OFFICE OF THE NATIONAL PUBLIC AUDITOR

FEDERATED STATES OF MICRONESIA

AUDIT OF TELECOM CREDIT CARD USAGE

REPORT NO. 2010-04

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National Public Auditor
February 24, 2010

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February 24, 2010

His Excellency Manny Mori, FSM President
The Honorable Members of the FSM Congress

RE: Audit of Telecom Credit Card Use

We have completed an audit of the Federated States of Micronesia Telecommunications Corporation's (Telecom) credit card use. Our audit was conducted to achieve four objectives:

1. To determine if Telecom had developed appropriate policies and procedures regarding credit card use;
2. To determine if Telecom's practices adhered to its written policies and procedures;
3. To determine the extent to which credit cards were used for personal use and, if so, whether Telecom incurred any expenses as a result; and
4. To determine if credit card use was consistent with the operating objectives of Telecom.

Telecom had established a credit card policy governing use of corporate credit cards. The policy limits card use to expenses authorized by approved travel authorizations. Telecom's policy includes a clause stating that "unauthorized charges must be reimbursed within 30 days," to accommodate emergencies that may sometimes arise while traveling. The policy also limits card use to the corporate officers.

A review of Telecom's credit card statements and other documentation revealed that Telecom did not adhere to its policy. Credit cards were used for items ranging from travel expenses to representation to personal expenses to items purchased over the internet. Additionally, usage was not limited to the corporate officers. The Executive Secretary was often given the task of making travel and other internet purchases for management, employees and the Board of Directors. Concern that controls were not sufficient to prevent unauthorized use of the credit cards is discussed in the audit report. The report also notes that the policy should be updated to reflect change in practice.

The audit found that personal use of the credit cards routinely occurred. Inclusion in the credit card policy of the clause stating "unauthorized charges must be reimbursed within 30days" may have contributed to the lax environment regarding credit card use. Telecom's executives charged over $27,000 of personal items during the audit period of October 2006 through May 2009. Because Telecom did not always retain receipts or invoices for charges, the audit team could not verify whether 80 transactions totaling 25,697 dollars for airfare, hotels, restaurants, and other miscellaneous charges were business-related or personal.

Over $7,000 of the $27,000 in personal charges was owed as of May 2009. $3,600 of the $7,000 was aged more than 240 days. As a result, Telecom has incurred interest charges resulting from the personal use. In total, Telecom has incurred $2,294 in interest charges and late fees though the audit team could not segregate fees and charges resulting from personal use of the cards from those resulting from business use of the cards.

Telecom's enabling legislation states that Telecom is to operate solely for the benefit of the public and can only incur indebtedness for the purpose of expanding and improving telecommunications facilities. Analysis of the credit card statements revealed that in 23 of 32 months tested one officer spent more than $1,000 a month hosting dinners and that many of these dinners exceeded $500. Though, the meals and entertainment were within the Board-approved representation budget, these meals can be considered excessive given that Telecom is a component unit of the national government and is bound by the statutory limitations discussed above. Therefore, the audit report questions the necessity and appropriateness of these meals. The audit report recommends that the Board adapt a policy governing the use of representation funds.

The audit report also discusses concern that Telecom incurred excessive expenses when taxis were used by the executives for personal errands. The report cites one such trip to Honolulu during which over $200 was spent going to Costco, Ross, Home Depot and the zoo. The report recommends that the Board develop a policy regarding the use of the taxis. The report also recommends that the Board review the taxi charges incurred by Telecom and consider asking the executives to reimburse Telecom for any charges the Board finds to be inappropriate.

In discussing the conditions noted above, the report offers several recommendations concerning segregations of duties and other aspects of internal control.

The report was reviewed with Telecom's executive management team. The management team generally agreed with our findings and recommendations. Their written response to the audit report is included as an appendix.

Respectfully yours,

Haser Hainrick
National Public Auditor

XC: Vice President
Chairman & Members of the Telecom Board of Directors
Chief Executive Officer, Telecom
Chief Operating Officer, Telecom
Acting Chief Financial Officer, Telecom
Secretary, FSM Department of TC&I

Office of the National Public Auditor
Audit of Telecom Credit Card Usage
Report No. 2010-04

TABLE OF CONTENTS

Office of the National Public Auditor
Audit of FSM Telecom Credit Card Usage
Report No. 2010-04

INTRODUCTION

Background

The Federated States of Micronesia Telecommunications Corporation (hereafter referred to as Telecom) is an entity of the FSM national government responsible for the provision of telecommunication services throughout the FSM. Telecom operates as a tax-exempt entity. A six member Board of Directors (hereafter referred to as the Board) is responsible for overseeing the operations of the organization.

A Chief Executive Officer (CEO) who reports to the Board manages the operations of Telecom. In addition to the CEO, the executive management team consists of a Chief Financial Officer (CFO) and Chief Operating Officer (COO). The CEO, CFO, and COO are all provided with Telecom-issued credit cards.

The CFO resigned in March 2009 to accept a position with another national government entity, and the CFO's credit card was cancelled in the same month, March 2009. Telecom has been operating with the Senior Accountant as the acting CFO up to the date this report is issued.

In fiscal years 2007, 2008, and 2009 to May 31, a total of $366,963 was charged to the three credit cards. Table 1 below provides the annual expenditure by card.

Table 1
Annual Credit Card Expenditures by Card

Card Holder	Fiscal 2007	Fiscal 2008	Oct 2008 – May 2009	Period Tested Total Spent
CEO	$52,803	$93,440	$84,561	$230,804
COO	13,956	37,114	13,247	$64,317
CFO	24,492	24,802	22,549	$71,842
Totals	$91,251	$155,356	$120,357	$366,963

Source: Corporate Credit Card statements for months ended 10/28/06 – 5/28/09

The credit cards were used to purchase airline tickets for approximately 39 individuals plus the 3 executives, plus hotel accommodations, meals, training registration, association memberships, recurring items such as satellite phones monthly charges, representation, and incidentals such as computer equipment and software. Approximately 60% of the total spent was for purchases performed over the Internet by the Executive Secretary.

Objective, Scope and Methodology

Objective - The objectives of this audit were to:

1. Determine if Telecom had developed appropriate policies and procedures regarding credit card use.

2. Determine if Telecom's practices adhered to its written policies and procedures.
3. Determine the extent to which cards were used for personal use and, if so, whether Telecom incurred any expenses as a result.
4. Determine if credit card use was consistent with the operating objectives of Telecom.

Scope

This audit focused on Telecom credit charges incurred during fiscal years 2007, 2008 and 2009 through May. The audit scope was limited to credit card usage and Telecom's internal control process as it relates to credit card usage and payment.

This audit was conducted pursuant to Title 55 of the FSM Code, Chapter 5, which states in part:

> *"The Public Auditor shall inspect and audit transactions, accounts, books, and other financial records of every branch, department, office, agency, board, commission, bureau, and statutory authority of the National Government and of other public legal entities, including, but not limited to, States, subdivisions thereof, and nonprofit organizations receiving public funds from the National Government."*

Methodology

The audit fieldwork was conducted at Telecom's headquarters in Kolonia, Pohnpei.

To determine if Telecom had appropriate policies and procedures regarding credit card use we analyzed Telecom policies and procedures and compared the results to recommended United States Office of the Inspector General (US OIG) best practices for federal agencies use of travel cards, and to US Internal Revenue Services requirements to which competitors of Telecom must comply.

To determine if Telecom has correctly implemented its policies, we performed a walkthrough of relevant processes with Telecom staff and reviewed credit card use and payment records.

To determine if credit cards were used for personal use, the audit team judgmentally selected a sample of expenditures for review. During the process walk-through, the audit team noted that incompatible key duties were being performed by one person and the account statements were not reconciled by an independent person. Due to this condition the audit team selected nearly all expenditures over $100 for testing from the credit card statements provided by Telecom, more than 600 individual charges.

To determine if credit card use was consistent with the operating objectives of Telecom the audit team analyzed the nature and purpose of the expenditures to determine whether they appeared to serve the business interests of Telecom. Telecom's enabling legislation, as found in Title 21 of the FSM Code, was used by the audit team to establish criteria for use in determining whether expenditures served the business interests of Telecom.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions.

Prior Audit Coverage and Referral

Telecom, as a component unit of the FSM national government, is included in the annual fiscal audit of FSM national government operations. That fiscal year 2008 audit, referred to as the single audit, was conducted by the firm Deloitte and Touche. The resulting management letter reported the following:

> *FSMTC credit cards were used for personal expenses*[1]

The auditors found that the personal charges were indicated as such and that an accounts receivable record indicated that the employee was being held liable for reimbursing Telecom the amount charged.

CONCLUSION

The audit team found that Telecom lacked proper oversight of operational activities related to credit card use. For example, though the Board approves a representation fund, no limitations are placed on the use of that fund (See Finding 1). Additionally, though the Board is responsible for setting policy, management engaged in and approved practices that did not conform to the established credit card policy (See Findings 2 and 3). Moreover, standard business practices (control activities) designed to prevent and detect fraud, waste, and abuse of corporate credit cards were not in place (See Findings 4 - 7). Furthermore, due to the lax control environment, Telecom incurred unnecessary expenses related to unnecessary credit card interest charges (See Findings 8).

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The findings are discussed in detail in the following pages.

[1] FY 2008 Single Audit Report Management Letter Section 1 Item 6, issued 12/19/08.

FINDINGS AND RECOMMENDATIONS

1. Corporate credit cards were used to pay for dining and entertainment that may be excessive.

In Title 21, Chapter 2 of the FSM code pertains to Telecom. Section 203 defines the corporation's powers and responsibilities. In listing responsibilities, per Item (8), the Corporation is:

> *To incur indebtedness for the purpose of expanding and improving telecommunications facilities, to the extent and on such terms as are deemed commercially reasonable by the Corporation.*

Additionally, Section 208 establishes that:

> *The Corporation shall exist and operate solely for the benefit of the public…"*

Based on those requirements, we would expect that Telecom's senior management would act in a fiscally prudent manner resulting in minimum expenditures for food/entertainment and that those expenses would only be incurred when necessary to expand and improve telecommunication facilities and services. Moreover, since Telecom is a local telecommunications provider, we would not expect large expenditures related to entertainment. While in the corporate world 'wining and dining' is an expected business practice for a sales-related organization trying to attract corporate customers, this does not apply to Telecom.

Instead, we found that Telecom's expenditures for meals and entertainment appeared to be excessive for a government owned entity. One officer had meals and entertainment exceeding $1,000 per month in 23 of the 32 months tested. In fiscal year 2008, the officer's card had charges for meals and entertainment exceeding $1,000 in 10 of the 12 months. See Table 2 below.

Table 2

10 Months in fiscal 2008 with meals and entertainment exceeding $1,000 each, to one officer's Corporate Credit Card

Months (Format: Statement End Date)	**Cost of Meals and Entertainment** (Items under $100 are not included)
10/28/2007	2,872.75
11/28/2007	1,530.51
1/28/2008	2,128.01
2/28/2008	3,631.55
3/28/2008	1,783.96
4/28/2008	1,193.97
6/28/2008	2,181.50
7/28/2008	3,007.31
8/28/2008	2,403.33
9/28/2008	2,790.03

Source: Telecom Corporate Credit Card #XX40, statement dates 10/28/2007 through 9/28/2008

Table 3 below presents the credit card meals and entertainment activity for a representative month (8/29/08-9/29/08).

Table 3

One month of meals and entertainment

Trans Date	Description	Amount
8/29/08	PCR Hotel & Restaurant	$717.25
9/04/08	PCR Hotel & Restaurant	$164.50
9/13/08	Hy's Steakhouse (Guam)	$678.63
9/13/08	Michikusa Club	$80.00
9/13/08	New Evergreen Lounge	$650.00
9/14/08	AJI Ichi Japanese Restaurant	$79.50
9/15/08	Hyatt Regency Restaurant	$345.70
9/18/08	Hilton Resort Restaurant	$233.95

Source: Telecom Corporate Credit Card #XX40, statement closing date 9/28/08

We found that on 41 occasions between October 2006 and April 2009, executives charged meals that each exceeded $500.00. While board members and employees should, at times, be treated to a nice meal or reception as a show of gratitude, some items appeared to be excessive for an agent of the government tasked with the purpose of providing a necessary service to the citizens of the FSM. For example, a dinner for the Telecom Board of Directors in Kosrae during the month of March 2008 cost $1,100.00. In February 2009 a dinner for Telecom department and state managers cost $904.00

The 41 meals/entertainment charges exceeded $500 are listed in table 4 below

Table 4

Meals and entertainment exceeding $500 each

Reff	Transaction Date	Restaurant	Amount	Noted By Management
1	4/14/2009	PCR Restaurant	596.25	Dinner w/Tyco, DRG & Calpac Reps
2	3/10/2009	PCR Restaurant	641.50	Dinner w/Board of Directors
3	2/11/2009	PCR Restaurant	904.00	Dinner w/Dept & State Managers
4	12/9/2008	PCR Rest	634.50	Dinner/Board, Management & staff
5	10/9/2008	Sushi Taro	642.90	Dinner w/FSM Amb & Staff
6	9/29/2008	Village	577.10	Dinner w/ADC Reps
7	8/29/2008	PCR Rest	717.25	Reception hosted for Huawei Rep & Cutover Team
8	9/13/2008	Hy's Streakhouse	678.63	Dinner w/AMD Reps & B. Chairman-Guam
9	9/13/2008	New Ever Lounge	650.00	Drinks w/AMD Reps & B. Chairman-Guam
10	8/12/2008	Truk Stop	1,095.68	Reception for all employees of Chuuk
11	8/9/2008	Truk Stop	680.92	Dinner w/key staff of Chuuk office
12	7/3/2008	PCR Rest	767.50	Dinner w/NTA Reps.
13	7/12/2008	Sorabol Rest	535.00	Dinner w/ Special Advisor on Catholic Education
14	6/6/2008	Village	848.00	Dinner w/AMD Reps
15	5/29/2008	PCR Rest	703.50	Dinner w/Huawei Rep & Trainees

Reff	Transaction Date	Restaurant	Amount	Noted By Management
16	6/10/2008	Oceanview Rest	630.00	Dinner hosted for Board of Directors
17	3/11/2008	Kosrae Nautilus	1,099.89	Dinner w/Board of Directors
18	2/24/2008	PCR Rest	1,039.50	Reception for annual retreat attendees
19	2/15/2008	PCR Rest	1,028.25	Reception for Huawai Training Graduates
20	2/1/2008	PCR Rest	765.50	Dinner w/Huawei Trainer & Trainees-Grad
21	1/17/2008	Sorabol Rest	680.00	Dinner w/FSMTC Delegation
22	12/12/2007	Oceanview Rest	638.50	Dinner w/Board of Directors
23	11/23/2007	PCR Rest	728.00	Receiption for Huawei Rep. IN Tech Training
24	10/29/2007	PCR Rest	619.50	Reception - LGC Reps.
25	10/12/2007	PCR Rest	1,407.50	Reception hosted for Huawei Trainers & Trainee
26	8/28/2007	Oceanview Rest	748.75	Dinner w/Leyong, Marketing staff & P&E
27	8/30/2007	PCR Rest	528.00	Dinner w/ Consultant in Fiber Optic and RUS
28	8/3/2007	PCR Rest	761.50	Welcome reception for new IT Manager
29	8/21/2007	PCR Rest	729.00	Dinner w/Huawei Installation team
30	7/26/2007	PCR Rest	615.00	Dinner w/Huawei Reps
31	7/30/2007	PCR Rest	510.00	Dinner w/Huawei Reps
32	7/7/2007	Hy's Streakhouse	543.38	Representation
33	5/21/2007	PCR Rest	688.50	Dinner w/Wind Generator Rep & Mr. Vocea
34	4/10/2007	PCR Rest	928.00	Reception for NEC System Training Participants
35	3/27/2007	Oceanview Rest	522.25	Dinner w/Huawei Rep
36	2/13/2007	PCR Rest	1,028.00	Dinner hosted for retreat participants
37	2/10/2007	PCR Rest	821.25	Dinnerw/Huawei Reps & State Managers
38	12/18/2006	PCR Rest	649.00	Dinner w/Board of Directors
39	12/10/2006	Steak House	538.34	Dinner w/Cygnus Mill Reps
40	10/12/2006	Village	687.25	Dinner w/Cordell Rep & Trainees
41	10/9/2006	Truk Stop	544.69	Dinner w/AMD F-Tech, Kikukawa & FSMTC Reps

Source: Telecom Corporate Credit Card #XX40 statements for 10/28/2006 through 5/28/2009, receipts and notations attached to payment requests.

Cause and Recommendation

The use of credit cards to purchase expensive meals can be attributed to a corporate environment that allowed for fine dining and entertainment. The Board did not establish any limitations on the use of representation funds. Though the Board approves an annual budget for representation[2], it does not establish any guidelines or policies regarding use of those funds. As a result, management was not restricted in the use of representation funds.

We recommend that a policy be developed, reviewed and approved by the Board that specifies the appropriate guidelines and rules to govern the expenditure of representation funds.

[2] In 2009 the Board approved a representation budget of $25,000.

2. The executives did not comply with Telecom's Credit Card Policy regarding unauthorized charges

Telecom's established credit card policy limits credit card usage to items and amounts authorized on the travel authorization (TA). The policy also includes a clause stating "unauthorized charges must be reimbursed within 30 days."

The audit team found that the organization did not adhere to its credit card usage policy. Specifically:

- All 3 Officers used the Corporate Credit Cards for personal charges throughout the time period tested. See Table 5 below.

Table 5

Summary of personal charges to the corporate credit card by each Officer, for the audit test period of 10/01/06 through 5/28/09.

Card Holder	Personal Charges To Credit Card	Relative Proportion
CEO	$4,977	18%
COO	$18,219	66%
CFO	$4,502	16%
Total	$27,698	100%

Source: Corporate Credit Card statements for 10/28/2006 through 5/28/2009, secretary's inter-office memos, journals and ledger entries.

- The COO was allowed to make personal purchases beyond his ability to reimburse Telecom timely. The COO has a balance owing at May 31, 2009 exceeding $7,000 for personal expense, $3,600 aged more than 240 days. This does not include interest and late fees incurred by Telecom, nor interest for use of Telecom funds (it should not be an interest free loan).
- The CEO did not always reimburse personal charges within 30 days.

Cause and Recommendation

Personal use of the corporate credit cards by the executives became accepted under the clause of "unauthorized charges must be reimbursed within 30 days."

We recommend the following:

1. The COO pay-off the amount owed plus interest for use of funds (240+ days), plus the incidental credit card charges paid by Telecom (for interest and penalty fees). If the COO is not in a position to pay in full within 30 days, then the COO should obtain alternative financing or provide a promissory note for Telecom's and his protection.
2. The policy for Corporate Credit Card Use be modified:

a. To dictate no personal use of the cards, but to include a clause for "emergency use" under certain, specified circumstances and to include repayment requirements under such events.
b. To include a clause stating card privileges will be cancelled if it is not used according to policy.

3. The executives did not comply with the Credit Card Policy that states in capital letters "THE CARD USERS ARE LIMITED ONLY TO THE CORPORATE OFFICERS." (Capital letters were used in the policy only for this particular clause).

Though the policy very explicitly limits use of the credit cards the corporate officers, the audit team found that the card was also used by the ES and for individuals other than the officers. Specifically:

- The CEO Credit Card was used to purchase airfare for approximately 28 other individuals amounting to $58,131 or more, plus costs of related travel arrangements. See Table 6.
- The COO Credit Card was used to purchase airfare for approximately 2 other individuals amounting to $2,785 or more, plus costs of related travel arrangements. See Table 6.
- The CFO Credit Card was used to purchase airfare for approximately 9 other individuals amounting to $9,227 or more, plus other items. See Table 6.
- Airfare, hotels, training registration and other items were generally purchased by the Executive Secretary (ES), and charged to the Corporate Credit Cards using the Internet. See Table 6.

Table 6

Summary of airfare charges to the corporate credit cards, listed by account charged, for the audit test period of 10/01/06 through 5/28/09.

Credit Card	Card Holder Airfare	Employees & Board Airfare	Individuals (Emp & Bd)	Unknown Airfare
CEO	$14,999	$58,131	28	$4,665
COO	25,455	2,785	2	
CFO	3,657	9,227	9	
Total	$44,111	$70,143		$4,665

Source: Corporate Credit Card statements for months ended 10/28/06 – 5/28/09, travel authorizations, purchase records.

Cause and Recommendation

In prior years Telecom made travel arrangements through the local travel agencies. An executive decision was made to purchase travel arrangements internally using the Internet in order to eliminate the expense of travel agency service charges . This function, along with credit card privileges, was tasked to the Executive Secretary (ES). This was an executive decision, that overrode the policy limiting credit card use specifically to the Corporate Officers. Travel arrangements, training registrations and other items were purchased by the ES on behalf of approximately 39 different individuals plus the 3 executives. This action bypassed the established control framework, resulting in the conditions described throughout this report.

Policy and procedures understandably should evolve with changes in the business climate including adding the practical use of emerging technologies, but should follow a formal process of good governance.

We recommend the following:

1. Officers must not override existing policy and procedure. Instead, Officers should propose modifications and new policy, along with new controls (procedures) to the Board of Directors for consideration and approval.
2. Management should consider expanding and further developing its governance framework by defining more specifically tools for:
    a. Policy and procedure adjustments and improvements.
    b. Values, principles, and ethics education, reinforcement and monitoring.

4. Audit staff could not verify the legitimacy of $41,528 charged to corporate credit cards.

Funds are required to be expended in a manner that adheres to the FSM Code as well as the organization's policies and procedures. Additionally, it is expected that Telecom will conform to standard business practices. Specifically, credit card expenditures should have been conducted in accordance with the following:

- Telecom Policy & Procedures state: Corporate Officers "must submit to the Accounts Payable Section copy of the Visa Voucher with supporting invoice(s) within 10 days after the trip is completed."
- Generally accepted business practices: All credit card charges should be supported by documentation sufficiently adequate to establish the charge as a legitimate, business expense.

However, the audit team found that executives do not always submit supporting documentation for purchases made with credit cards. Rather than require the submittal of the receipts, the organization's practice was to allow executives to indicate, upon inquiry, whether the purchase was for business or personal use.

As a result, the validity of 107 transactions totaling $41,528 could not be verified because Telecom did not have supporting documentation. Airfare, hotels, restaurants and miscellaneous comprising approximately 80 items totaling $25,697 could easily have been misused for personal benefit. Telecom paid many of these charges without evidence as to whether the charges either in sum or individually, were appropriate, accurate or valid.

Cause and Recommendation

The Officers did not submit credit card activity to the normal accounting functions. The Organization's practice was that the Executive Secretary (ES) would receive the credit card statements and give copies to the card-holders to label the charges that are personal. The ES would prepare an inter-office memo requesting Accounting to make payment, listing separately the credit card charges indicated to be business or personal, without receipts. The statement copies, with the executive's indication of business or personal, were discarded according to the ES and are no longer available.

We recommend all matters regarding credit card security, administration and accounting functions be given to the Accounting Department. The Accounting Department should be appropriately empowered to ensure or govern:

1. The appropriate use of credit cards for internet purchasing including implementation of security controls.
2. Appropriate, accurate recording of all activity posted to the credit card accounts by the Bank Credit Card Issuer.

5. Practices involving use of corporate credit cards for personal items created an environment that encouraged misuse.

An organization should have policies and procedures to mitigate the risk that a traveler may submit personal expenses as business expense.

Note: In March 2009, the Telecom Board of Directors declared that personal items may no longer be charged to the Corporate Credit Cards.

Telecom allowed corporate executives to use corporate credit cards for personal use and then submit reported expenses 'offset' to the personal charges. For example, if a traveler makes a $10 personal purchase on the corporate credit card and the traveler pays $10 in cash to a taxi driver then the charges 'offset' each other and the corporation would pay the $10 to the credit card and not pay the employee a $10 travel reimbursement. While the practice may be inherently logical, Telecom did not institute controls or limits to prevent abuse. The lack of controls may inherently encourage executives to submit falsified records in order to offset personal charges to the corporate credit cards.

Corporate executives claimed taxi fare expense, of which $6,139 were offset against the personal charges made to the Corporate Credit Cards. Moreover, many of these reported taxi trips were for personal trips to shopping malls, a few entertainment establishments, and other personal visits.

Table 7

Summary of cash expense with receipts and without receipts, credited or offset to personal charges, listed by credit card account for the audit test period of 10/01/06 through 5/28/09.

TABLE OF OFFSETS TO PERSONAL CHARGES				
	All Offsets[1]	**Offsets: Expenses With No Receipts[2]**		
Card Holder	**Total**	**Total**	**Taxi: All**	**Taxi To Malls, Shops, Medical, Entertainment & Residential Areas[3]**
CEO	$1,545	574	554	132
COO	$6,537	4,967	4,752	1,843
CFO	$946	946	833	459
Total	$9,028	$6,487	$6,139	$2,434

[1]All Offsets is the total amount applied as credit against personal charges. The "All Offsets" total is comprised of expenses with receipts and reported items with no receipts.
[2]Offsets with no receipts were primarily taxi service.
[3]This information is based on trip logs submitted by the executive. The trip logs appear to have been created at the same time for all entries, indicating the logs were prepared upon return to Pohnpei.

Source: subsidiary ledgers and travel vouchers for the test period of October 2006 through May 2009.

Telecom may have paid up to $9,028 in personal expenses incurred by its corporate officers during the audit period of October 2006 to May 2009. It is understandable that travelers may, on occasion, need to use taxis for personal business while away from home. However, trips were identified by the audit team during which the Telecom traveler did not appear to limit the use of taxis. For example, on one ten-day trip to Honolulu, the traveler spent $790 in cab fare, an average of $79 per day. On the day of arrival, the traveler took a taxi from the airport to the hotel and later that same day took a taxi from the hotel to Costco and back, took a second shopping trip to Ross and then back to the hotel, and lastly took a taxi from his hotel to the Waikiki Marriot and back. On subsequent days, the traveler's destinations included Home Depot, a second trip to Ross, the Waikiki zoo, etc. Additionally, each business day the traveler took taxis from the hotel he stayed at to the hotel the conference was being held at, in addition to nightly trips for dinner and/or entertainment. Appendix A contains the handwritten taxi log submitted by the traveler for a trip to Honolulu that began on January 10, 2007 and ended on January 19, 2007.

Cause and Recommendation

This condition was caused by lax control policies that did not limit allowable expenditures to business only. Telecom had no policy governing or limiting taxi use and therefore Telecom travelers were not required to limit their use of taxis. By contrast, the FSM national government Financial Management Regulations sets a $30 fixed allowance to offset costs such as taxis, phone calls, etc[3].

[3] FSM FMR 4.14 (g)

Additionally, travelers were allowed to submit handwritten logs of their taxi use without receipts and therefore there is no way to validate whether the trips actually occurred. Moreover, because common practice is for taxi drivers to hand travelers blank receipts (which were lacking), there is an inherent risk that travelers will submit falsified taxi receipts in order to increase the amount of reimbursement.

We recommend:

1. The CEO and Telecom Board should consider requiring travelers to reimburse Telecom for the personal use of taxi service for trips to malls, shops, medical appointments, entertainment, etc. that the CEO and Board determine exceed what they would expect a prudent traveler to incur. This should include expenditures that were:
   a. Used as offsets or credit against personal card charges. These items were submitted by travel voucher and used to offset against personal credit card charges.
   b. Reimbursed to the executives by check (versus offset against personal charges). These items were also submitted by travel voucher by the executives but were reimbursed by check. These are not included in the table of offsets above and are in addition to the $6,139.
2. Telecom establish a policy that sets limits both the acceptable uses for taxis and the dollar amounts that may be incurred and that requires the submittal of appropriate receipts and documentation of the business purpose.

6. The Credit Card Bank Account Activity was not reconciled and the outstanding liability (monthly statement ending balance) was not verified, not reconciled, and not accrued to the general ledger.

Credit card accounts must be monitored, transaction activity must be verified, and, ending balances must be reconciled to specific unpaid charges on a regular and frequent basis by someone not having purchase authority or knowledge of the secured credit card information. This is a key control against credit card abuse since unauthorized charges should be detected in a timely manner.

Title 21 of the FSM Code, Section 227 Accounts and Records states:

> *The Board and the chief executive officer shall be jointly responsible to ensure that the budget and finance officer prepares proper and complete books of account reflecting all income, expenses, assets, liabilities, capital, and retained earnings of the Corporation. Accounting for the Corporation shall be on the accrual basis…*

Additionally, the Telecom Corporate Credit Card Policy, procedure 7 relative to Accounts Payable, states: "Review the monthly statement for unpaid balances and immediately report any discrepancies to the Senior Accountant for resolution."

The audit team found that the Accounting Department did not receive, review, or reconcile the monthly statements. The Executive Secretary, who performs internet purchasing and requests payments, is the one who receives the monthly statements in conjunction with the daily mail. Copies of statements are not provided to Accounting.

As a result, charges were paid by Accounting without verifying agreement to the credit card account record. Specifically:

- Internet purchases, performed by the Executive Secretary (ES) and amounting to over 60% of the total amount spent were paid following purchase and were not reconciled to the actual charges on the statement of account.
- Charges for foreign currency purchases were systematically paid by Accounting at amounts different than the amounts posted to the account.
- Airfare charges amounting to $6,640.97 were cancelled by the ES and the payment (check #27764) was made following the cancellation. The payment for cancelled charges was not detected since Accounting processes payment without verifying to the credit card account and the ES did not advise Accounting of the cancellation.
- Charges were not identified as unpaid until the audit team inquired about items in our test sample for which supporting documents could not be found.

Additionally, as a result of the current process there is no assurance that payment amounts are for legitimate purchases. While it may seem inherently logical that the card holders would want all charges to be paid, in the absence of third party review (Accounting) to reconcile the account there is no assurance that charges were incurred. For example, Accounting could be asked to pay $1,000 towards the credit card balance in preparation for a $1,000 hotel stay that will be incurred. If the hotel stay were cancelled, the $1,000 payment would be applied to other charges which may or may not be legitimate business charges.

Cause and Recommendation

The Corporate Officers, the card-holders, overrode the existing Accounting Controls by limiting Accounting's role to making payments when (and in the amounts) requested to do so by the ES.

The executives did not comply with the procedure requiring supporting invoices be submitted for all charges, and a specific procedure for lost receipts was either not developed or not followed.

We recommended in finding 2 above that all matters regarding credit card accounting be given to the Accounting Department and that a Credit Card Administrator function be established and serve as the sole Telecom liaison with the credit card issuer.

We specifically recommend:

1. Transfer of responsibility for credit card administration to the Accounting Department.

2. Internet viewing of bank credit card account activity, inquiry access only and / or, initial receipt of the monthly statements with copies given to the card holders.
3. Reconciliation of charges paid or submitted for payment with the charges per the account statement.
4. Reconciliation of account month-end balance to charges not processed for payment (unverified charges).
5. Identification of charges-to-card not paid previously.
6. Identification of unauthorized charges, if any.

7. The Policy and Procedure does not specify the responsibilities, policies, and procedures necessary for individual card-holders and others who are charged with oversight.

In order to be effective, policies and procedures must state all elements expected and assign responsibility for the performance of:

- what constitutes complete and accurate records,
- mechanisms to ensure the integrity of purchases, for example card security, and
- consequences if policy and procedure is not followed including cancellation of card privileges and instead, use of alternative means such as travel advances only.

A review of the Telecom Credit Card Policy revealed that it does not specify:

- Credit Card security measures generally, and internet purchasing specifically.
- The type of information required of card holders for supporting documentation.
- Reconciliation and confirmation of all account activity (charges, payments, credits, fees)
- Consequences if policy and procedure are not followed**.**

Cause and Recommendation

The lack of adequate governance processes caused policies and procedures to stagnate. Management bypassed the prescribed policies and procedures instead of developing new policy and procedures.

We recommend management amend the Telecom Corporate Credit Card policies and procedures, to include**:**

1. Credit Card security measures generally, and internet purchasing specifically.
2. The specific type of information required of card holders, e.g., itemized receipts, explanatory card holder notes for the purchase, for example number of meals purchased or persons receiving, and the expected benefit to Telecom.
3. Consequences if policy and procedure is not followed including cancellation of card privileges and instead, use of alternative means, for example travel advances only.

8. Telecom incurred interest and late fees of $2,294 on personal and business charges not paid timely.

An organization should not unnecessarily incur interest charges and late fees. Moreover, the organization should not incur interest charges and late fees that result from personal use of the organizations credit card.

The audit team found that Telecom incurred $2,294 in unnecessary interest and late fees. However, the audit team could not determine the amount incurred for personal use since business and personal charges were commingled in the same months. See Table 9 below for interest and late fees on all charges (business and personal).

Table 9

Summary of interest and late fees charged, by dollar amount and number of months in which the fees were incurred, for the period tested of October 01, 2006 through May28, 2009, a total of 32 months.

Card Holder	Interest and Late Fees	Months (Of 32 Tested)
CEO	409	5
COO	1,347	26
CFO	688	15
Total	$2,294	N/A

Source: Corporate Credit Card statements for months ended 10/28/06 – 5/28/09

Whereas it is typical for an organization to receive a credit card statement and then make payment for the statement balance, Telecom's procedure is to make payments for specific purchases in the days following purchase prior to receiving the monthly statement. Specifically, internet purchases are in advance of travel and are paid within days of purchase, and travel vouchers are to be filed by the traveler within 10 days of return.

Hence, the interest charges and late fees were incurred when Telecom was not reimbursed on personal charges on a timely basis, when business charges (travel vouchers) were not submitted timely, and when charges were not identified as unpaid. Interest and late fees were incurred only when charges were not paid within 25 days of the credit card statement date.[4]

Cause and Recommendation

Though nonpayment or late payment of card charges resulted in interest and late fees, the ultimate cause was the lack of administrative oversight of credit card activity, lack of reconciliation to ensure

[4] The credit card accounts have a 25 day grace period following the statement close date.

timely and complete accounting of charges and payments. The executives used the credit cards without establishing the appropriate controls, without accountability.

Implementation of the recommendations described throughout this report will prevent unnecessary charges such as the interest and late fees noted in this finding. We reiterate the following:

Finding 2, Recommendations 1 and 2:
The COO pay-off the amount owed plus interest for use of funds (240+ days), plus the incidental credit card charges paid by Telecom (for interest and penalty fees). If the COO is not in a position to pay in full within 30 days, then the COO should obtain alternative financing or provide a promissory note for Telecom's and his protection.

Finding 6, Recommendations 3, 4 and 5:
- Reconciliation of charges paid or submitted for payment with the charges per the account statement.
- Reconciliation of account month-end balance to charges not processed for payment (unverified charges).
- Identification of charges-to-card not paid previously.

<u>APPENDIX A</u>, Page 1 of 2:

Example of Taxi Fare, this regards a trip to Honolulu during January 10-17, 2007

TAXI FARES (1)

1/10/07	Airport to Pagoda	$40.00
1/10/07	Pagoda to Costco & Back	40.00
1/10/07	Pagoda to Ross Downtown and Back	30.00
1/10/07	Pagoda to Waikiki Marriot and Back	30.00
1/11/07	Pagoda to Kelly O'Neil's and Back	20.00
1/11/07	Pagoda to Home Depot and Back	40.00
1/11/07	Pagoda to International Market and Back	30.00
1/12/07	Pagoda to Hilton Hotel and Back	20.00
1/12/07	Pagoda to Waikiki Zoo and Back	30.00
1/12/07	Pagoda to Palolo and Back	40.00
1/13/07	Pagoda to Hilton and Back (Twice)	40.00
1/13/07	Pagoda to International Market and Back	30.00
1/13/07	Pagoda to Kelly O'Neil's and Back	20.00
1/14/07	Pagoda to Hilton and Back (Twice)	40.00
1/14/07	Pagoda to Ross Downtown and Back	30.00

<u>APPENDIX A</u>, Page 2 of 2:
Example of Taxi Fare, a trip to Honolulu during January 10-17, 2007

(2)

1/14/07 PAGODA TO PALOLO AND BACK	30.00
1/15/07 PAGODA TO HILTON and BACK (TWICE)	40.00
1/15/07 PAGODA TO PALOLO AND BACK	30.00
1/16/07 PAGODA TO HILTON AND BACK	20.00
1/16/07 PAGODA TO MARRIOT AND BACK	30.00
1/17/07 PAGODA TO HILTON AND BACK	24.00
1/17/07 PAGODA TO INTERNATIONAL MARKET AND BACK	30.00
1/18/07 PAGODA TO COSCO AND BACK	40.00
1/18/07 PAGODA TO PALOLO AND BACK	30.00
1/19/07 PAGODA TO AIRPORT	40.00
TOTAL	$ 790.00

MANAGEMENT RESPONSE: Page 1 of 2

fsmtc
FSM Telecommunications Corporation

February 11, 2010

National Public Auditor
RECEIVED
Date 02/16/10

2.16.2010

Mr. Haser Hainrick
National Public Auditor
FSM National Government
Palikir, Pohnpei FM 96941

Re: Exit Conference – Telecom Credit Card

Dear Mr. Hairick:

This is to thank you and your audit team for having shared the draft of Report No. 2009-05 with the Management of FSMTC and for having made the changes agreed to on pages 1, 4, 5, 11 and 12.

As to the findings and recommendations, we offer the following comments:

1. We will work with our Board of Directors to develop guidelines and rules to govern representation funds.

2. All credit card charges by COO have been paid in full and Management will work closely with the Board on Corporate Credit Policy to reflect recommendation 2 on page 8 of the report.

3. Management will work on the adoption of recommendations 1 and 2 on page 9.

MANAGEMENT RESPONSE: Page 2 of 2

4. Management will work with the Accounting Department on the security measures cited on page 10.

5. Telecom will establish policy on ground transportation for people traveling on corporate business.

6. Management has noted the recommendations on page 13 and will work with the Accounting Department on appropriate measures to be implemented.

7. Similar to 6 above, management has noted the measures recommended.

8. We have taken note of finding #8 and pertinent recommendations and have taken appropriate measures to put these to rest.

If any clarification on this communication is required, do me know.

Sincerely yours,

Takuro Akinaga
President/CEO

Office of the National Public Auditor
Audit of FSM Telecom Credit Card Usage
Report No. 2010-04

NATIONAL PUBLIC AUDITOR'S COMMENTS

We would like to thank management and staff of FSM Telecom for their assistance and cooperation during the course of our audit.

The ONPA may perform a follow-up review within the next 9-12 months to ensure that Telecom has taken corrective measures to address all the findings and recommendations provided in this report.

In conformance with government auditing standards, we provided a copy of the draft report to the management of Telecom to provide a response to the audit. A reply was received from the CEO which did not indicate specific corrective actions to be taken of our findings and recommendations. We have printed his reply in the Management Response section of this report.

In addition to providing copies of this report to the President, Vice President and Members of the 16th Congress, we also sent copies to the following officials:

- All State Governors
- Chairman & Members of the Telecom Board of Directors
- Chief Executive Officer, Telecom
- Chief Operating Officer, Telecom
- Acting Chief Financial Officer, Telecom
- Secretary, FSM Department of TC&I

A copy of this report is posted on our website. Furthermore, we will make copies available to other interested parties on request.

If there are any questions or concerns regarding this report, please do not hesitate to contact the office. Contact information for the Office can be found on the last page of this report, along with the National Public Auditor and staff who made major contributions to this report.

Haser H. Hainrick
National Public Auditor

February 24, 2010

Office of the National Public Auditor
Audit of FSM Telecom Credit Card Usage
Report No. 2010-04

ONPA CONTACT AND STAFF ACKNOWLEDGEMENT

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ACKNOWLEGEMENTS	In addition to the contact named above, the following staff made key contributions to this report: Eric Spivak, CIA, Audit Manager Ron Sufficool, CPA, CIA, CFE, CISA, CMA Audit Supervisor Keller Phillip, Auditor-In-Charge Yolanda Leben, Auditor
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