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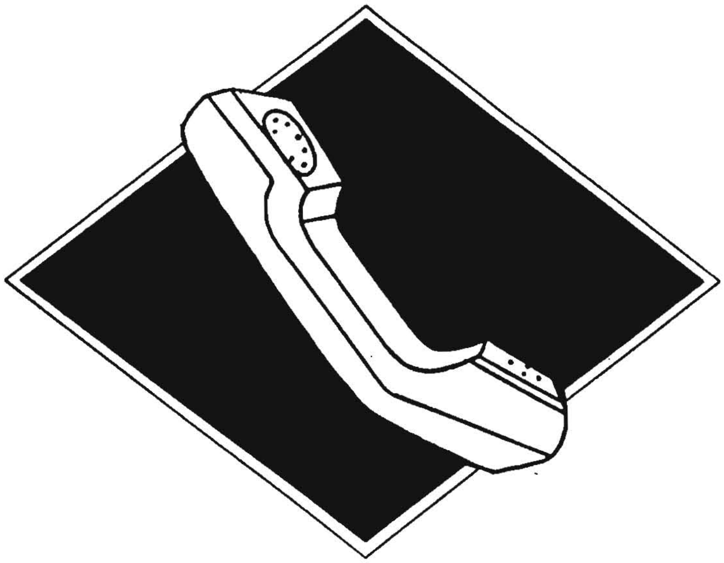

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SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY

NON-CONTACT SALES INCENTIVE PROGRAM CONTROLS

FEBRUARY 1993

By Authority of
The State of Florida for
The Public Service Commission
Division of Research and Regulatory Review

SOUTHERN BELL TELEPHONE AND TELEGRAPH COMPANY

[redacted]

NON-CONTACT SALES INCENTIVE PROGRAM CONTROLS

Carl Vinson, Project Manager
Management Review Specialist

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1.1 Background

This audit of Southern Bell's non-contact sales incentive programs was performed by the Division of Research and Regulatory Review, Bureau of Regulatory Review at the request of the Division of Communications. The purpose of the review was to assist in the investigation of Southern Bell's non-contact sales practices in Docket 900960-TL.

On December 6, 1990, in response to allegations of improper billing of Southern Bell customers, the Division of Communications requested a docket be established to initiate show cause proceedings against Southern Bell (the Company). In response, the Commission issued Order Number 24041, directing that no show cause order be issued at that time, but that an investigation be conducted to fully disclose the facts surrounding the allegations of improper billing. This order also required Southern Bell to file a weekly report reflecting the number and amount of refunds made to customers who were improperly billed for services they did not authorize.

In July 1991, the Company discontinued its non-contact sales incentive program, Goldline. Since that date, no other non-contact sales incentive programs have been implemented.

The Company's weekly refund reports to the Commission indicate that as of September 30, 1991, the Company had refunded over $800,000 to about 34,000 customers throughout the state. Since that date, the required weekly reports have provided no updates to this dollar amount, and the Company's response to Staff's Third Set of Interrogatories, Item 28, indicated that as of October 1992, the final refund totals were "not yet available."

In October 1992, through a settlement with the Office of Statewide Prosecution, the Company agreed to pay restitution of approximately $15,200,000 to more than 900,000 customers, and to revise billing practices and controls. Of this amount, Southern Bell agreed to pay $10,500,000 to customers who were billed for optional services as a result of the Company's non-contact sales programs, and $3,005,000 to customers who may have been denied rebates for service outages. The settlement stipulated that no admissions of wrongdoing or liability were made by the Company. The Advisory Opinion of the Tenth Statewide Grand Jury, noted that penalties for any such wrongdoing fall under the jurisdiction of the Public Service Commission.

1.2 Objectives

The primary objectives of this audit were to assess both the adequacy of the controls surrounding the Company's non-contact sales incentive programs and the adequacy of Management's response to control problems and violations. More specifically, Regulatory Review Staff sought to answer three key questions:

- Did Southern Bell provide adequate internal controls in its non-contact sales incentive programs to prevent the improper billing of customers?
- Did the actions or omissions of Southern Bell Management lead to the improper billing of customers?
- Has Southern Bell taken adequate steps to prevent the recurrence of improper billing of customers?

1.3 Scope

This audit focused on internal controls surrounding the Company's various non-contact sales incentive programs. These programs were intended to generate additional revenue through the sale of services by "non-contact" employees; those whose regular duties did not include sales. Since these programs were primarily targeted at the Network Department, the review was directed towards Network personnel and activities. However, the roles of other key groups involved in these sales incentive programs, such as the Customer Services Department, were examined as well.

The timeframe analyzed in this audit was the period 1985 through 1991, when Southern Bell Executive Management discontinued all non-contact sales programs. Since the Company sought to improve the controls surrounding non-contact sales programs during late 1989, the control changes implemented by the Company in 1990 became a point of specific focus.

1.4 Methodology

Information regarding non-contact sales program methods and controls was gathered through employee interviews, document requests, and formal discovery. Interviewed Company personnel represented a cross-section of management levels, staff support personnel and craft employees involved in non-contact sales programs.

The findings and conclusions summarized below were developed for consideration by the Division of Communications based upon analysis of the information examined. Where applicable, recommended improvements regarding any future resurrection of non-contact sales incentive programs by the Company are also presented in this report.

A draft of this report was provided to the Company to verify the factual accuracy of its contents. Based upon the Company's response, certain revisions were made to statements of fact. However, no changes to the intent of the findings or conclusions were made as a result of the Company's input.

1.5 Findings and Conclusions

Based upon analysis of the evidence obtained, the following findings and conclusions are presented. These conclusions provide responses to the three questions posed (in section 1.2) as the primary objectives of this audit. The findings and conclusions are discussed further in section 6.0 of this report.

Adequacy of Controls - 1990 and Prior

Conclusion 1: **Southern Bell did not provide adequate internal controls in its non-contact sales incentive programs to prevent or detect the improper billing of customers.**

Finding 1: **Controls Over Sales Referral Processing And Verification Were Inadequate.**

Finding 2: **Non-Contact Employees Received Little Training And Guidance In Proper Sales Methods.**

Finding 3: **Lack of Non-Contact Sales Internal Audits and Network Staff Reviews Hindered Detection Of Control Failures.**

Finding 4: **Procedures For Tracking Employee Time Spent In Non-Contact Sales Were Inadequate.**

Adequacy of Management's Response to Problems

Conclusion 2: **The actions and omissions of Network Department management led to the improper billing of customers.**

Finding 5: Management Did Not Investigate Evidence Of Improper Sales And Misbilling In A Timely Manner.

Finding 6: Management Did Not Improve Non-Contact Sales Controls In A Timely Manner.

Adequacy of Present Controls

Conclusion 3: **If Southern Bell resumes the use of a non-contact sales incentive program based upon Goldline, additional controls are needed to prevent the recurrence of improper billing of customers.**

2.0 NON-CONTACT SALES PROCESS OVERVIEW

2.0 NON-CONTACT SALES PROCESS OVERVIEW

2.1 *Purpose of Non-Contact Sales Incentive Programs*

Since the 1970's, Southern Bell has used incentive and recognition programs to generate additional revenues through sales of services by "non-contact employees". These employees, such as maintenance administrators and service technicians, perform functions that do not involve selling. However, the Company recognized that selling opportunities may arise in the course of performing many non-sales jobs. For example, while repairing a service outage, a service technician may discuss Southern Bell's inside wire maintenance plan with the customer, thereby generating a sale of this service and additional revenues. To reward these employees for the additional effort required, incentives were offered.

Initially, these incentives were of nominal value, such as coffee mugs for top sellers or a breakfast for the top-producing workgroup. By the mid-1980's, the potential value of incentive awards had greatly increased. Participating employees accumulated sales credit "points" which could be redeemed through a catalogue for prizes such as guns and wide-screen TV sets. Through a pyramidal scoring system, the top sellers' managers were able to earn catalogue merchandise or luxury cruises.

Although the value and level of sophistication of the incentives offered through the non-contact sales programs increased over time, the basic process and related internal controls changed little. In order to understand the controls surrounding non-contact sales programs, and the problems the Company eventually experienced, it is necessary to understand how these programs were developed, monitored and administered.

2.2 *Sales Incentive Program Guidelines*

Prior to 1987, the Atlanta-based I/M Operations Support Staff organization assisted the Florida Network Support Staff in the development of non-contact sales programs. After that date, the Florida IMC/I&M Support Staff (Network Staff) developed programs, which were approved by the Florida Network Vice-President and the Personnel Department. Exhibits 1 and 2 display the organizational relationships as of 1991 between the various groups involved in planning and participating in non-contact sales programs. Exhibit 3 displays the organization of the Florida Network Department and the various positions participating in non-contact sales programs.

Written program guidelines were required to include at a minimum the planned time frame (generally less than twelve months), a description of eligible employees, criteria for determining award recipients, a description of awards and awards distribution, and a budget

SOUTHERN BELL NETWORK ORGANIZATION
AS OF 1991

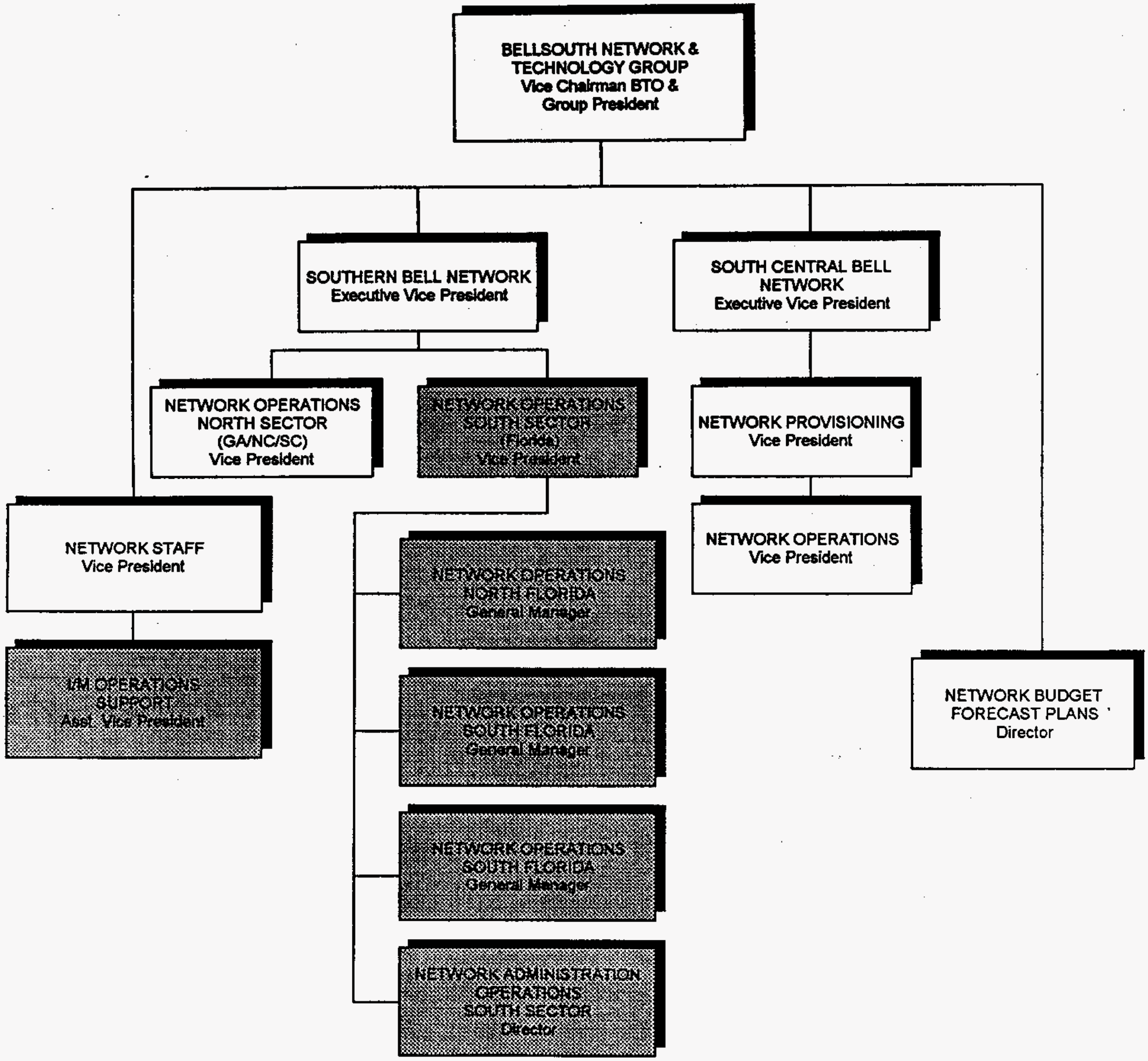


EXHIBIT 1 *SOURCE: COMPANY RECORDS*

NETWORK I/M OPERATIONS SUPPORT STAFF
AS OF 1991

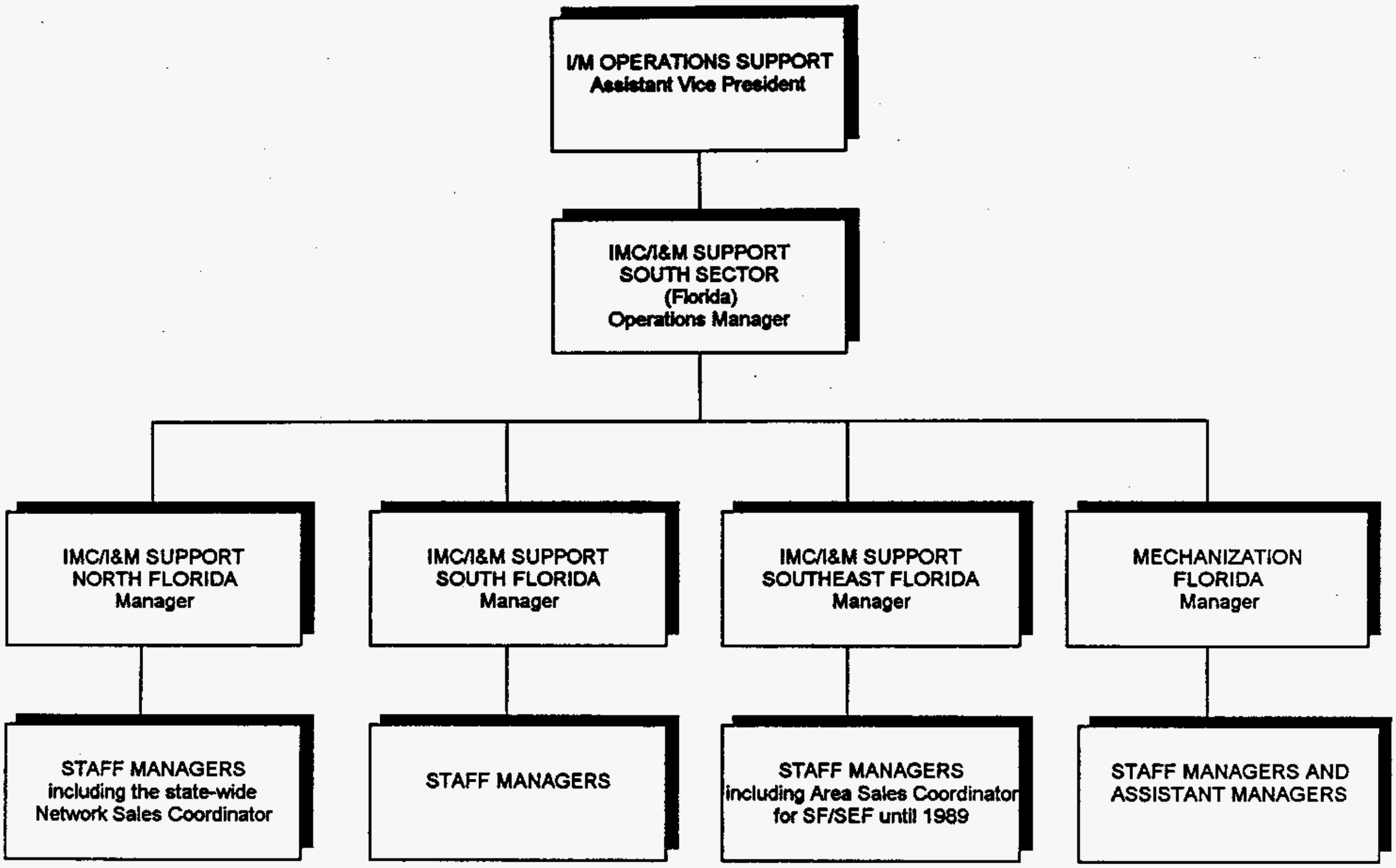


EXHIBIT 2 *SOURCE: COMPANY RECORDS*

SOUTHERN BELL OF FLORIDA
NETWORK REPORTING HIERARCHY
AS OF 1991

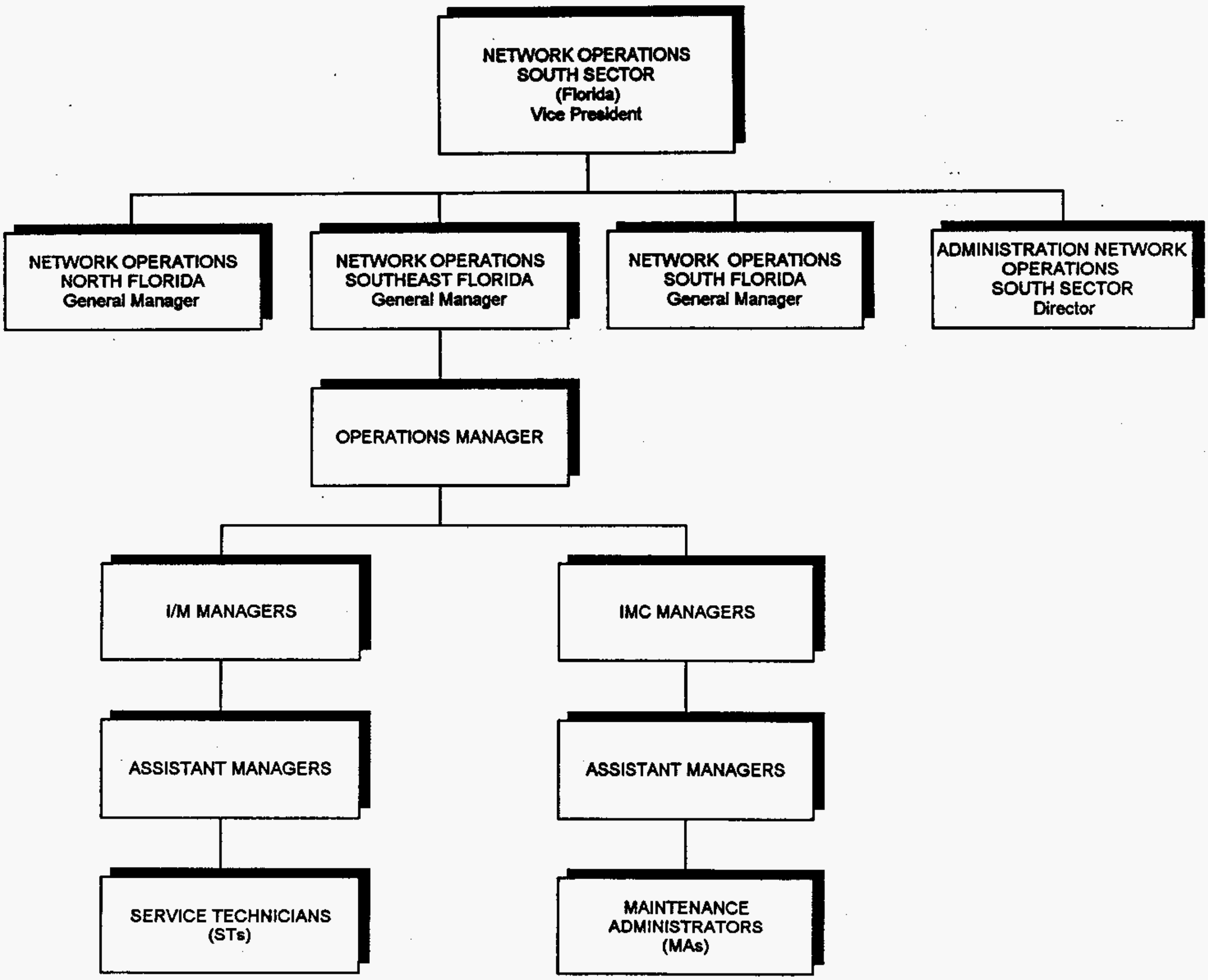


EXHIBIT 3

SOURCE: COMPANY RECORDS

providing total costs. Once developed, these guidelines were reviewed and approved by the Vice-President and the General Managers of the sponsoring department (e.g., Network), and by the Tax Office and Personnel Departments.

Exhibit 4 shows the non-contact sales incentive program planning and budgeting process for submitting non-contact sales programs as of 1988. Guidelines for the development of these programs were provided in Southern Bell's *Executive Instructions* and *Personnel Policy Manual*. Specifically, *Executive Instruction Number 4* addresses the general policy for incentive programs, including types and levels of awards, the responsibilities and roles of various departments and entities involved, and reports and controls.

Additional guidelines for the development of non-contact sales incentive programs were provided by the *Personnel Policy Manual*, Section 51.102, Employee Compensation Management and Non-Management Special Award Programs - Sales and Performance. This interdepartmental procedure further defined the necessary program criteria, departmental budget requirements, approval requirements, expense reporting and tracking forms, and types of award programs.

Sales incentive awards for non-contact sales employees were limited by the *Personnel Policy Manual* to .3% or less of the department's annual Management Salary Budget. The budget included base salaries, Management Team Incentive Awards, and Individual Incentive Awards.

2.3 Sales Referral Processing Methods

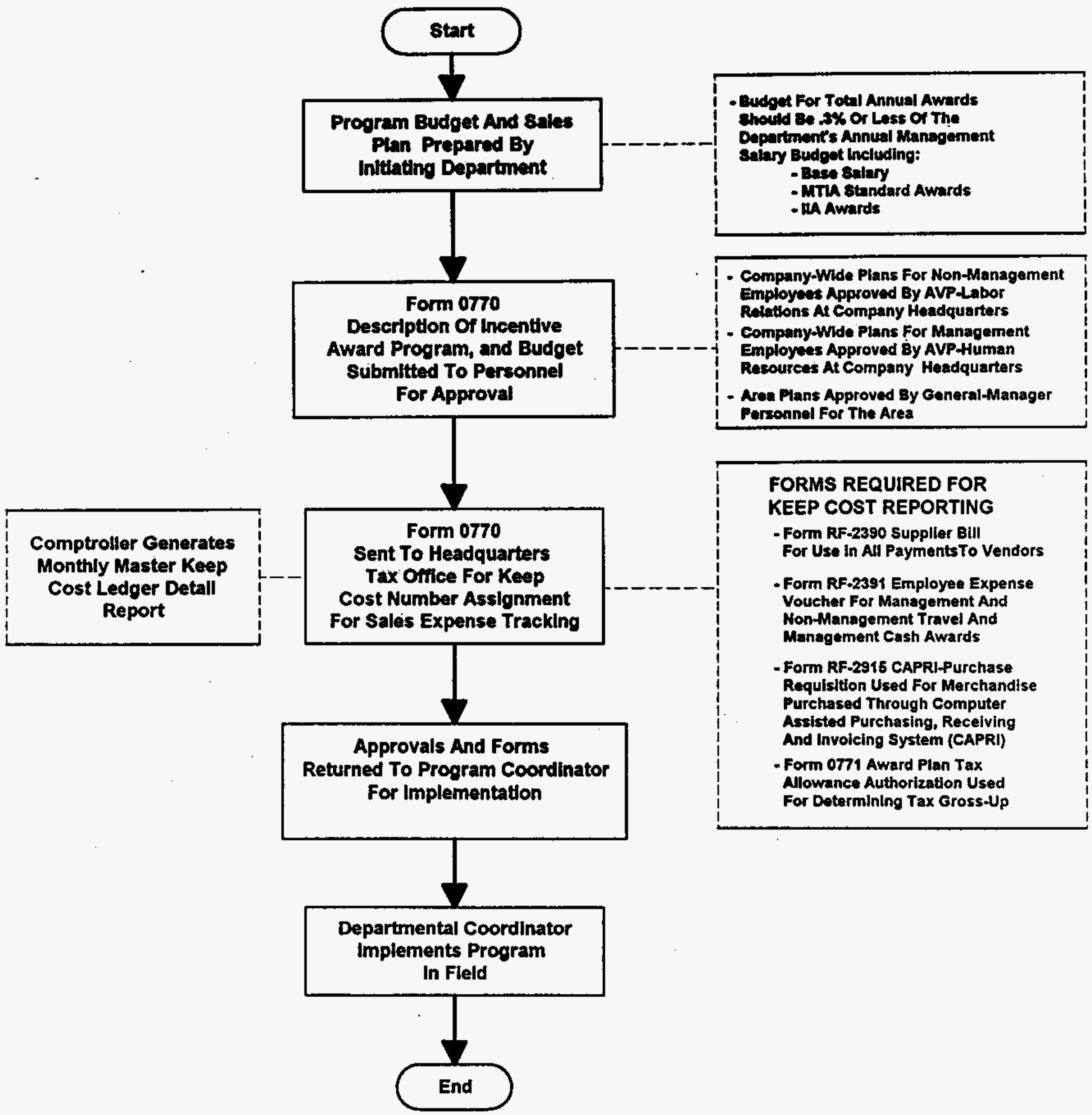
2.3.1 Basic Referral Processing

Prior to 1986, sales of services were negotiated by service technicians while on customers' premises and reported through the installation or repair service order form. To ensure receiving proper credit for the sale, the service technician recorded his assigned sales code on the service order. Uniform Service Order Code (USOC) notations of the service additions were also entered on the existing installation or repair order and processed with the completed order.

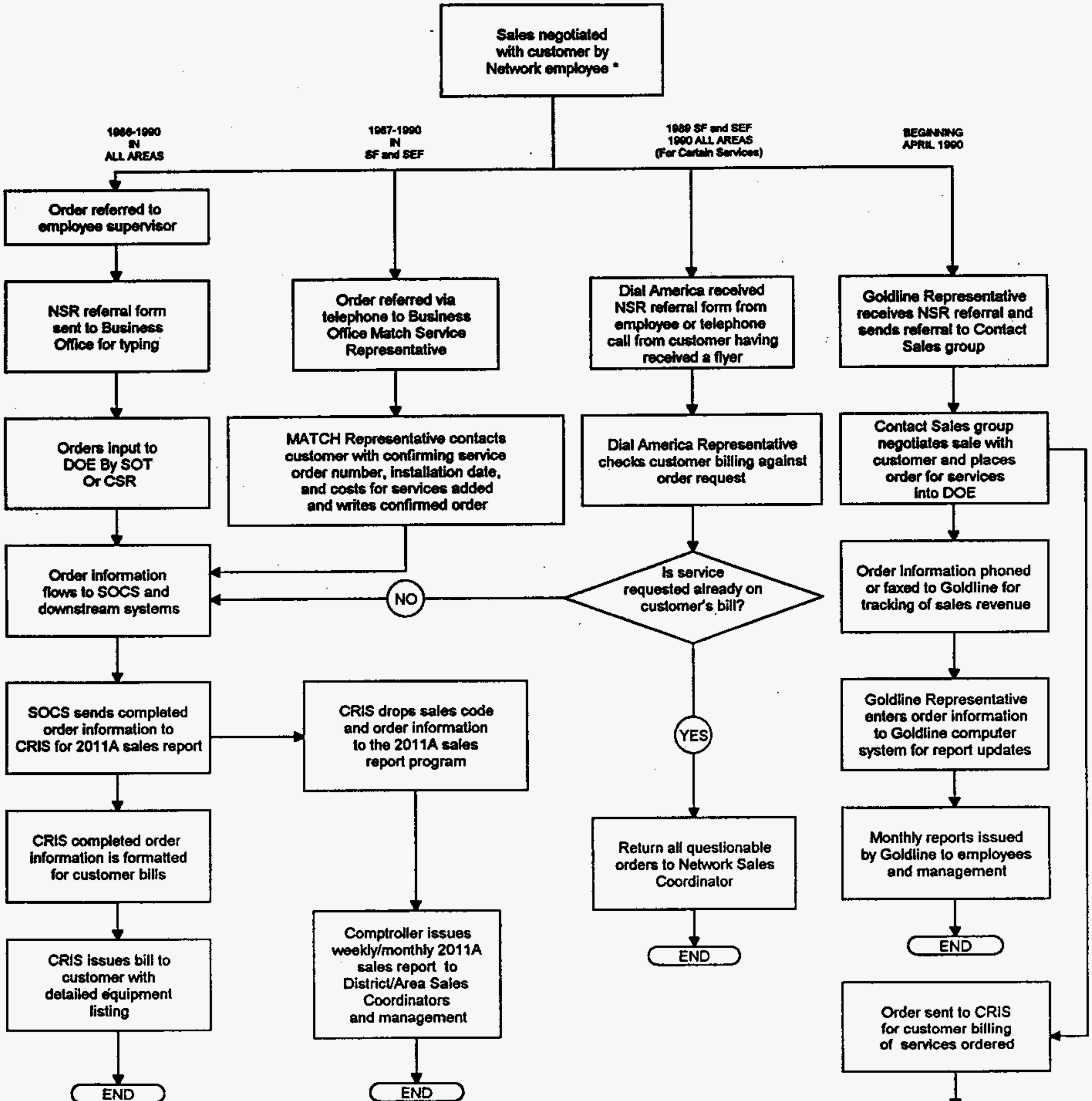
In 1986, the Network Sales Referral form, or NSR-86, was designed for the specific purpose of reporting sales of services by non-contact employees. This same form continued to be used through 1990, although varying methods for processing the Network Sales Referrals were employed over the years.

As shown in Exhibit 5, upon completion of a sale, the NSR-86 was forwarded to the employee's immediate supervisor, then to the local business office for input by the Customer Service Department. The NSR-86 form included a space for the customer's signature evidencing his/her authorization for the services to be added. However, this control was

NON-CONTACT SALES PLANNING AND BUDGETING PROCESS
AS OF 1988



NON-CONTACT SALES REFERRAL PROCESS
1986-1991



CSR - Customer Service Representative
SOCS - Service Order Communication System
SOT - Service Order Typist
NSR - Non-Contact Sales Referral
NF - North Florida
SF - South Florida
SEF - Southeast Florida

* Network employees involved in non-contact sales were:

1. Repair Service Attendants (RSA)
2. Maintenance Administrators (MA)
3. Dispatch Clerks (DC)
4. Service Technicians (ST)
5. Outside Plant Technician (OPT)
6. Construction Repair Technicians (CRT)

EXHIBIT 5

SOURCE: STAFF ANALYSIS

not always used, since employees had the option of telephoning in completed sales. In these instances, the Customer Service employee filled out the NSR-86 over the telephone and these forms would not include a customer signature.

A Service Order Typist or Customer Service Representative then entered the order into the Direct Order Entry (DOE) system, which forwarded the customer billing information to the Customer Record and Information System (CRIS).

2.3.2 MATCH Program Referral Processing

During 1986, the processing of a high volume of NSR-86 forms increased the workload of the Customer Service Department, resulting in resentment towards the Network Department. The Customer Service Representatives involved received no incentive awards for their role in processing the NSR-86 forms. Further, since these Customer Service Representatives were (and still are) responsible for meeting sales objectives as a basic element of individual performance evaluations, the Network employees making sales of the same services were viewed as competitors. The increased workload of processing NSR-86 forms and the perceived competition resulted in distrust which threatened cooperation between these two departments.

To allow Network employees the option of obtaining technical assistance from Customer Service personnel in making sales of complex services, the MATCH program was developed in 1987. This program was set up in South and Southeast Florida to receive and process non-contact sales referrals through the business office. MATCH established a means for Customer Service Representatives to receive credit towards sales objectives for referrals made by the non-contact sales employees.

MATCH referrals were made by Network employees by calling the MATCH service representative in the business office on a special toll-free line. After receiving the referral, the MATCH representative would call the customer to complete the sale. Once completed, the sale was reported by the MATCH service representative, who entered the order into DOE. The MATCH service representative also recorded the sales codes of the Network employee who generated the lead and the Customer Services employee who closed the sale. The order flow and sales reporting flow were the same for the MATCH program as previously described.

2.3.3 Referral Processing by DialAmerica

The Company used DialAmerica, a direct marketing contractor, to process referrals for non-contact sales programs from time to time during the years 1985 through 1990. DialAmerica processed reports of sales via telephone by non-contact employees to reduce processing delays and relieve some of the additional workload placed on the Customer Services Department.

However, since DialAmerica was located in Atlanta, receiving sales credit was sometimes delayed. As a result, some Network employees, such as many in North Florida, continued to have their sales referral forms processed through Southern Bell business offices.

Exhibit 5 shows how DialAmerica received referrals from non-contact sales employees via the NSR-86 form or over the telephone. Upon receiving the referral, the DialAmerica representative verified through CRIS records that the customer did not already subscribe to the service requested. If there were no problems with the order, it was processed through the Direct Order Entry (DOE) system and followed the normal order flow. If the service requested was already listed in the customer billing records, DialAmerica representatives returned the order to the Network Sales Coordinator without entering it into DOE.

DialAmerica's capabilities were limited to issuing orders for custom calling, inside wire maintenance, Touchtone, and Touchstar services. Orders for other services were forwarded to Southern Bell for handling.

2.3.4 Goldline Program Referral Processing

By late 1989, the Company recognized a need to redesign its sales incentive programs. The new program, called Florida Goldline, included improved internal controls and operations centralized to a single location and staff. In April 1990, implementation of Goldline was completed throughout the state. Although transition from the use of the NSR-86 form continued until June 1990, Goldline became the only sales referral processing method for non-contact sales during 1991. Goldline was used to refer leads for the sale of all services and equipment offered by Southern Bell.

The Goldline program allowed all Florida employees to participate in referring sales leads to the Goldline staff, who routed the referrals to appropriate contact sales groups. The sales office representative then contacted the customer, negotiated the sale, and placed the order for the services sold. If additional services were negotiated by the contact sales employee, the referring employee shared credit for this sale as well.

Completed sales orders from the business office contact sales group were processed via Direct Order Entry (DOE) and orders processed through the Marketing sales groups were processed through the VAX System for CPE sales tracking. Completed orders were forwarded to CRIS (Network Services) and to the CPE Billing System (CPE services) for subsequent issuance of customer bills. The 2011A system tracked sales of network services, however CPE sales by Marketing personnel were tracked by a separate system.

Information regarding sales, made from the non-contact employee referral, was also sent back to the Goldline office by the contact sales office. The non-contact sales employee received sales credit in the Goldline computer system for the referral. The contact sales employee receiving the referral and completing the sale received credit towards his/her sales objective. The Goldline system produced individual monthly statements accounting for referrals and sales made by each participating employee and manager. Monthly reports to employees were only issued if the employee had been involved in sales activity during the reporting period. If sales referrals were made in one month, and completed by the contact sales employee in the next month, a report would not be issued until the month the sale was completed and issued.

2.4 *Sales Incentive Program Administration*

2.4.1 Role of Sales Coordinators

The Florida Network Staff administered the non-contact sales incentive programs through the Operations Manager, IMC/I&M Support Staff and two area sales coordinators, shown on Exhibit 2. Under the direction of the Operations Manager, the coordinators helped implement annual sales programs developed by Headquarters I/M Operations Support Staff in Atlanta, and beginning in 1987 prepared and implemented programs customized for Florida.

Annual campaigns promoted year-long programs and themes, while spurt campaigns promoted short-term localized emphasis on specific Company services. Area sales coordinators disseminated information to the districts, and conducted program kickoff meetings. One coordinator was responsible for programs in North Florida and the other was responsible for Southeast and South Florida programs. These coordinators carried out their duties as an additional assignment to their existing Network Staff workload. In 1989, the duties of the two area coordinator designations were consolidated under one statewide Network sales coordinator.

Local or district sales coordinators, appointed by district management, also assisted in administering the non-contact sales programs by tracking and monitoring local sales and revenues, and preparing sales credit checks for disbursement after review by appropriate managers. District sales coordinators reported sales results for individuals, work groups and the district in which they served. Like their area sales coordinator counterparts, district coordinators were given these sales responsibilities as an extra assignment, in addition to regular duties.

2.4.2 Sales Results Reports

The mechanism for reporting and tracking completed sales was the Form 2011, revised in 1988 to become the Form 2011A. This sales report was utilized to track Customer Service Departments' sales, as well as non-contact sales program results. Generated monthly by the Comptroller system, the 2011 and 2011A profiled individual, group and district sales totals. The 2011A report continued to be the primary method of reporting non-contact sales results until the Goldline program was established with its own results tracking system in April 1990.

The Goldline program established its own reports to monitor sales results and referrals received. These reports included: monthly sales totals for managers, individual employee monthly statements tracking results of each referral and total sales credit, sales transactions producing six-months' revenue of $1,000 or more, percentage of successful referrals, and status of unresolved referrals.

2.4.3 Pre-Goldline Sales Credits and Award Redemption

Over the period 1986 through 1990, sales credit incentives were set at 10% of the additional revenue generated from each sale. The additional revenue was tracked on the basis of semiannual revenue for the purposes of incentive calculation. Based upon the Company's experience, these services were expected to be retained by customers for about 6 months. For example, a service with a $2 monthly fee was expected to generate $12 of revenue ($2 times 6 months), resulting in $1.20 in sales credit awards for the non-contact sales employee.

Of the sales credit awarded, 10% went to the employee actually making the sale, 3% to his Pay Grade 3 manager, 2% to his Pay Grade 4 or 5 manager, and 1% to his Pay Grade 6 or 7 manager. The rewarding of managers and supervisors for their employees' efforts was intended to provide an incentive for managers to motivate employees to generate sales revenue.

Based upon the 2011 report, the district sales coordinators prepared bonus point checks for employees who had accumulated sales credit, as shown in Exhibit 6. Initially, coordinators issued bonus point checks monthly. To reduce administrative time and cost, sales credit redemption checks were eventually issued quarterly, and ultimately on an annual basis. The 2011 sales report initially did not reflect sales subsequently cancelled by customers. In 1987, the Company began deducting sales credit when customers cancelled services within 60 days of the sale.

During the period 1986 through 1989, employees redeemed bonus point checks for items selected from a catalog through E.F. MacDonald Company. Reports of sales credit checks issued and the merchandise orders were sent to E.F MacDonald through BellSouth Services Purchasing. The merchandise was delivered to the employee's home or workplace. Tax expense reports were forwarded to the State Sales Coordinator who forwarded them

AWARD REDEMPTION PROCESS
AS OF 1988

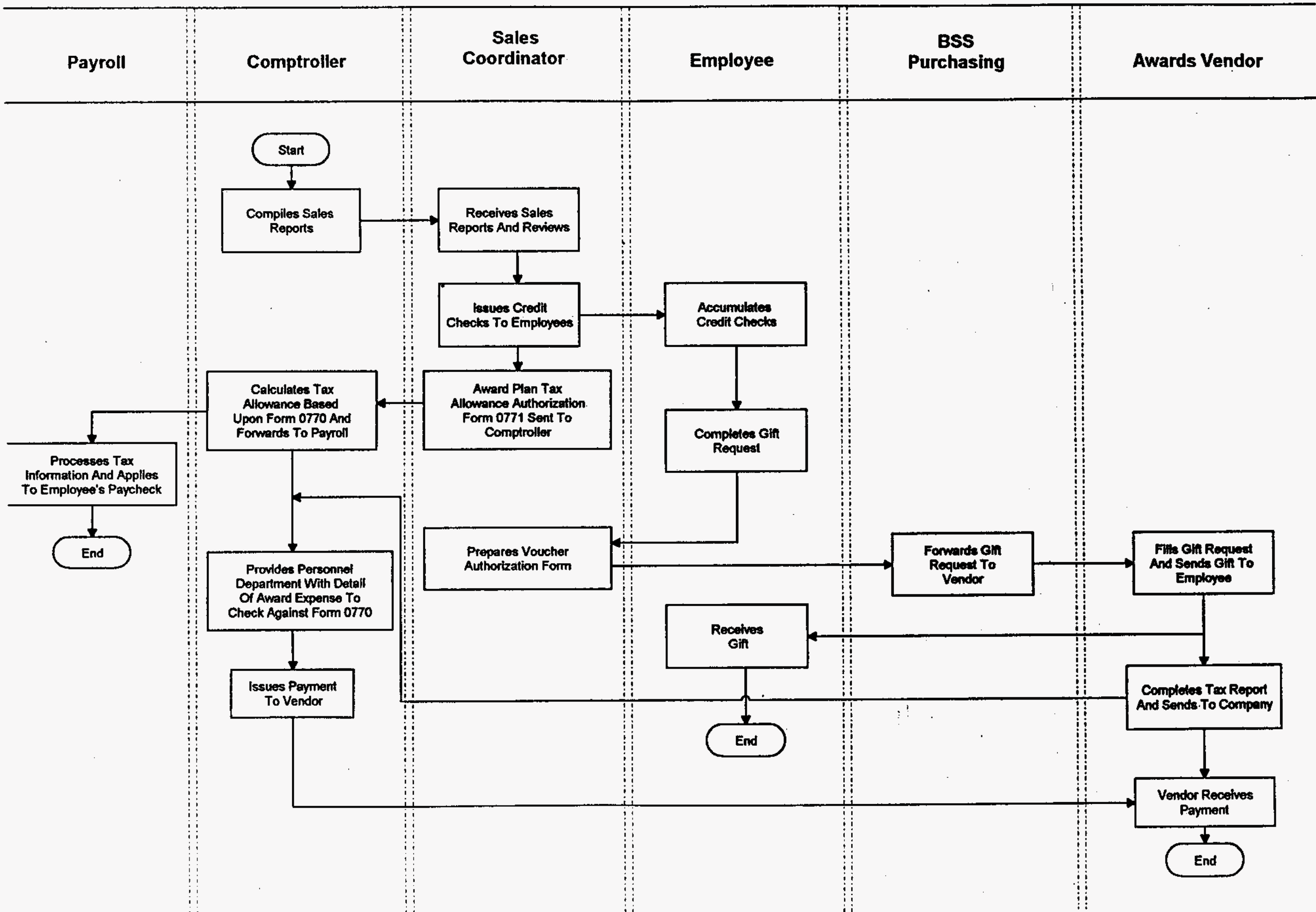


EXHIBIT 6

SOURCE: STAFF ANALYSIS

to the District Sales Coordinators. District Sales Coordinators were responsible for having forms approved by appropriate managers and sending them to Payroll for taxing and gross-up. This information was then forwarded to Personnel for posting to payroll records.

2.4.4 Goldline Sales Credits and Award Redemption

Goldline sales credits were awarded in a manner similar to earlier sales programs, but credits were awarded to both employees and managers at a substantially lower rate. Through Goldline, the seller of services received just 4% of the resulting semiannual revenue, or less than half of the 10% awarded in prior incentive programs. First through fifth level managers received about one-tenth of the former revenue credit, or about .4%, .3%, .2% .1%, and .025%, respectively. Rewards for the sale of equipment were limited to $500 of sales credit.

Under the Goldline program, sales credit for each employee was tracked through the individual monthly statements. Employees accumulated sales credits and at their discretion, requested issuance of gift certificates by the Goldline center. The certificates could be redeemed for merchandise through Marketing Innovators, Inc. for merchandise from specified local retailers. Redeemed sales credits were to be reported to the Comptroller and Personnel Departments for tax calculation and reporting purposes.

3.0 CONTROLS

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3.1 Procedural Controls

The three primary procedural mechanisms used to guide and control the non-contact sales program were the *Executive Instructions*, the *Personnel Policy Manual*, and the *Program Guidelines* for each of the sales programs. These policies and guidelines evolved over time at least partly in response to changes, such as problems encountered with the sales incentive programs.

As discussed, the *Executive Instructions* were issued by Southern Bell Corporate Headquarters as a means of providing common policy and guidelines to the four state operations of Southern Bell. These instructions set forth company-wide policies and procedures essential to conduct and guide business operations in an orderly and efficient manner.

Further procedural guidelines for non-contact sales programs were included in the *Program Guidelines* issued with each sales program, from the IMC/I&M Support Staff. During the period 1988 through 1990, 20 non-contact sales incentive programs were developed by the Florida Support Staff, and guidelines were issued to provide basic instructions about each particular program.

Other than the brief *Program Guidelines*, no training manuals, procedural manuals or other literature was provided to participating managers and employees. Although the *Program Guidelines* provided an example or two of how a sales opportunity could be recognized, the actual implementation of the sales effort and sales practices were left up to the program participants.

Revised guidelines provided in the *Personnel Policy Manual*, Section 51.102 for Sales Awards Programs were issued by the Vice President-Personnel, in Atlanta, on November 27, 1990. These supplemental guidelines represent in many instances notable departures from prior practices in sales incentive programs.

For example, these guidelines specified that all awards recognition should be nominal in value, that all programs should be approved in advance by the Legal Department, that customer canvassing, telephone banks, boiler rooms and related sales activity should be specifically authorized, that managers not directly involved in sales efforts could be recognized for sales results of subordinates, but should not be eligible to accumulate points toward awards for a subordinate's sales, that awards points should not be shared or transferred between employees, and that employees should not be reassigned from their normal job duties to be devoted to sales efforts.

Specific, detailed instructions were needed to insure that a consistent, professional, and effective approach would be taken in these sales programs that involved thousands of employees with diverse job and training histories. Detailed written procedures would have provided Network Department line managers with a consistent means of evaluating the quality of his/her organization's efforts and results in the unfamiliar area of sales.

3.2 *Processing and System Controls*

The process of generating and handling sales and sales referrals varied over the period reviewed in this audit, but the underlying controls changed little. Some controls were built into the handling of the reported sales. Others were provided through the computer systems that processed the sales. Despite the discovery of problems with sales reported by incentive program participants, over the period 1986 through 1991, changes in controls were few. Most of the control changes made were associated with the implementation of the Goldline program in 1990.

3.2.1 Documentation of Pre-Goldline Sales

During the period before 1986, when non-contact sales were simply added to the service order by service technicians, the sales of services was less than fully documented by means of the technician's written additions to the service order. As the sales order was processed, it may not have been reviewed by anyone other than the Service Order Typist.

With the inception of the NSR-86 form, a separate piece of documentation was created solely for the purpose of documenting the sale. This 3-part form provided a copy to be reviewed by the district sales coordinator and the selling employee's manager, a copy for the employee to retain to verify his receipt of proper sales credit, and a copy to be processed by the business office. This form provided an opportunity for managers and others to become aware of any problems with the sales being reported. In addition, the Form 2011A provided individual and group sales results.

In response to the Staff's January 3, 1991 request for information, the Company described the management controls for verifying the correctness of the information reported by the employees in the non-contact sales programs. First and second-level managers provided the front line of defense, according to the Company's response. The Company stated, "The primary management controls over the sales programs prior to 1990 were vested in the first and second level managers in the various districts in Florida. These managers received regular reports on the sales results of their subordinates and were in a position to identify any anomalies in the level of reported sales."

Despite this response, the Company's sales program guidelines and literature did not clearly establish the duties and responsibilities of managers for monitoring the quality of the sales effort or the resulting sales themselves. Extensive documentation provided by the Company indicates that managers were urged to motivate employees to sell, but little mention is made of the specific role and duties of the managers involved in these sales programs, such as monitoring the sales effort.

The Company's response to the January 3, 1991 Staff request maintains that a secondary control was also provided by sales coordinators and customer service representatives. In its response to Item 13(g) of this request, the Company stated, "In addition, the sales coordinators received copies of the Form 2011As which reflected the sales made by the various employees working within each sales coordinator's geographic area of responsibility, which should have enabled the sales coordinators to identify abnormal activities," and ". . . the Company's service representatives were responsible for handling customer complaints and informing their supervisors if they became aware of problems that were repetitive or appeared to represent some inappropriate activity, which is how the matter now under investigation came to the attention of the appropriate management personnel."

Interviews with Network Department employees indicate that managers and sales coordinators paid little attention to this monitoring role since they were primarily responsible for their main job duties, and since the sales programs were just an added peripheral activity. There appears to have been a misconception among non-contact personnel that monitoring of sales quality was to be performed by the Customer Service Department upon receipt of the sales referral forms. Some checking was performed by Customer Services at the point the NSR-86 information was being input. However, this was largely limited to the verification, by checking the CRIS records, that the sale reported did not involve a service that was already being provided to the customer.

The Company's response to Staff's First Set of Interrogatories, Item 10 indicates that the Company introduced a confirmation letter in early 1987 that was sent upon completion of new and transfer orders. However, this would not provide verification of sales to existing customers, who were the main target of the sales incentive participants.

3.2.2 Documentation of Goldline Sales

With the implementation of Goldline, controls surrounding the selling and reporting of sales were improved in several ways. According to the Company's responses to Staff's Third Set of Interrogatories, Item 47, Goldline was implemented "as a result of efforts to enhance Southern Bell's employee referral program". Goldline represented an effort to correct problems with the prior non-contact sales incentive programs. Many of the control improvements represented by Goldline directly related to problems encountered in the prior programs.

One control improvement from the Goldline program was that sales were eventually closed by trained contact sales employees this decreased the chance that customers were given incorrect information, or that pressure sales tactics were used. In addition, the tracking of sales referrals through the Goldline system protected the accuracy of sales credit and provided a means of assigning responsibility if an unauthorized sale was discovered.

The processing of all sales referrals through a single point and single method was itself an improved control. The fact that Goldline provided a central processing point increased the likelihood that problems, trends, or program weaknesses would be detected. For example, all sales referrals were routinely examined mechanically to insure there were no duplication of sales.

The primary control improvement in the Goldline system was the separation of the sales process into two parts: the referral and the closing of the sale, each performed by different employees. The referral provided by the non-contact employee was telephoned or faxed into the Goldline center, and passed on via fax to designated contact sales personnel, frequently Customer Service Representatives. Once the assigned contact sales employee contacted the potential buyer, he or she reported the results to the Goldline Center, usually via fax. This, in effect, represented a separation of duties between the three employees involved, increasing the difficulty of reporting a fictitious or unauthorized sale.

3.2.3 System Processing Controls

The mechanized systems for inputting contact and non-contact sales programs were shared since non-contact sales were not essentially different from the contact sales routinely made by Customer Service and Marketing personnel. Therefore, mechanized system controls in place for non-contact sales were very similar to those of the contact sales program.

Once received by the business office (and after 1990, by the Goldline Center) mechanized processes issued the order, billed the customer for the service ordered, gave employees sales credit, issued monthly sales reports and accounted for individual and company tax liability. The mechanized systems involved were: Interim Billing and Order Support System (IBOSS), Business Office Customer Records Information System (BOCRIS, which was developed to replace IBOSS), Direct Order Entry System (DOE), and the Customer Records Information System (CRIS), VAX CPE sales processing system, and the CPE Billing System.

The mechanized process began when the NSR-86 sales referral form information was typed into DOE by the Customer Service Representative or Service Order Typist. After the implementation of Goldline in 1990, the sales referral information was entered into the Goldline system by Goldline personnel. The information was sent via fax to the business office or Marketing Department for handling. IBOSS was used by the business office to display customer billing information on Customer Service Representative screens for use in discussing bills or making sales to customers. IBOSS provided customer record information, such as the customer name, address, telephone number, equipment billing, and credit class.

In 1991 Southern Bell replaced IBOSS with the Business Office Customer Record Information System (BOCRIS). IBOSS and BOCRIS were both points of control for the Sales Referral Process. These systems provided a check point to compare the services requested by non-contact sales referrals against current customer billing, and to determine whether related or pending orders were issued by other employees for the same services. These systems also allowed the business office to determine whether sales referrals included services for which the customer was already being billed.

Orders were entered into the Direct Order Entry System (DOE), then forwarded through the Installation and Maintenance Center and dispatched to an installer in the field. The order information was forwarded to SOCS, the Service Order Communication System, and then to downstream systems. After processing through all applicable systems, orders were completed in CRIS, and billing was generated. CRIS then sent the customer an itemized bill showing the services added, monthly billing for all equipment and services, and installation charges. Orders also dropped to a file run against the 2011A program to generate the weekly and monthly sales reports and summaries.

3.2.4 Sales Credit Tracking Controls

Sales credit information, including the code for the product or service sold, the revenue increase or decrease, and the employee sales code for awarding sales credit was obtained from CRIS. This information was then compiled and output in the form of the 2011A report, which shows monthly sales revenue for individual employees, groups, and management employees. From the 2011A report the district sales coordinator issued a sales point credit check to employees. The sales point credit checkbooks were maintained and manually administered by each district sales coordinator, rather than being centrally administered by a single source.

The 2011A report acted as the primary control to determine whether sales credits were correctly issued. The appropriate sales credits for the period could be determined by multiplying the total sales revenues reported on the 2011A by the number of points per dollar assigned by the sales program guidelines. However, the 2011A did not include a record of each NSR-86 submitted and its outcome. Some Network employees accused Customer Service employees of "stealing" sales and claiming credit by entering their own sales codes. In these instances, the referral forms were returned with a notation that the customer already subscribed to the service sold. Without a formal record of the handling of a referral, such allegations were difficult to prove. The 2011A form itself did not provide a means of determining whether the sales reported therein were improperly handled or legitimate sales.

Under Goldline, the means of tracking sales credit became the individual monthly statement that was produced by the system developed specifically for Goldline in 1990. This statement did provide the seller with a list of all referrals he or she submitted, and indicated for each one whether a sale was made. If a referral was disputed, it could be traced from its receipt to its assignment to a contact sales employee. The Goldline system also had the advantage of being administered through a single point of control, the Goldline Center in Miami, as was the sales credit redemption process.

3.2.5 Employee Time Reporting Controls

The Mechanized Time Reporting (MTR) system categorized the time spent by employees in the course of their work. The MTR system information provided management with a measurement of time individual employees and employee groups spent in sales activities.

The MTR system is dependent upon the accurate recording of Job Function Codes (JFCs) to detail employee time spent in these different activities. However,

3.3 *Review and Audit Controls*

Within the area of audit and review controls, the IMC/I&M support staff organization was available to assist the Network managers in examining sales practices, results, or other aspects of the programs. In other areas of Network operations, the Network Staff performs periodic reviews testing adherence to procedures, accuracy of reported results, and other information supporting management of the Network Department's daily operations. However, this group did not provide such reviews or examinations regarding the overall practices and controls in non-contact sales incentive programs.

As with any function within the Company, formal internal audits represent a significant control, enabling management to detect and prevent fraud. However, the formal internal audits conducted during the period 1985 through 1989 were only occasionally of direct relevance to the non-contact sales incentive programs.

4.0 CONTROL PROBLEMS

4.0 CONTROL PROBLEMS

Over the period 1985 to 1990, instances of sales falsification marred the Company's non-contact sales incentive programs. Viewed separately, these unauthorized additions to customer bills may appear to be isolated instances over a period of time. However, when viewed chronologically together, the incidents described in this section of the report show patterns of recurring problems, and failure by management to detect and prevent continuing unauthorized customer billings. Exhibit 7 presents a timeline of selected events that illustrate these patterns. These incidents are described in detail in this section.

Because management did not take adequate action on each situation identified, the amount of surviving information varies. In some instances, allegations and evidence of potential fraud triggered requests by the managers involved for an investigation by the Security Department, while other similar situations were handled internally by the managers involved. In cases where no Security Department investigation was requested, potentially valuable documents were discarded and employees had the opportunity to change their tactics. As a result some allegations of potential fraud were never resolved. Eventually, well-documented cases gave detailed evidence of the problems, causes, and effects. However, complete investigation of the earliest instances and appropriate follow-up by management could have brought the problems into the open years sooner.

4.1 Sales Falsification: 1985-1986

4.1.1 South Florida 1985

In 1985, a number of South Florida Customer Service Representatives received customer complaints of improper billing for services they claimed not to have ordered. At the same time, Service Representatives, following up on their own sales orders, reported finding their sales codes removed and replaced by those of Network employees.

These complaints, and a large quantity of questionable sales forms, were referred to Network and Customer Services Support Staff. A Customer Services Support staff member in turn notified her General Manager of this problem. The General Manager - Customer Services Support indicated the problem had been referred to the Network General Manager - IMC/I&M Support. Any action taken as a result is unclear. However, the Security Department was never requested to investigate the situation, nor was the Internal Auditing Department requested to perform an audit to identify control weaknesses or recommend improvements to non-contact sales programs.

Although the actual number of suspect sales is unknown, they may have numbered in the hundreds since the forms in question were described as a stack about six inches high. These forms were later destroyed by the Customer Services Staff.

SOUTHERN BELL NON-CONTACT SALES CONTROL PROBLEM TIMELINE

DATE	EVENTS
1985	SOUTH FLORIDA • Large number of suspect sales forms provided to Customer Service Department Staff General Manager who contacted Network Department Staff General Manager. No documentation of action or security investigation exists.
1986 DECEMBER	NORTH MIAMI • Service Technician is terminated for falsifying sales of Trouble Isolation Plan.
1987 MAY	ORLANDO • Customer Services Assistant Manager reports Maintenance Administrator in Orlando to Network Sales Coordinator in Jacksonville for adding unauthorized services to customer bills, no documentation of action or security investigation exists.
1987 DECEMBER	MIAMI • Two Miami Metro District Service Technicians are terminated for falsifying sales of Call Waiting services, with one ST blaming management pressure to sell as the reason for falsifying sales.
1988 MARCH	WEST PALM BEACH • Manager, Customer Services questions a large volume of NSR sales forms submitted for processing by a single employee; contacts employee's Network Assistant Manager to report suspicions of unauthorized sales.
1988 JUNE	WEST PALM BEACH • Manager-Customer Services sends memo to inform Network Assistant Manager that suspected fraudulent non-contact sales will no longer be processed by her workgroup.
1988 JUNE	MIAMI • General Manager-Network contacts Operations Manager-IMC/I&M Support regarding revamping entire state sales program, methods of improving verification of referrals, and insuring boiler room operations are not rewarded. Recommended changes provided in response were not implemented.
1988 DECEMBER	ORLANDO • Administrative Support Manager-Network is informed by Business Office of 20 complaints concerning unauthorized service additions. Network employees assure manager sales are ok, Network and manager dismisses questionable sales as insignificant versus high volume of sales made by the employees. No other action taken.
APRIL 1989-JUNE 1990	ORLANDO • Two employees make approximately 40,000 unauthorized sales, allegedly at the direction of their supervisor; one employee admits 75% of her sales during the period were unauthorized and the other admits that all of his sales were unauthorized.
1990 JUNE	ORLANDO • Network Operations Manager-Orlando requests SBF Security Department to investigate possible fraud by the two Orlando Network employees. Security investigation begins September 1990.
1990 OCTOBER	ORLANDO • Orlando investigation completed resulting in the termination of two non-management employees and an Assistant Manager.
1990 OCTOBER	WEST PALM BEACH • Investigation of West Palm Beach uncovers unauthorized customer billings for the Inside Wiring Maintenance Plan, results in termination of a Manager-Network and Service Technician, suspected of making unauthorized sales referrals since 1988. Operations Manager was retired at the Company's direction, and Southeast Florida Network General Manager was disciplined.
1990 OCTOBER	STATEWIDE • Southern Bell General Attorney requests investigation into Inside Wire Maintenance/Tip Plan.
1990 OCTOBER	STATEWIDE • Southern Bell General Attorney requests Southern Bell General Internal Auditor to conduct an audit of Non-contact Sales (Number F00-19-67).

EXHIBIT 7 *SOURCE: STAFF ANALYSIS*

4.1.2 North Miami 1986

As early as 1986, a Service Technician in North Miami was terminated for falsifying sales in a non-contact sales incentive program. According to personnel file records, the Commercial Department discovered in October 1986 that the employee was reporting sales to disconnected telephone numbers. Despite being warned and reminded of proper methods for making sales, customer complaints continued to be received regarding additions of services resulting from this employee's sales. In November 1986, the Service Technician's supervisor checked 17 suspect sales, finding that all 17 lines were either disconnected or assigned to another customer. These incidents of sales falsification, along with other procedure violations were cited as the reasons for dismissal of this employee in December 1986.

4.2 Sales Falsification: 1987

4.2.1 Orlando 1987

In May 1987, an Assistant Manager in Customer Services reported a problem to the Network Sales Coordinator regarding sales made by a top seller in Orlando. The Network Sales Coordinator arranged for the Assistant Manager Customer Services to meet with the selling employee's supervisor, also an Assistant Manager, and left the problem with them to be resolved. No follow-up was made by the Network Sales Coordinator.

The same top seller was later accused of adding unauthorized services to customer bills in 1989, and again in 1990. Finally in 1990, when Company Security was requested to investigate suspected fraud by employees in the Orlando non-contact sales program, this employee admitted to adding unauthorized services to customer bills and was terminated, along with two others, as discussed in Section 4.4.1 below.

4.2.2 Miami Metro 1987

In 1987, two Miami Metro district Service Technicians, who were assigned full-time to sales activities, were terminated for intentional falsification of sales. One of these employees confessed to adopting the fraudulent techniques of her co-worker as a result of perceived pressure from a first-line manager to equal the co-worker's higher sales results.

The improper sales were discovered as a result of complaints from customers who discovered services added to their bills without their consent. These customers included Southern Bell employees and their relatives. Services were reported on the NSR-86 form, and since there was no verification control, these false sales were input to the billing records by the Customer Services Department.

The Company's security investigation included detailed examination of evidence of nearly 200 disputed or suspicious sales by these employees, indicating the incident did not result from honest errors or misunderstandings with customers. The total number of sales reported by these two individuals totalled in the thousands. The employee who confessed stated that the majority of her sales were false. These two employees focused almost exclusively upon the sale of the Company's Call Waiting service.

4.3 Sales Falsification: 1988-1989

4.3.1 West Palm Beach 1988-1989

In 1988, one of the largest instances of sales falsification was identified by Customer Service business office employees in West Palm Beach. However, full resolution and investigation spanned over two years. Discovery of this fraud began when a Customer Services Manager in West Palm Beach questioned the large volume of Network Sales Referral Forms (NSR-86) submitted for processing, most generated by a single employee.

From her own familiarity with sales, she suspected these results were not humanly possible and later noticed the forms submitted were in street address sequence. Her analysis of a sample of 50 reported sales indicated that none of these customers had been actually contacted about subscribing to the Wiring Maintenance Plan. After contacting the Network Assistant Manager supervising the employee suspected of generating the false sales, and issuing follow-up warning memos without results, the Customer Services Manager refused to process these suspicious referrals and referred the matter to the Customer Services staff support organization.

However, the Network Assistant Manager was not easily deterred from having his group's sales processed. During early 1988, this Assistant Manager had found a way to bypass controls to have his group's sales referrals processed. This required the agreement of a second Customer Services Manager to allow a Network clerk to use of a computer terminal in her business office to input sales orders. In exchange for allowing this unusual arrangement, that circumvented the proper separation of duties, the Network Assistant Manager agreed to share sales credits with the Customer Services work group.

In mid-1989, the Customer Services Manager who had originally detected the fraudulent nature of these sales referred the problem to the Assistant Staff Manager for Customer Services. The Customer Services Manager also provided a number of the falsified referral forms for examination. Rather than reporting the problem to appropriate upper management within the Network Department, an agreement was reached in late 1989 among the DialAmerica representative, the North Florida Customer Services Sales Coordinator, the Area Sales Coordinator, and the Assistant Staff Manager-Customer Services. Under this agreement, Network Sales Referrals were to be sent directly to DialAmerica.

This indirect solution was intended to relieve Customer Services of responsibility for processing the questionable sales and to deter the efforts of the Network Manager and his employees. DialAmerica was to handle the referrals and forward questionable ones to the Area Sales Coordinator for resolution. However, this problem was not resolved by the action taken and the questionable sales continued. Finally, the situation was investigated and resolved in 1990, as discussed in Section 4.4.2 below.

4.3.2 Orlando 1988

In late 1988 the Administrative Support Manager-Network Orlando, was informed of a list from the Business Office reflecting the names of about 20 customers complaining that services had been added to their telephone without authorization. The list reflected that two Maintenance Administrators and one Service Technician had issued the orders in question.

The Administrative Support Manager questioned the Service Technician about the suspect sales referrals. The Service Technician assured the Administrative Support Manager that they were valid. The Assistant Support Manager dismissed the questionable sales as being a few complaints out of the hundreds of orders issued by the Service Technician, and failed to examine whether a larger pattern of problems might have existed. No sampling of orders submitted by the Service Technician was conducted to determine whether other sales might have had similar problems.

4.4 Sales Falsification: 1990

4.4.1 Orlando 1990

In June of 1990, a series of customer complaints in the Orlando area initiated events that resulted in recognition by top Network Department management that serious problems existed regarding the legitimacy of sales made through the non-contact sales programs. According to Southern Bell's Florida Vice President-Network, "Our first knowledge that something was awry came about in the Orlando area, and it came to us by customer complaints". Despite this statement, the 1990 Orlando events were not new developments--they were merely the continuation of the 1988 problems discussed in sections 4.2.1 and 4.3.2 above.

On June 26, 1990, the Network Operations Manager-Orlando Division requested the Security Department to begin an investigation into possible sales fraud. Security was delayed in beginning the investigation in Orlando until September of 1990. According to the Company, the delay was due to other investigations being conducted.

The initial Orlando investigation was completed in early October, 1990, and revealed that certain employees had added services to customer bills without authorization.

Investigation records showed the unauthorized billings affected over 20,000 customers within the Orlando service area.

The two employees involved had made 44,516 sales over a period extending from March 1989 through mid-June 1990. One employee admitted that all 25,292 of the Inside Wiring Maintenance upgrades submitted during the period were unauthorized, while the other employee estimated that at least 75% of the 19,224 sales she made were false.

Both employees stated that they falsified the sales at the direction of their immediate supervisor, an Assistant Manager, and that other managers were aware of improper sales. The Assistant Manager denied the accusations of the two employees, but all three were later terminated by Southern Bell, as a result of further investigation. A total of twelve employees in the Orlando operations were either counseled, suspended, or terminated.

4.4.2 West Palm Beach 1990

On October 18, 1990, the BellSouth General Attorney requested an investigation into the Inside Wire Maintenance Plan/Tip Service in Southern Bell of Florida. This investigation coincided with the conducting of Internal Audit FOO-19-67. The investigation of non-contact sales operations in West Palm Beach began in October of 1990.

The West Palm Beach investigation finally brought to resolution the incidents previously mentioned in Section 4.3.1. Several improper sales methods were reported in the West Palm Beach investigation. These included Network employees assigned exclusively for sales, boiler-room operations conducted at several different locations, employees selling from their home, employees canvassing entire areas by telephone and in person, the sharing of sales credits among the work group, and the use of calling cards and fliers intended to cause new tenants to initiate their new services through the non-contact employee, rather than the business office.

As a result of the West Palm investigation, a top-selling Service Technician and his manager were terminated. Additionally, a Network Operations Manager was retired at the Company's option, and a Customer Services Operations Manager and the Network General Manager for Southeast Florida were counselled and received financial penalties.

The terminated employees were those originally suspected in 1988 who produced high volumes of suspect referrals that were refused processing by a Customer Services manager. Since inadequate handling of a clearly improper situation allowed this top-selling employee to continue to operate for two additional years, thousands of additional customers may have been wrongfully charged for services not requested.

4.4.3 Miami 1990

After the investigation of the West Palm Beach non-contact sales operations, the Security investigation moved to the South Florida area. Interviews were conducted during November 1990. While the investigation did not result in dismissal and identification of specific falsified sales, it did note practices identical or similar to those used to generate improper sales in the West Palm Beach and Orlando areas. Many of these control weaknesses and improper methods were reported to have occurred during 1988 and 1989 in South Florida.

Among the control problems and questionable methods noted were: sales to customers already subscribing to a particular service, sales on lines with disconnected service, sales referrals for telephone numbers in numerical sequence and address sequence, referral forms not reviewed by managers and suspicious referrals not investigated, employees designated for full-time sales, employees selling from their homes and working overtime on sales, brochures or fliers provided to cause customers to request new service through non-contact employees, boiler-room operations, sale of Custom Calling features to pay phones, and sales that resulted in reduced Company revenue but producing individual sales credit.

5.0 MANAGEMENT'S RESPONSE

5.0 MANAGEMENT'S RESPONSE

5.1 Lack of Corrective Action: 1985-1989

As revealed in the various incidents described throughout Section 4.0, the eventual resolution of evidence of improper activity all too frequently did not include corrective action by Company managers at many levels. A common thread running through many of these incidents was that such evidence was either passed on to others for review, or merely explained away and ignored. For most of the period 1985 through 1989, Company management missed opportunities to pursue and detect sales fraud, and then to discover and correct the control weaknesses that allowed the fraud to occur.

For example, as early as 1987 in Orlando, an employee was suspected of improper sales, but was not fired until 1990, after a security investigation was finally requested and conducted. Due to inadequate follow-up by the Network Sales Coordinator, the selling employee's manager, and managers to whom each of these reported, the resolution of this problem and proper corrective action was delayed for years.

Similarly, suspicions about the top seller in West Palm Beach which began in 1988 were not adequately pursued to resolution until his termination in 1990. This lost opportunity to expose the improper activity resulted from simple failure by the Customer Service Department managers to contact Company Security or the Network managers involved.

Direct involvement or tacit cooperation on the part of other Network and Customer Services managers involved also presented a roadblock to investigating and correcting the underlying problems. As noted, one of the terminations resulting from 1990 West Palm security investigation was a manager who defied warnings that his employee was generating false sales. He was also assisted by the cooperation of a Customer Service Department manager who agreed to process these sales. Despite these difficulties, lower level managers were the first line of defense for preventing and detecting abuses. In many cases, the disciplinary actions later taken by the Company against 4 levels of managers indicate that certain managers "dropped the ball" in discovering, investigating or correcting abuses within their organizations. As indicated in the response to Staff's 17th Request for Production of Documents, Item 1, the grounds for these disciplinary actions clearly state that the Company found most of these managers to have "inadequately investigated complaints of improper activities."

A series of 1988 memoranda indicate that upper management also failed to correct problems that led to abuses. In May 1988, the South Florida Network Operations General Manager directed a Network IMC/I&M Support Operations Manager to develop suggestions for standardizing the sales programs, and to discourage the use of "boiler rooms" and canvassing sales techniques. In this request, the South Florida General Manager refers to a recent meeting with the Network Vice-President and the other two Network Operations General Managers, where the use of boiler rooms apparently was discussed.

In response, a June 1988 memorandum was produced by the Network IMC/I&M Support Operations Manager, transmitting the requested suggestions to all three Network Operations General Managers. One improvement suggested was enforcing proper use of the NSR-86 form, requiring that the customer's signed authorization be verified by Customer Services before processing the sale. Another suggestion was for Network Staff to conduct periodic spot reviews and direct telephone call verification with customers of reported sales. According to the South Florida General Manager's deposition, however, these suggestions were apparently not implemented. This incident reveals that Company upper management was aware as early as mid-1988 of potential problems with current sales practices and the need for improved controls, but that incomplete action was taken to follow through on this need.

Management did not adequately pursue potential evidence of wrongdoing and adequate control improvements despite the clear early warnings provided by the 1986 North Miami and 1987 Miami Metro incidents that resulted in terminations of 3 employees for fraudulent sales. Since a security investigation was conducted in the Miami Metro case, the resulting report informed managers such as the South Florida Network Operations General Manager, Personnel General Manager and corporate Assistant Vice President of Security of the incident. The occurrence of these two separate incidents close together should have caused concern among all levels of management, and increased attention to preventing and investigating any additional cases. Instead, the subsequent occurrences received less than adequate attention from management.

Disciplinary action taken against a Network General Manager, who reported directly to the Network Vice-President, indicates some responsibility for sales fraud problems lies with the highest levels of the Network Department. The early detection and protracted resolution of the West Palm Beach sales fraud was documented by the Company's Security Department investigation. According to the Response to Staff's First Set of Interrogatories, Item 12, the disciplinary action against the Network General Manager was imposed by Southern Bell due to his "[f]ailure to manage responsibilities properly and failure to exercise satisfactory judgement."

5.2 Investigations And Audits: 1990

During 1990, Security Department investigations finally triggered a chain of events that led to widespread activity to expose and curb abuses related to non-contact sales incentive programs. As discussed in section 4.4.1, in June 1990, the Operations Manager-Network in Orlando requested a Security Department investigation into possible fraud. After the completion of the investigation in October 1990, the Company's General Attorney for Florida requested additional interviews be conducted to determine whether there might be possible involvement by other employees.

On October 16, 1990 the Company's General Attorney requested the Internal Audit Department to complete an audit of non-contact sales. On October 18, the BellSouth Corporation General Attorney requested the Security Department to conduct an internal investigation of Inside Wire Maintenance/TIP (Trouble Isolation Plan) service within Florida. Southern Bell has stated that it notified the U.S. Attorney, the Florida Attorney General, and members of the Public Service Commission later in October 1990.

As part of the identification process, and in conjunction with the investigations, the company extracted employee sales data for the highest sales producers, and those employees found to have submitted unauthorized order referrals. This information was used to scrutinize high sales producers for possible fraudulent actions.

Upon completing the identification of the problems associated with the non-contact sales program, Southern Bell began a series of disciplinary actions against employees. Also, Southern Bell identified and notified customers potentially affected by improper sales practices, and issued refunds to customers.

5.3 Employee Disciplinary Actions

Exhibit 8 shows the number of disciplinary actions taken against employees involved in all sales-related incidents during the years 1986-1991. All 36 employees formally disciplined during the period 1986 through 1991 received the disciplinary action because they were found by the Company to have either engaged in improper sales practices, because they knew or should have known of such practices, or because they failed to take appropriate management action. By far the largest number of disciplinary actions took place in 1990, as a result of the security investigations of non-contact sales programs. It should be noted, however, that the employees disciplined in 1990 had actually committed the various infractions and violations during the years 1987, 1988, 1989, and 1990. Therefore, the fact that most of the related discipline was meted out in 1990 does not mean the improper activity was limited to the year 1990 alone.

The 24 employees disciplined in 1990 included 5 Customer Service Department employees engaged in their normal customer contact sales activities. In addition, one Customer Services Department manager and 18 Network Department employees were disciplined for actions or omissions related to non-contact sales. Of these 18 Network employees, 15 or 83% were management employees, and 3 or 17% were craft (non-management) employees.

Although numerous non-contact employees may have participated in the sales programs over the years, the number of disciplinary actions taken represent enough abuses to question the adequacy of controls involved. Based upon the statements made by employees in the Company's Security Department investigations, it would also be unrealistic to believe that all of the employees involved were detected or identified In addition, the number of employees involved, their geographical distribution, and the timeframe associated with these disciplinary actions contradict a claim that abuses were limited to a few isolated incidents of improper activity. These violations involved dozens of employees and were detected in all three of the Company's state regions over a seven-year time period.

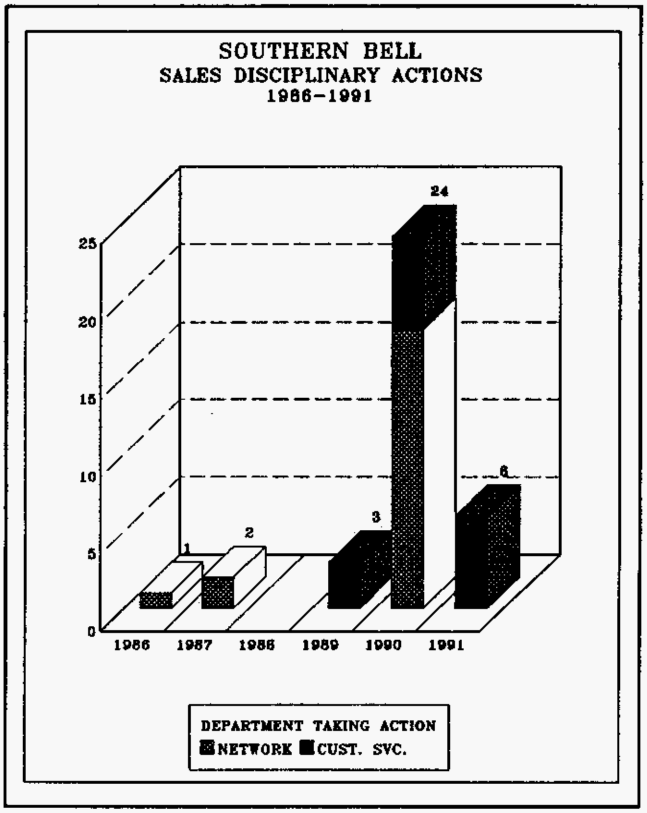

EXHIBIT 8 *SOURCE: Staff POD 17, Item 1; Staff 1st Interrogatories, Item 12.*

Three of the terminated Network employees admitted to adding unauthorized services to customer bills. Every other Network employee who was disciplined as a result of the investigations denied any improper conduct, or in the case of management employees, denied knowing of, or authorizing, improper employee conduct. All disciplined employees were required to return prizes earned through sales programs to the Company.

5.3.1 North Florida

A total of 13 disciplinary actions were taken in 1990 against employees in the Orlando area, which is included in the Company's North Florida region. As a result of the September 1990 Orlando internal investigation described in Section 4.4.1, the Company terminated three employees directly involved in adding unauthorized services to subscriber's billing. In addition to the terminations, the disciplinary actions taken included the two-week suspension without pay of two Managers and one Assistant Manager, and the counselling of one Operations Manager, one Manager, one Support Manager, and three Assistant Managers. The basis for these actions as stated by the Company in these employees' personnel record entries included "mismanagement", "failure to properly utilize employees in their proper work assignments", "failure to adequately investigate complaints of improper activity", "failure to properly supervise subordinates", and "failure to exercise satisfactory judgement."

An investigation of other divisions within the North Florida area resulted in 1990 disciplinary action against a Jacksonville Service Representative who received counseling as a disciplinary action. Three Service Representatives in Cocoa were also suspended in 1989 for falsely reporting sales items on service orders.

However, according to the deposition of the Operations Manager who was counselled, an additional employee had been terminated in 1988 ostensibly for performance and attendance problems, when she was known to be generating false sales. During the last eighteen months of her employment, she was credited with nearly 15,000 sales of wire maintenance plans.

5.3.2 Southeast Florida

In 1990, a total of 11 employees in three locations within the Southeast Florida region received disciplinary actions. As a result of the West Palm Beach investigation, seven Network Department employees received disciplinary actions by the Company. These included a Manager and a Service Technician who were terminated, an Operations Manager was retired at the Company's option, an Assistant Manager who received two weeks suspension without pay, and an Administrative Support Manager who was counseled. Most significantly, the Southeast Florida Network General Manager, who reports directly to the Network Vice President, was also disciplined and was denied incentive pay compensation for 1990 and 1991. The Company's grounds for the actions against the other employees included "failure to adequately investigate complaints regarding improper activity" and "misconduct that resulted in certain subscribers being charged for certain services they neither requested [n]or authorized."

The Customer Services Department employees disciplined in 1990 included one Operations Manager and one Service Representative who were counselled, one Service Representative who was suspended, and a third who was terminated. The latter three were disciplined for adding services customers did not authorize in the course of their normal contact sales roles. However, the Operations Manager was found to have inadequately handled evidence of the West Palm Beach non-contact sales falsification.

In 1991, six additional employee disciplinary actions relating to sales violations were taken by Southern Bell. The Southeast Florida region accounted for three employee disciplinary actions involving Customer Service Representatives. In incidents stemming from their normal contact sales activities, one Service Representative in Fort Lauderdale was terminated for adding services to customer records that were not requested or authorized, a second in Fort Pierce was suspended for the same cause, and a third in West Palm Beach was warned for "involvement" in similar actions.

5.3.3 South Florida

The earliest terminations resulting from improper non-contact sales occurred in the South Florida region's North Miami and Miami Metro districts. There, one employee was discharged in 1986, and two were discharged in 1987. In each instance these terminations stemmed from the investigation of customer complaints of services being added to their accounts without authorization. These events provided warning signs that should have been heeded in subsequent years. However, when the same signals were observed later, they were not adequately investigated and resolved.

In the South Florida region, there were three employee disciplinary cases relating to customer contact sales during 1991. One Miami area Service Representative was terminated for adding services without proper authorization and two others were warned for the similar activity.

5.4 Refunds To Customers Affected

Beginning in 1990, the Company implemented efforts to identify the scope of misbilling associated with the non-contact sales program revealed by the Orlando investigation. These efforts centered around identifying and notifying customers thought to be affected. Since the Orlando investigation focussed on two employees who had produced unusually high sales of the Inside Wiring Maintenance Plan, an effort was made to identify other possible fraud by employees with the highest levels of sales. However, these analyses produced no other suspects. According to the Company, the customers identified as having services added by these employees were notified by letter and given refunds.

According to the Company's response to Staff's 3rd Set of Interrogatories, Item 32, all Florida customers who were sold services through non-contact sales programs were contacted by mail and asked to review the accuracy of the services for which they are being billed. In July, 1991, the Southern Bell of Florida President ordered approximately 140,000 letters sent to selected customers, in an effort to notify customers that had potentially been affected by unauthorized employee upgrades of customer services statewide.

By order of the Commission, weekly refund status reports have been submitted since January 1991. As of September 30, 1991, Southern Bell had refunded a total of $804,515 to 33,830 customers who had services added to their bills improperly through the non-contact sales incentive programs. According to the Company's response to Item 28 of Staff's 3rd Set of Interrogatories, as of October 1992, final totals of refunds were not yet available.

Under the terms of the October 1992 settlement with the Office of Statewide Prosecution, the Company has also agreed to refund $10,500,000 to customers who were sold services through non-contact sales programs. In addition, the Company agreed to an extended controls and procedural review process to be conducted by an outside consultant.

6.0 FINDINGS AND CONCLUSIONS

6.0 FINDINGS AND CONCLUSIONS

6.1 Adequacy of Controls: 1990 and Prior

Conclusion 1: **Southern Bell did not provide adequate internal controls in its non-contact sales incentive programs to prevent or detect the improper billing of customers.**

Southern Bell did not have adequate controls in place to prevent non-contact sales employees from improperly billing customers prior to 1990. Although controls were improved during 1990, sufficient internal controls were still not in place to prevent possible improper billing of customers as of 1991, when non-contact sales incentive programs were eliminated. The lack of sales order verification with customers was the most important control weakness allowing employees to continue to add unauthorized services.

Finding 1: Controls Over Sales Referral Processing And Verification Were Inadequate.

During the period 1986-1991, controls over sales referrals failed to prevent Southern Bell employees from generating unauthorized customer orders for services. In each of the incidents, controls were circumvented simply by submitting unauthorized order forms for adding services to customer bills.

Several weaknesses in sales referral processing controls allowed these unauthorized customer billings to occur, including:

- the processing of sales referrals without completed customer contact and signature information
- the failure of managers and supervisors to verify sales referrals with customers to check their validity
- the failure of Customer Service Representatives and Service Order Typists to verify suspect orders against customer billing records
- the simultaneous use of different methods and locations for processing of referrals
- allowing employees to circumvent controls by finding the processing method that offered the weakest control checks.

Additionally, the lack of uniform Network procedures assigning specific responsibilities for verifying non-contact sales referrals to managers, supervisors and business office representatives served to weaken controls over the process. District sales coordinators, supervisors and managers also admitted that they did not verify orders, and there were no procedures requiring such actions.

The only verification routinely performed was by the Customer Service employees who typed orders into the Direct Order Entry system. They compared the referral order with the customer billing record to assess whether the service requested was currently being billed. However, this did not guarantee that the sale was legitimate, only that the service had not already been sold to that customer.

These control weaknesses in processing sales referrals allowed unauthorized orders to be issued without being detected unless customers monitored their bills and reported the problem. Ultimately customer complaints about unauthorized billings, and not internal controls, led Southern Bell to recognize these problems existed.

Finding 2: Non-Contact Employees Received Little Training And Guidance In Proper Sales Methods.

Employee interviews and Company Security investigations indicate that little attention was given to training non-contact sales employees in proper sales methods and techniques. Usually sales duties were relegated to a few employees interested in working full-time in sales, or to light duty personnel used for telephone solicitation because they could not perform their normal duties due to injury or illness.

Sales training generally consisted of employees observing other employees successful in making sales. While this informal method was better than no training, it did not necessarily insure the use of professional and ethical methods. Security investigations revealed that methods of circumventing controls were passed on through this type of informal training, sometimes with the consent of managers.

The absence of formal sales training in accepted methods and sales techniques left managers and non-contact sales employees to determine their own methods and techniques for reaching sales goals. The lack of formal sales training placed managers unfamiliar with sales methods in the position of providing whatever training they could, contributing to inconsistency among methods used in different areas of the Company. As a result of the lack of sales training and procedures, in some quarters improper practices became a routine method of producing sales.

Finding 3: Lack of Non-Contact Sales Internal Audits and Network Staff Reviews Hindered Detection Of Control Failures.

Although the IMC/I&M Support Staff organization performed operational and compliance reviews in other areas of Network Operations, no such reviews were performed for the Network Department's sales programs. The only evidence of Network IMC/I&M Support Staff reviews of non-contact sales programs was an assessment conducted in 1988 at the request of the South Florida Network Operations General Manager, as described in section 5.1. This assessment offered recommendations for improvement that were never implemented by the Florida Network Operations General Managers and Vice-President.

Regular Network Staff reviews should have been performed to evaluate whether programs were being conducted according to standards, and whether improvements to the programs were necessary. Similarly, periodic internal audits of the sales incentive programs would have helped identify weaknesses in controls and assess the need for control improvements. The absence of regular Network Staff reviews and internal audits of the non-contact sales programs contributed to the control failures by allowing improper activities and practices to continue undetected throughout the period evaluated in this audit.

One advantage of a review or audit function performed by a separate group is the company-wide or macro perspective of such a group. This often allows quicker identification of trends throughout the Company. For example, individual Network Department managers may not have been aware of incidents in other districts, whereas auditors may have been able to recognize patterns and similar recurrent problems observed in audits of other districts.

Finding 4: Procedures For Tracking Employee Time Spent In Non-Contact Sales Were Inadequate.

The proper reporting of employee time spent in sales activities was important to maintaining the separation of regulated and nonregulated expenses and in tracking and reporting program expenses accurately. Until August 1988 there were no Southern Bell procedures for tracking non-contact sales activities separate from regular duties. In addition, there were no procedures to capture separate non-contact sales time spent in regulated and non-regulated services.

29 Employee interviews, Security investigations and
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31 Without proper time reporting of non-contact sales activities to the individual incentive programs Southern Bell would not have been able to accurately track the expenses associated with each program.

Conclusion 2: **The actions and omissions of Network Department management led to the improper billing of customers.**

Sufficient evidence exists to conclude that Network Department management did not fulfill its obligation to properly manage the non-contact sales function. Some managers appear to have encouraged improper billing of customers. Other managers failed to adequately investigate evidence of improper activity, thereby extending the duration of intentional misbilling of customers. In general, management created an atmosphere stressing the desired end (i.e., sales and revenue generation) without appropriate attention to the means used.

Finding 5: Management Did Not Investigate Evidence Of Improper Sales And Misbilling In A Timely Manner.

As discussed earlier, all levels of Company management missed opportunities to identify improper sales activity by failing to adequately investigate customer complaints or reasonable evidence of improper activity by Company employees. These complaints were not disjointed, isolated incidents. Instead, their frequency and similarities should have provided a warning that action was required.

Since sales falsification was not limited to one location, one employee, or one time frame, the widespread nature of this failure represented a systemic problem. Security investigations repeatedly revealed that managers of employees generating questionable referrals considered the number of customer complaints very small, compared to the large number of orders being processed, and did not feel there was a problem. Managers did not look beyond the immediate problem to determine what other problems may have existed with employee sales referrals.

No incentives existed to prompt managers to aggressively pursue non-contact sales problems. Obstacles to uncovering and resolving these problems included:

- a lack of written procedures requiring managers to verify the integrity of orders
- upper management emphasis on enhancing non-contact sales revenues
- reluctance to discourage honest sales by appearing suspicious
- competition among managers to increase revenues
- direct personal benefit for improper sales through sales incentive awards
- the impact of sales on other management compensation, such as MTIA and IIA awards.

These factors may have deterred some managers from aggressively pursuing the symptoms of the deeper problems with the sales incentive programs. Whatever the cause, management appears to have been unaware or unconcerned about the possibility of sales fraud and did not create an atmosphere of dealing aggressively with improper activity.

Because management failed to provide proper controls, employees easily circumvented the ones that were in place, while simultaneously reaping personal financial gains, winning recognition from their supervisors, and enhancing the Company's bottom line. Since they did not create an atmosphere which inhibited the acceptance of fraudulent activity, top managers appear to have either placed an inordinate degree of trust in human nature, or were not serious about controlling possible abuses. Because managers frequently did not aggressively pursue the evidence of wrongdoing, the problems of sales fraud through unauthorized billings continued to grow until 1990, when the problem could no longer be ignored.

Finding 6: Management Did Not Improve Non-Contact Sales Controls In A Timely Manner.

Although numerous incidents of unauthorized billings and improper practices continued to take place during the period 1985-1990, Southern Bell did not take adequate and timely actions to effectively improve the non-contact sales controls. Well before 1990, the use of boiler-rooms was known to Network General Managers as were the improper acts of terminated employees. Patterns of customer complaints, and allegations between the Network and Customer Services Departments were numerous and could not have escaped the attention of upper management.

The result of this delay was that customers continued to be improperly billed for services not requested, while the Company profited. At worst, the Company's actions imply it felt there was no incentive to give up this additional source of revenue. At best, this failure implies a degree of carelessness, naivety, or incompetence.

Still, until 1990 and the development of Goldline, no substantive response to these obvious problems was made by Company management. Although Goldline included some improved controls over sales referrals, it also contained control weaknesses. Finally, in 1991 the Company's President discontinued Goldline, ironically bringing non-contact sales programs to an end without ever correcting the underlying problems.

6.3 *Adequacy of Present Controls*

Conclusion 3: **If Southern Bell resumes the use of a non-contact sales incentive program based upon Goldline, additional controls are needed to prevent the recurrence of improper billing of customers.**

As of July 31, 1991 the Company discontinued non-contact sales incentive programs. However, at the time these sales programs were discontinued, Southern Bell had not implemented adequate controls to prevent the recurrence of fraudulent billings. If in the future, the Company bases a new program on Goldline, or introduces a new program with similar controls, an examination of the adequacy of these controls is warranted. The greatest need is for verification of all sales, not just those involving new or transfer customers.

The Goldline program, instituted in April 1990, improved the verification of sales somewhat, through greater separation of duties between those employees referring sales and those making sales. After receiving a sales referral from the Goldline Center, the Customer Services or Marketing Department employee contacted the customer and completed the sale. The referral from another employee insured the existence of a legitimate potential customer. However, there was no further verification after the sale to be sure that the customer received only the service(s) authorized.

Since the sale was both made and reported by the contact employee alone, this afforded the opportunity to report a fictitious sale. According to the Company's response to Staff's Third Set of Interrogatories, Item 45, the control that would discourage such activity is the routine monitoring of (listening to) contact sales personnel by supervisors. Each quarter, a minimum of 18 customer contacts by each service representative are monitored to verify proper customer handling and sales technique. This control can deter or detect some fraudulent activity. But, more complete protection is needed to ensure that the customer is billed only for what he/she agreed to buy.

More complete protection against false sales would require additional follow-up by the supervisor. This follow-up should include verifying the conversation monitored against the printed sales order. Monitoring procedures do not currently include these verification steps. Neither the Company's sales performance evaluation practices (BSP 735-800-01SV) nor the *Observer Guidelines for Contact Referral* provide for such verification on a routine basis. Instead, sales calls are evaluated on: "recognized opportunity, discovering, proposing, and assuring", and "courtesy, accuracy, overall call handling, and bridging/sales techniques." The *Contact Observer Guidelines* do state that if a manager hears a potential ethics violation while listening to a call, the sale should be more closely examined. However, simply listening to the monitored calls without reviewing the corresponding sales orders leaves the Company at risk for the most common methods of adding false sales that have been documented.

An additional problem with sales conversation monitoring is that no matter how many sales conversations are observed, the fraudulent reporting of sales from conversations that never took place at all, would still escape detection. No matter how large a sample of each employees' sales are monitored, an employee could simply report a sale made from a referral without ever contacting the customer.

6.4 *Further Action*

Although the Company is not conducting any non-contact sales incentive programs, past control problems are nevertheless relevant to the Company's ongoing efforts to sell its optional services. Based upon the control problems described in this report, the following actions should be strongly considered:

1. Require the Company to provide customers with a complete itemization of services billed in each monthly statement.

2. Require the Company to obtain written authorization from customers before additions of optional services are made to customer bills.

3. Require the Company to perform a review of sales practices and procedures employed by the Company's customer service representatives and other contact sales personnel.

4. Require the Company to perform a review of the time recording practices currently employed in the sale of regulated versus non-regulated services by the Company's customer service representatives and other marketing personnel.

7.0 APPENDIX

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7.1 Glossary of Terms and Acronyms

BOCRIS (BUSINESS OFFICE CUSTOMER RECORD INFORMATION SYSTEM) - A business office record information system, replacing IBOSS, providing customer billing and order information.

BOILER ROOMS - Unofficial centers of sales activity where Network employees were assigned to solicit sales of optional services to customers via telephone.

CAPRI (COMPUTER ASSISTED PURCHASING, RECEIVING AND INVOICING SYSTEM) - The BellSouth purchasing system used for ordering and tracking employee award choices from the awards vendor catalog.

CPE (CUSTOMER PREMISES EQUIPMENT) - Telephone sets, jacks and other customer-owned equipment located on the customer's premises beyond the network protector, or point of demarcation.

CRIS (CUSTOMER RECORD AND INFORMATION SYSTEM) - Billing and customer information operating system.

CRSAB (CENTRALIZED REPAIR SERVICE ATTENDANT BUREAU) - One of two trouble report receiving facilities, located in Jacksonville and Miami, which generate and route trouble reports to the nearest IMC.

CSR (CUSTOMER SERVICE REPRESENTATIVE) - Customer Service Department employees responsible for negotiating and inputting customer orders for new service, changing existing service, relocating service, removing service and answering billing inquiries.

DC (DISPATCH CLERK) - Network Department clerical support employees who assign installation and repair orders to service technicians and process the completed orders for billing.

DIALAMERICA - Atlanta-based telemarketing contractor used by Southern Bell to perform special promotions and assist with the processing of non-contact sales orders.

DOE (DIRECT ORDER ENTRY) - A system used to enter and track information for customer service orders.

GOLDLINE - Company-wide sales incentive program employed during 1991 to process sales referrals for all Southern Bell services through a centralized referral point.

I&M (INSTALLATION & MAINTENANCE) - Area of Network operations involving repair and installation of service.

IBOSS (INTERIM BILLING AND ORDER SUPPORT SYSTEM) - A system providing the business office with customer billing information used to negotiate sales and discuss customer billing problems.

IIA (INDIVIDUAL INCENTIVE AWARD) - Annual lump sum payment awarded to selected managers based upon the individual performance of the employee and the amount of the award pool.

IMC (INSTALLATION AND MAINTENANCE CENTER) - Network Department operations unit usually responsible for trouble report handling, monitoring, and dispatching functions.

MA (MAINTENANCE ADMINISTRATOR) - IMC employees responsible for screening, testing, dispatching, monitoring, and resolving trouble reports.

MATCH - Sales incentive program in which Network employees referred sales leads to Customer Services Representatives, sharing sales credit upon completion of a sale.

MTIA (MANAGEMENT TEAM INCENTIVE AWARD) - Annual lump-sum payment to selected management employees based upon the overall financial performance of the team (state organization) and the individual manager's performance level.

MTR (MECHANIZED TIME REPORTING SYSTEM) - Computer system for tracking and categorizing employee time spent in various activities designated by job function codes.

NSR-86 (NON-CONTACT SALES REFERRAL FORM) - The printed form used for recording, transmitting, and inputting sales by non-contact employees.

OPT (OUTSIDE PLANT TECHNICIANS) - Field technician responsible for repair of existing distribution cable and plant facilities.

RSA (REPAIR SERVICE ATTENDANT) - CRSAB employees who receive initial repair calls from customers, recording pertinent information to originate a trouble report.

SOCS (SERVICE ORDER COMMUNICATION SYSTEM) - Computer system used to process marketing and special service orders and provide order information to marketing representatives handling customer billing and order requests.

SOT (SERVICE ORDER TYPIST) - Customer Service Department employees responsible for inputting service orders to DOE.

ST (SERVICE TECHNICIAN) - Field technician responsible for installation of new service and repair of network facility and equipment problems.

TIP (TROUBLE ISOLATION PLAN) - Service for locating repair problems within customer premises or network facilities.

USOC (UNIFORM SERVICE ORDER CODE) - Alpha-numeric code used to identify each service or product billed to customers.

VAX - Computer operating system for processing and tracking CPE sales by Marketing personnel.

WC (WORK CENTER) - A central reporting location for service technicians and other employees involved in field related activities.