	Costco Retail Services	5, 10	3	London Pacific	126.63	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
8/29/2003	859089	Capitol One Source	5, 11	3	London Pacific	102.22	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/3/2003	859768	Capitol One Source	5, 11	3	London Pacific	21.29	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/9/2003	860887	Costco Retail Services	5, 10	3	London Pacific	95.24	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/19/2003	863617	Capitol One Source	5, 11	3	London Pacific	82.66	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/19/2003	863620	Wiliam Ditenhafer	5	3	London Pacific	25.00	pizza for 4 Front consultants on 8/25/03	Wasteful expenditure to purchase lunch for consultants
9/26/2003	865333	Capitol One Source	5, 11	3	London Pacific	25.40	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/9/2003	868803	Capitol One Source	5, 11	3	London Pacific	86.97	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/14/2003	869576	Capitol One Source	5, 11	3	London Pacific	41.25	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
10/14/2003	869589	Costco Retail Services	5, 10	3	London Pacific	168.15	soft drinks, key lime pie for employees	Wasteful expenditure to purchase soft drinks and dessert for employees
1/8/2004	7010	Costco	5, 10	3	London Pacific	81.84	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
1/28/2004	7082	Wiliam Ditenhafer	3, 5	3	London Pacific	64.08	“dinner for consultants” at Stool Pigeons—attendees Ditenhafer, Jerry Tucker, Jon Fox, Brian Waismen, Gene Lay, Ashby Spratley, Robert Morris	Wasteful expenditure to purchase dinner for consultants

**APPENDIX B  
DEPARTMENT OF INSURANCE—RAD TRUST  
QUESTIONED COSTS—FOOD PURCHASES**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
2/23/2004	7123	Bank of America -VISA—Sunflower's		3	London Pacific	\$ 32.79	lunch for LP meeting with Brian Falk (D&T)...Boyce, Lane, Joe, Brian, David, Michael	Wasteful expenditure to pay for lunch for employees and tax services consultant
3/29/2004	7213	Bank of America-- VISA--Café Carolina, Fresh Market, Harris Teeter	5	3	London Pacific	140.64	LP meeting...sandwiches from Café Carolina (\$112.59), fruit salads from Fresh Market (\$20.56), drinks from Harris Teeter (7.49)	wasteful expenditure to pay for lunch for employees
4/26/2004	7297	Bank of America-- VISA--Harris Teeter, Café Carolina	5	3	London Pacific	260.71	breakfast and lunch for meeting with Hartford, NOHLGA, Harris Teeter (\$22.64), Café Carolina (\$238.09)	wasteful expenditure to pay for breakfast and lunch for employees and potential buyers
5/5/2004	7319	Costco	5, 10	3	London Pacific	101.60	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
9/7/2004	7591	Costco	5, 10	2	London Pacific	78.38	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
11/8/2004	7719	Costco	5, 10	2	London Pacific	87.09	soft drinks for employees	Wasteful expenditure to purchase soft drinks for employees
3/21/2005	8113	Costco Retail Services	5, 10	2, 5	London Pacific	72.42	soft drinks, cherry pie, ice cream for employees	Wasteful expenditure to purchase soft drinks and dessert for employees

Total	\$ 9,322.97
RAD Trust	\$1,417.98
London Pacific	\$7,904.99

Legend

- 1 former Senior Deputy Commissioner
- 2 current Senior Deputy Commissioner
- 3 former RAD Trust director
- 4 current Deputy Commissioner for Financial Analysis
- 5 current examiner-in-charge of London Pacific estate
- 6 current London Pacific treasurer
- 7 former London Pacific operations manager
- 8 former DOI financial analyst
- 9 former London Pacific assistant operations manager
- 10 current London Pacific personnel director
- 11 former London Pacific operations clerk

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**APPENDIX C  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--TRAVEL**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
8/28/2002	2647	Gene Lay	1	1, 2	RAD Trust	\$ 1,441.50	first class airfare on both legs of outgoing trip to Sacramento, CA	wasteful expenditure to fly first class
4/2/2003	2961	Gene Lay	1	electronic pymt	RAD Trust	1,492.00	first class airfare on both legs of outgoing trip to Sacramento, CA	wasteful expenditure to fly first class
7/30/2003	3169	Joe Holloway	4	electronic pymt	RAD Trust	1,009.00	first class on outgoing trip to Newark, NJ	wasteful expenditure to fly first class
3/16/2004	elec pymt	Peggy Dehart	3	electronic pymt	RAD Trust	1,352.90	first class airfare on all 4 legs of trip to and from Sacramento, CA	wasteful expenditure to fly first class
3/31/2004	3564	BB&T Bankcard-- Expedia, SANS Institute, Southwest Air, Transcender Corp	2, 3	2,4	RAD Trust	6,314.40	house in Kissimmee, FL for AGSI conference for Gene Lay, William Ditenhafer, and 2 Advantec employees (\$1,999.20), tuition for conference for Gene Lay (\$3,245), airfare for conference (\$191.20), software for class taken by Ashby (\$879)	wasteful expenditure for total seminar costs over \$10,000 for two employees
4/15/2004	elec pymt	Gene Lay	2	electronic pymt	RAD Trust	585.88	meals, parking, baggage, car rental, and gas associated with SANS Conference in Orlando, FL	wasteful expenditure for total seminar costs over \$10,000 for two employees
4/27/2004	3598	BB&T Bankcard-- SANS Institute, Southwest Air	2, 3	3, 4	RAD Trust	973.00	additional SANS conference tuition (\$755), airfare change of date charge (\$28), books for conference (\$170)	wasteful expenditure for total seminar costs over \$10,000 for two employees
5/4/2004	elec pymt	Peggy Dehart	2	electronic pymt	RAD Trust	987.90	first class airfare on both legs of return trip from Sacramento, CA	wasteful expenditure to fly first class
5/17/2004	3620	Hickory Beeline Travel	2	2, 4	RAD Trust	1,327.90	first class airfare on all 4 legs of trip to and from Sacramento, CA for Peggy Dehart	wasteful expenditure to fly first class
10/5/2004	3779	Hickory Beeline Travel	4	2, 4	RAD Trust	715.00	first class airfare on both legs of return trip from Sacramento, CA in addition to \$387.90 for original ticket for Laura Beasley	wasteful expenditure to fly first class
10/20/2004	3795	Hickory Beeline Travel	4	2, 4	RAD Trust	834.20	first class airfare on one of two legs of return trip from Sacramento, CA for Peggy Dehart	wasteful expenditure to fly first class



**APPENDIX C  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--TRAVEL**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
11/19/2004	3832	Hickory Beeline Travel	4	2, 4	RAD Trust	\$ 1,414.80	first class airfare on one of two legs of outgoing trip to Sacramento, CA for Peggy Dehart and Laura Beasley	wasteful expenditure to fly first class
11/9/2004	elec pymt	Justin Vargas	2	electronic pymt	RAD Trust	752.40	first class airfare on one of two legs of return trip from Sacramento, CA for Justin Vargas	wasteful expenditure to fly first class
12/13/2004	elec pymt	Justin Vargas	2	electronic pymt	RAD Trust	925.40	first class airfare on both legs of outgoing trip to Sacramento, CA for Justin Vargas	wasteful expenditure to fly first class
3/29/2004	7213	Bank of America-- Visa-- SANS Institute		3	London Pacific	3,245.00	conference registration (\$3,245) for William Ditenhafer for SANS Security Conference 2004--email to charge to RAD Trust credit card	wasteful expenditure for total seminar costs over \$10,000 for two employees
4/26/2004	7297	Bank of America-- Visa--Delta Air	5	3	London Pacific	567.20	airfare for William Ditenhafer for trip to Orlando, FL for SANS Conference	wasteful expenditure for total seminar costs over \$10,000 for two employees
5/3/2004	7314	William Ditenhafer	3, 5	3	London Pacific	318.25	meals for SANS Security Conference	wasteful expenditure for total seminar costs over \$10,000 for two employees

Total	\$24,256.73
London Pacific	\$4,130.45
RAD Trust	\$20,126.28

Legend:

- 1 former Senior Deputy Commissioner
- 2 current Senior Deputy Commissioner
- 3 former RAD Trust Director
- 4 current Deputy Commissioner for Financial Analysis
- 5 examiner-in-charge of London Pacific estate

**APPENDIX D  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--MISCELLANEOUS ITEMS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
11/26/2002	2758	The Wall Street Journal	1	1, 2	RAD Trust	\$ 319.00	two year subscription	Unnecessary expenditure when stock information and business news available for free online
1/21/2003	2828	Lawyers Weekly	3	1, 2	RAD Trust	282.23	annual subscription renewal for materials for Department of Justice attorneys	Unnecessary expenditure to pay for subscription for attorneys from Department of Justice
1/21/2003	2831	Patterson Business Systems	1	1, 2	RAD Trust	1,800.00	disassemble and move Kardex Kompakt system for DOI, "needed to clear space in Glenwood office to put LP files"	Wasteful expenditure without evidence of cost/benefit analysis of whether a more economical method of providing storage space could have been found
3/5/2003	2903	PC Magazine	4	1, 2	RAD Trust	29.97	PC magazine annual subscription	Wasteful expenditure with little or no benefit to the estates
3/27/2003	2944	Association of Certified Fraud Examiners	1, 4	1, 2	RAD Trust	130.00	annual dues--certified fraud examiner for Alex Spencer and \$10 donation to Ritchie-Jennings Memorial Scholarship Fund	Wasteful expenditure for estates paying for certification dues for DOI employee and donation for scholarship fund. DOI does not pay for certifications
7/9/2003	3124	BB&T-VISA--Logan Trading Co	3	2, 4	RAD Trust	64.13	plants and pots	Wasteful expenditure
12/17/2003	3426	Lawyers Weekly	3	3, 4	RAD Trust	283.55	annual subscription renewal for materials for Department of Justice attorneys	Unnecessary expenditure to pay for subscription for attorneys from Department of Justice
1/9/2004	3461	Seritec Inc	3	2, 4	RAD Trust	32.96	nameplates for Advantec	Wasteful expenditure to pay for nameplates for offices of vendor/contractor
2/3/2004	3489	Elizabeth Clementine Peterson	4	2, 4	RAD Trust	277.25	Bankruptcy Practice Manual for Department of Justice attorney	Unnecessary expenditure to pay for subscription for attorneys from Department of Justice
3/25/2004	3557	PC Weekly	3	2, 4	RAD Trust	34.97	PC magazine annual subscription	Wasteful expenditure with little or no benefit to the estates
5/19/2004	3621	Association of Certified Fraud Examiners	4	2, 4	RAD Trust	120.00	annual dues--certified fraud examiner for Alex Spencer	Wasteful expenditure for estates paying for certification dues for DOI employee and DOI does not pay for certifications

**APPENDIX D  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--MISCELLANEOUS ITEMS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
10/20/2004	3797	The Wall Street Journal	4	2, 4	RAD Trust	\$ 319.00	two year subscription, "used by estates for stock pricing"	Unnecessary expenditure when stock information and business news available for free online
12/21/2004	3869	Lawyers Weekly	4	2, 4	RAD Trust	294.25	annual subscription for Clem Peterson (DOJ attorney)	Unnecessary expenditure to pay for subscription for attorneys from Department of Justice
5/18/2005	4102	Robert Half Finance & Accounting	6	2, 4	RAD Trust	13,000.00	candidate placement fee for RAD Trust controller position	Unreasonable amount to pay for employee search
6/4/2004	3639	BB&T Bankcard--Barnes&Noble, CTIA exam	2, 3	2, 4	RAD Trust	223.14	study guide for CompTIA exam(\$48.14), CompTIA exam (security+ certification) for Gene Lay (\$175)	Unnecessary expense with little benefit to estate to pay for certification examinations for DOI employees
10/9/2003	3286	BB&T-VISA--Legacy Center		2, 4	RAD Trust	2,480.00	training for Gene Lay, Ashby Spratley, and Laura Beasley for self-esteem training	Lack of benefit for estates, Unreasonable cost for training for almost \$1,000 per employee
12/3/2003	3397	BB&T-VISA--Legacy Center	3	2, 4	RAD Trust	995.00	training for Gene Lay	Lack of benefit for estates, Unreasonable cost for training for almost \$1,000 per employee
3/9/2004	3544	BB&T Bankcard--www.element5info.com, Hotwire	5	2, 4	RAD Trust	2,531.25	What's Up Gold Seminar in New Orleans for William Ditenhafer (\$1,788.25), airfare for trip (\$743)	Unreasonable cost for training in excess of \$2,000 for one employee
10/1/2002	720042	Consulting Services--Tom Frommelt	3	5	London Pacific	3,280.00	invoice for work performed prior to receivership changed dates to allow payment rather than being classified as "class 5"	Invoice dates altered to avoid rules regarding payments to vendors
12/23/2003	890696	Global Software, Inc	5	3	London Pacific	1,500.00	one day of technical service to assist with installation of spreadsheet server application	Unreasonable charge for one day of assistance

**APPENDIX D  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--MISCELLANEOUS ITEMS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
1/12/2004	7034	Bank of America-- Visa--Citrix System, Staples, Handspring, Inc., Covad.net	3, 5	3	London Pacific	\$ 1,677.13	"downloaded course materials" (\$150), Quick Books "for RAD Trust Accounting"(\$278.14), case for William's phone (\$29.99), no documentation for Covad.net (\$619), Caseman computer carrying case (\$600)	Insufficient documentation for course materials, estate should not directly pay entire cost for software for RAD Trust, items paid with inadequate documentation to support payments, wasteful expense for computer shipping case when RAD Trust already purchased one
5/20/2004	7371	Bank of America-- Visa--CTIA Exam	5	2	London Pacific	175.00	security certification exam for William Ditenhafer	Unnecessary expense to pay for certification examination for employee
3/29/2004	7213	Bank of America-- Visa-- Paypal/Artfires		3	London Pacific	40.45	weather radio (\$40.45) purchased through paypal	Unnecessary purchase
3/7/2005	8087	Rodney Calles	5, 7	2	London Pacific	143.94	cellular phone for LP employee (5 months before LP operations shut down)	Wasteful purchase to buy new cell phone for employee 5 months before closing of estate operations

Total	\$30,033.22
RAD Trust	\$23,216.70
London Pacific	\$6,816.52

- Legend
- 1 former Senior Deputy Commissioner
  - 2 current Senior Deputy Commissioner
  - 3 former RAD Trust director
  - 4 current Deputy Commissioner for Financial Analysis
  - 5 current examiner-in-charge of London Pacific estate
  - 6 acting RAD Trust controller
  - 7 current DOI applications analyst programmer

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**APPENDIX E**  
**DEPARTMENT OF INSURANCE--RAD TRUST**  
**QUESTIONED COSTS--LACK OF BIDS, QUOTES, AND/OR PURCHASE ORDERS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
8/6/2002	2612	BB&T-VISA--Paypal	1, 3	1, 2	RAD Trust	\$ 1,373.94	Compaq hard drives (\$342, \$378, \$290, \$275.45), model (\$88.49) purchased through ebay paid through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes
9/5/2002	2648	BB&T-VISA--Paypal	3	1, 2	RAD Trust	426.00	Compaq controller card for 360 server purchased through ebay paid through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes
3/13/2003	2886	BB&T-VISA--Paypal	1, 3, 4	1, 2	RAD Trust	7,162.00	3 Compaq 360 servers for London Pacific (\$7,010) purchased through ebay and paid through paypal, Compaq replacement hard drive for server purchased through ebay paid through paypal (\$152)	Non-compliance with procedures by buying items through ebay without bids or quotes
4/2/2003	2956	BB&T--VISA--PayPal	3	1, 2	RAD Trust	126.00	spare Compaq disk drive for server purchased through ebay and paid through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes
4/30/2003	3033	BB&T-VISA--Paypal	3, 4	2, 3	RAD Trust	314.00	compaq disk drive for server purchased through ebay and paid through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes
5/5/2003	3041	BB&T	2, 3	2, 3	RAD Trust	1,028.00	switch for LAN purchased through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes
5/28/2003	3083	BB&T--VISA--PayPal	3, 4	2, 3	RAD Trust	630.00	two Compaq spare drivers for LP server purchased through ebay/paypal	Non-compliance with procedures by buying items through ebay without bids or quotes
8/4/2003	elec pymt	Gene Lay	2	electronic pymt	RAD Trust	352.62	reimbursement for "extreme switch power unit inadvertently charged to personal account" purchased through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes

**APPENDIX E  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--LACK OF BIDS, QUOTES, AND/OR PURCHASE ORDERS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
11/26/2003	3394	Gene Lay	2	electronic pymt	RAD Trust	\$ 319.99	backup laser printer for London Pacific Sacramento office purchased through ebay with personal credit card through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
1/9/2003	806509	Gene Lay--CyberPower	5	5	London Pacific	1,720.69	server (\$557) and backup power supply (\$1,163.69) purchased through ebay on personal credit card	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
1/17/2003	808734	Gene Lay--CyberPower	5	3	London Pacific	289.33	server purchased through ebay on personal credit card	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
1/28/2003	810716	Trip Sanders		3	London Pacific	6,950.00	3 Compaq DL-360 servers purchased through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
4/16/2003	8282549	The Gallery	5	3	London Pacific	2,425.00	Compaq DL360 server with hard drives, CD rom drives, ethernet ports purchased through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
4/24/2003	831152	The Gallery	5	3	London Pacific	4,420.00	DL360 backup server and shipping purchased through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
6/2/2003	838995	Bank of America--IBM, Hello Direct Inc, Moredirect.com	5	3	London Pacific	17,593.92	purchases of laptop computers, hard drives, headsets, parts without purchase orders or invoices, items ordered through ebay	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order

**APPENDIX E  
DEPARTMENT OF INSURANCE--RAD TRUST  
QUESTIONED COSTS--LACK OF BIDS, QUOTES, AND/OR PURCHASE ORDERS**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
12/4/2003	883893	Bank of America-PayPal	5	3	London Pacific	\$ 281.20	replacement PDA for William Ditenhafer purchased on ebay (\$281.20)	Non-compliance with procedures by buying items through ebay without bids or quotes and without purchase order
12/19/2004	889101	Bank of America-Paypal	5	3	London Pacific	137.04	handsfree device ordered through ebay (\$22.08), shipping for software ordered through ebay (\$89.98), phone docking cradle ordered through ebay (\$24.98)	Non-compliance with procedures by buying items through ebay without bids or quotes
3/29/2004	7213	Bank of America--Visa--Paypal/Artfires		3	London Pacific	40.45	weather radio purchased through paypal	Non-compliance with procedures by buying items through ebay without bids or quotes

Purchases without bids and/or quotes \$45,590.18  
Purchases without purchase order \$34,000.13

- Legend
- 1 former Senior Deputy Commissioner
  - 2 current Senior Deputy Commissioner
  - 3 former RAD Trust director
  - 4 current Deputy Commissioner for Financial Analysis
  - 5 current examiner-in-charge of London Pacific estate



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**APPENDIX F**  
**DEPARTMENT OF INSURANCE--RAD TRUST**  
**QUESTIONED COSTS--OTHER INADEQUATE DOCUMENTATION**

DATE	CHECK #	PAYEE	APPROVED BY	CHECK SIGNED BY	FROM ACCOUNT	QUESTIONED AMOUNT	DESCRIPTION	AUDIT QUESTION/ ISSUE/ CONCERN
7/25/2003	851181	Bank of America--Techskills.com, Veritas Software Corp	2	1	London Pacific	\$ 8,584.00	no documentation for charges, nothing for charge to Techskills.com (\$8,495), handwritten note from William Ditenhafer for Veritas Software Corp (\$89)	Improper business practices paying for items with inadequate supporting documentation
8/29/2003	859087	Bank of America--Mail Boxes Etc, Budget Rent-A-Car, Chevron, Handspring Inc	2	1	London Pacific	1,095.96	no documentation for charges, lack of documentation questioned by "Pat" but notation by someone "go ahead and pay"	Improper business practices paying for items with inadequate supporting documentation
11/6/2003	875920	Bank of America--Dell, CyberPower, PayPal	2	1	London Pacific	1,130.27	no documentation for charges to Dell (\$1,004.67), CyberPower (\$85), and Paypal (\$40.60), notation on sticky note that "no documentation for certain purchases"	Improper business practices paying for items with inadequate supporting documentation
12/4/2003	883893	Bank of America--Avis, Pacific Neon	2	1	London Pacific	2,143.34	auto rental in Sacramento without receipt (\$323.34), sign removal in Sacramento without receipt (\$1,820)	Improper business practices paying for items with inadequate supporting documentation
1/12/2004	7034	Bank of America--Visa--Covad.net	1, 2	1	London Pacific	619.00	no documentation for Covad.net	Improper business practices paying for items with inadequate supporting documentation

Total \$ 13,572.57

Legend

- 1 former RAD Trust director
- 2 current examiner-in-charge of London Pacific estate

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**DEPARTMENT OF INSURANCE**  
**State of North Carolina**

1201 MAIL SERVICE CENTER  
RALEIGH, N.C. 27699-1201

**JIM LONG**  
COMMISSIONER OF INSURANCE

(919) 733-3058

September 14, 2005

***Via Hand-Delivery***

The Honorable Leslie W. Merritt  
North Carolina State Auditor  
2 South Salisbury Street  
Raleigh, North Carolina 27699-0601

Dear Mr. Auditor:

Thank you for providing me with the opportunity to respond to the special review report of the Regulatory Actions Division Trust (RAD Trust).

I appreciate all of your efforts in responding to my request for an outside independent review of the operations of RAD Trust. You and your staff have been extremely thorough and professional throughout this review.

Prior to and during the special review, the receivership staff has made numerous improvements to the operations of RAD Trust. These improvements include, but are not limited to, the following: tightening the policies and procedures for purchase and contracting, the filing of quarterly reports for RAD Trust with Superior Court, elimination of all purchases of surplus items by employees, changes in business procedures for obtaining computer services, obtaining Council of State approval of the sublease between RAD Trust and DOI, strengthening inventory procedures, and reallocation of certain expenses between DOI and RAD Trust where appropriate.

The receivership staff and I will make full use of your findings and recommendations to continue to improve the operations of RAD Trust. The receivership staff is striving and will continue to strive to better mirror state procedures while effectively and professionally accomplishing the difficult business task of managing, operating and liquidating insurance companies.

Further reduction of expenditures for insurance companies in receivership has been and continues to be a top priority.

In the Estate of London Pacific Life and Annuity Company, the receivership staff reduced company general expenses from \$21.6 million incurred by the company in 2001 prior to the receivership to \$6.8 million by 2003 and a further reduction to \$5.6 million in 2004. While receivership staff reduced expenses for London Pacific by \$15.9 million prior to selling off the majority of the insurance business of this \$1.8 billion company, further expense cutting can and will be done.

Even though expenditures for meals while negotiating business deals, continuation of London Pacific's provision of soft drinks for its employees, and providing food and other morale builders for existing mission-essential insurance company employees may not be unusual expenses for this \$1.8 billion company, these private business practices can be changed. Consequently, I have directed receivership employees to eliminate non-essential expenditures, large and small, and I am requiring increased documentation of the business purposes of all RAD Trust and receivership expenditures.

While I hold myself and the receivership staff to a higher standard, it should be noted that the concept that the receiver/liquidator is legally separate from the State and stands in the shoes of the insolvent insurance company is not novel to North Carolina, is not novel in insurance company liquidation and is not novel in the law.

Motions litigation in a recent New York case illustrates this. See 2005 NY Slip Op 25319, 2005 N.Y. Misc. Lexis 1618. In that case, the Superintendent of the New York State Insurance Department and employees of the New York Liquidation Bureau moved to quash subpoenas from the New York Comptroller to audit the Liquidation Bureau. The Trial Court granted the motion to quash on the extent that the subpoenas were overly broad, and the Court ruled that the Superintendent as Liquidator occupies "a legal personality separate and distinct" from the position of the public official charged with regulating the insurance industry generally.

While I respectfully reserve the legal position that my role as Receiver, Liquidator and RAD Trust Grantor is legally separate and distinct from my general state duties as Insurance Commissioner, I have voluntarily chosen a different and stricter practical course for RAD Trust and the receivership staff. I am committed to the concept that receivership operations should operate in accordance with the highest standards of not just the business world, but also of state government.

It is out of this commitment that I personally invited the State Auditor in to audit RAD Trust, and it is out of this commitment I have already directed and will continue to direct RAD Trust and the receivership staff to make RAD Trust operations more consistent with the operations of state government and to further improve RAD Trust operations.

I thank you for all of your assistance in this matter.

With kindest regards, I am

Very truly yours,

A handwritten signature in black ink that reads "Jim Long". The signature is written in a cursive, flowing style.

Jim Long

Commissioner of Insurance

JL:tb

## DISTRIBUTION OF AUDIT REPORT

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In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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The Honorable Beverly M. Perdue	Lieutenant Governor of North Carolina
The Honorable Richard H. Moore	State Treasurer
The Honorable Roy A. Cooper, III	Attorney General
Mr. David T. McCoy	State Budget Officer
Mr. Robert L. Powell	State Controller
Mr. James E. Long	Commissioner of Insurance

### LEGISLATIVE BRANCH

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	Representative Douglas Y. Yongue

### Other Legislative Officials

Mr. James D. Johnson	Director, Fiscal Research Division
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September 19, 2005

## ORDERING INFORMATION

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Copies of this report may be obtained by contacting the:

Office of the State Auditor  
State of North Carolina  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0601

Internet: <http://www.ncauditor.net>

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Facsimile: 919/807-7647