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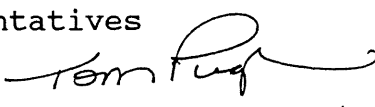
Minnesota House of Representatives

Dee Long, Speaker

COMMITTEES: ENVIRONMENT AND NATURAL RESOURCES FINANCE; JUDICIARY;
JUDICIARY FINANCE DIVISION ; LOCAL GOVERNMENT AND METROPOLITAN AFFAIRS

June 23, 1993

TO: Members and Staff
Minnesota House of Representatives

FROM: Representative Tom Pugh 
For the Special Committee on House Management

Enclosed for your information is the final report of the Special Committee on House Management Practices on the subject of telephone controls. It is a revised version of the draft report that was reported in the newspapers in late May; this final version is altered in some important particulars but not in its general thrust.

For your convenience I've enclosed also a three page document that summarizes the "highlights" of the report. This document outlines the problems that the committee identified, and the solutions that the committee recommends.

Attached to the report are several supporting documents that I thought members might find particularly useful and interesting. This is by no means all the documentation collected by the committee: other materials (available from the committee) are listed at the end of the report.

As you know, the Attorney General issued on June 7 a report on "The Unauthorized Use of Rep. Alan Welle's State Telephone Access Code." I have enclosed a copy of that report, for your information only. The Humphrey report was not part of the record that was considered as the basis for the report of the Special Committee, nor does the Humphrey report represent findings or conclusions of the Special Committee.

You will note differences in these reports. These differences are due in part to their different purposes and scope. The Humphrey report is the product of an investigation that aimed to "discover any misconduct by state employees or officials" (Humphrey report, page 7). By contrast, the Special Committee's charge was neither to investigate nor to assign culpability to



individuals; our charge was rather to examine House management practices and internal controls. (The second page of the committee's report describes more fully the committee's view of the scope of its responsibility.) Because of this difference in purpose, the Humphrey report and the Special Committee's report examined somewhat different issues and subjects, sought different types of information from different sources, and arrived at divergent conclusions on some matters.

I may be calling a meeting of the Special Committee to review the Humphrey report and probe some of the differences in fact and interpretation.

Highlights

Final Report on Telephone Controls

Special Committee on House Management Practices

June 23, 1993

In the autumn of 1991, the state suffered two costly incidents of toll fraud on state WATS lines. Perpetrators used the state's "InWATS" system, which allows access to state WATS lines from anywhere in the country, through the use of telephone access codes.

- The Department of Administration, as the state's telephone system administrator, is responsible for designing the InWATS system and contracting with commercial carriers for service. The House, Senate, and state agencies purchase InWATS service from the department.
- Remote access services, like the state's InWATS system, are susceptible to fraud perpetrated by persons using either an errant access code or a code acquired in various ways by illegal call-sale operations. Customers, not commercial carriers, pay the bill for this fraudulent use. Federal investigators estimate that loss to toll fraud on these systems exceeds \$2 billion annually.

One of the 1991 fraud incidents involved a telephone access code assigned to a member of the House of Representatives, the other an access code assigned to the Department of Natural Resources (DNR). Together, the two fraud incidents cost the state more than \$140,000. But, by using the InWATS system for long distance calling rather than credit cards, the state has saved close to \$3,000,000.

- The misuse of the House access code cost the House more than \$87,000. The misuse of the DNR code cost about \$57,000
- The state has experienced only three other known incidents of toll fraud since 1988, and none of these involved significant losses.
- The state has saved about \$500,000 annually since 1988 by using InWATS rather than credit cards. The House has saved about \$350,000 since 1984.

The Special Committee on House Management Practices was established by House Resolution No. 5 on March 24, 1993. The Committee was directed by the House to identify the deficiencies in management controls that permitted the toll fraud against the House and the changes needed to reduce the risk of such incidents in the future. The next two pages summarize the Special Committee's conclusions on these matters.

Problem: The InWATS system suffered from two technical deficiencies that delayed detection and interdiction of fraud. First, the system did not employ continual monitoring of long distance calls as a fraud detection method. In both the DNR and House incidents, the Department of Administration detected the misuse of the access code only after the fraud was so massive that the calls overloaded the state's WATS lines. Second, the system did not provide rapid reporting of call detail to users. Call detail reports arrived with WATS bills late in the month following the month in which the charges occurred.

The Department of Administration is correcting the technical deficiencies in the InWATS system. For its part, the House in 1992 made sweeping changes in the design of its InWATS services. Of the 134 House members, 108 members now must use a "corporate home account" for long distance calling from home. All members must use credit cards for long distance calling when away from home and office. These changes were made in July 1992 and substantially increased the security of the House system and lowered the House's financial exposure. The committee recommends continued efforts to take advantage of improved security technology.

Problem: The effects of technical deficiencies in the InWATS system were exacerbated by weaknesses in system administration. Poor interagency communication, confusion about agency roles and responsibilities, and inadequate procedures for detection, interdiction, and investigation all impaired the state's response to the fraud incidents.

The committee recommends that the Department of Administration correct these administrative deficiencies. The committee also recommends that House leadership take appropriate steps to further investigate the fraud perpetrated against the House and to secure restitution.

Problem: Current state law and administrative procedures do not provide adequate standards requiring state employees and officials to report suspected fraud involving state property.

The committee recommends that the legislature strengthen and clarify the legal requirements for reporting fraud involving state property.

Problem: The House's open office environment, although it fosters public access, is a potential security problem.

The committee recommends that House Administrative Services consider increasing security on unattended office telephones by September 1, 1993.

Problem: State and House policies on telephone use were unclear and poorly communicated to members and employees.

The committee recommends that the House adopt official policies on telephone use by September 1, 1993, and communicate those policies effectively to members and employees.

Problem: The law making telephone records private data, as interpreted and implemented by House administrators, adversely affected the detection and interdiction of toll fraud involving House WATS lines.

The enactment of House File 1377 (Laws 1993, Chapter 370) corrects this problem.

Problem: Monthly WATS bills were not subject to adequate review within the House. First, members and employees did not routinely see or review their individual WATS bills. Second, the Director of House Administrative Services did not use effective procedures to review WATS bills.

These problems the House has already largely corrected, by changing bill review procedures. The committee recommends additional changes to further strengthen the internal review of monthly House WATS bills.

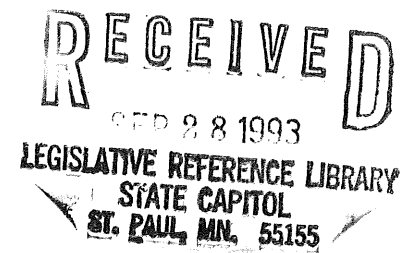
Problem: The responsibility for approving House expenditure abstracts was not, and is not, clearly delineated in practice. The speaker and the chief clerk, who bear the legal responsibility for approving and signing expenditure abstracts, did not routinely review, sign, or even see the abstracts.

The committee recommends a reevaluation of House procedures for reviewing expenditure abstracts.

Problem: The independent financial audit of the House in 1992 should have mentioned the telephone fraud.

The committee recommends that the House Rules committee define the scope of future financial audits of the House. Audit reports should be presented at public meetings of the Rules Committee and distributed to each House member.

**Special Committee
on
House Management Practices**



Final Report on Telephone Controls

June 23, 1993

The Special Committee on House Management Practices was established on March 24, 1993, by House Resolution No. 5.

The resolution directed the committee to examine the recent breakdown in controls over long distance telephone charges. The committee was directed to report to the House by April 14, 1993, on "the practices which permitted the breakdown in controls and the extent to which such practices have been changed."

The members of the committee were duly appointed by the speaker, also on March 24, 1993.

The members are:

Representative Thomas Pugh, Chair
Representative Marc Asch
Representative Dave Bishop
Representative John Dorn
Representative Dave Gruenes
Representative Sidney Pauly
Representative Tim Pawlenty
Representative Ann Rest

The committee produced an interim report on April 14, 1992. This is the final report of the committee on the subject of telephone controls.

Scope of the Report

The Special Committee's charge from the House, as expressed in Resolution No. 5, was to identify the management and administrative practices that permitted the telephone toll fraud loss that the House suffered in 1991. In accordance with this charge, the findings and recommendations in this report are addressed to systemic issues of management, administrative practices, and internal controls of the long distance telephone system.

The Special Committee did not conduct an investigation of the fraud or seek to evaluate or make judgments about the responsibility of individuals. The report describes the behavior of administrators and officials in responding to the 1991 toll fraud incident only insofar as this behavior illuminates or illustrates prevailing management and administrative practices. This was a deliberate decision by the committee. It was not the charge of the committee to investigate, determine, or make recommendations about the civil or criminal liability of private parties, public employees, or elected officials involved in the incident. The Attorney General and the Ramsey County Attorney both are conducting independent investigations for those purposes. The chair and the committee decided that the committee should avoid duplicating or interfering with those investigations. Neither was it the charge of the committee to question or investigate the personal ethical behavior or responsibilities of members of the House. This is the jurisdiction of the Ethics Committee. In fact, the confidentiality requirement of House Rule 6.10 enjoins the committee from including in this report any complaints about ethical violations. Accordingly, this report does not examine or issue recommendations on such matters.

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Executive Summary

What occurred in the toll fraud incident in 1991?

In the autumn of 1991, the state suffered two incidents of toll fraud practiced on state WATS lines. One of the two incidents involved a telephone access code assigned to the DNR, the other a code assigned to a House member. The two incidents together cost the state more than \$140,000.

Perpetrators of the fraud used telephone access codes that allowed access to the state WATS lines from anywhere in the United State. This remote access to state WATS lines is referred to as "InWATS" service. The House, Senate, and state agencies purchase InWATS service from the Department of Administration (Admin). As the state's telephone system administrator, Admin is responsible for designing the InWATS system and contracting with commercial carriers for service.

Admin and House staff believe that the fraudulent use of the House code began in the spring of 1991, probably in March, and mounted slowly through the summer, reaching very high levels in October and November. From January through August, 1991, the monthly WATS phone bill of the House varied between about \$15,000 and \$19,000, which was a normal level of use for the House. In September, the bill mounted to over \$23,000; in October, to well over \$36,000; in November, to \$59,000. (The total cost to the House of fraudulent use during this period was over \$87,000.)

Admin first discovered the fraud on November 14, 1991, when the state's InWATS lines became overloaded. On November 20 or 21, after following a series of detection steps, Admin was able to trace the likely source of the abuse to House access codes. Admin notified the director of House Administrative Services (HAS) (David Kienitz).

Overnight on November 20, as a preventive measure, Admin shut down legislative InWATS and routed calls to a recorded message. On November 21, as an investigative measure, Admin reopened legislative InWATS but redirected all legislative calls from computer routing devices to operators. By interviewing callers, Admin telephone operators were able to identify the access code that was being abused. By examining the call detail record (which was not available to Admin, for reasons of data privacy), the HAS director was able to identify both the access code that was being abused and the member assigned to that code. The HAS director notified Representative Welle, who was the member assigned to the code and also the newly elected House majority leader. The offending code was discontinued by Admin at the HAS director's request on November 21.

The two responsible House administrators -- the director of HAS and his supervisor, the House's staff director (Larry Bothwell) -- testified that they wanted the fraud to be aggressively investigated. They believed, initially, that the House would not be required to

pay for the fraudulent calls. Accordingly, they decided to withhold payment on the October and November WATS bills, pending the results of the fraud investigation.

During late November and early December, the HAS director cooperated with investigations by Admin and the commercial carrier (MCI). With the permission of Welle, the director of HAS turned over call detail records to Admin and MCI. However, the director, concerned about separation of powers and data privacy issues, requested that the staff in Admin maintain the confidentiality required by the data practices law. Admin reports that on or about December 2, after Admin staff identified a particular residential phone number in the Willmar area for further investigation, the director of HAS requested that the investigation not be pursued further at the time. But the director of HAS testified that he has no recollection of this discussion. Apart from this, testimony before the committee is in agreement: that neither the HAS director nor any other House staff requested the suppression of other facts in the case.

On December 12, 1991, at a meeting with MCI investigators, the director of HAS sought to determine the likelihood of success from the investigation and the probability of successful law enforcement efforts. He also wanted to discuss the House's liability for payment. Attending this meeting were the director of HAS, an Admin representative, and three representatives and fraud investigators from MCI. Although MCI representatives report a different recollection of what transpired at the meeting (see pages 14-15), the director of HAS and the Admin representative both came away with three conclusions: first, further investigation was not likely to be successful in finding culprits; second, even if suspects were identified, successful criminal prosecution or civil recovery was unlikely; and third, the House was liable for payment.

The HAS director reported these conclusions to the House director of staff and to Welle. Then Speaker Vanasek has stated that he was not informed, and the House staff director testified that he could not recall speaking to Vanasek at the time. Representative Long (who was considered the "speaker-elect," having recently been selected for that post by the majority caucus) was notified probably sometime in December (date unknown).

After the December 12 meeting, the HAS director informed Admin of the decision, on the part of the House, not to take the investigation further and to pay the telephone bill. Admin deferred to this decision. The director of staff then approved the House expenditure abstract that authorized payment of the October and November telephone bills. The abstract is dated December 27, 1991, and bears the stamped signature of then-speaker, Robert Vanasek.

The fraud incident was not reported outside the House (apart from the communications with MCI and Admin on the investigation, and with the Department of Finance relating to the abstract authorizing payment of the bill). House administrators and officials were not required by statute to notify outside law enforcement authorities, and they did not do so until March 1993, after the fraud was reported in the press and new evidence came to light on the release of the access code.

How was this allowed to occur?

Deficiencies in the InWATS system

Using the InWATS system, rather than credit cards, saved the state over \$500,000 annually since 1988 in operating costs. Since 1984, the House has saved about \$350,000. However, the InWATS system provided by Admin and its commercial carriers suffered from two technical deficiencies that delayed detection and interdiction of fraud.

The first of these deficiencies was that the system did not employ continual monitoring of long distance calls as a toll fraud detection method. In both the DNR and House incidents, the misuse of the access code was detected only after the fraud was so massive that the calls overloaded the state's InWATS lines. Second, the system did not provide rapid reporting of call detail to users. Call detail reports arrived with WATS bills late in the month following the month in which the charges occurred.

The financial risk from fraudulent misuse of InWATS fell on the state, rather than the carriers, because the carriers will accept financial responsibility for misuse of their credit cards, but not for misuse of proprietary InWATS access codes.

Deficiencies in system administration

The state's administration of the phone system did not compensate adequately for the delays in detection and interdiction that were inherent in InWATS design and technology. The fraud involving the DNR access code continued for almost two months after the problem was first detected and for three weeks after the abused access code was identified and traced to the Detroit Lakes office of DNR. The fraud involving the House access code continued undetected from the spring of 1991 until mid-November. Interagency communication related to the subsequent investigation of the House fraud was inadequate. The history of both of these fraud incidents suggests that the agencies involved in administering the state's phone system do not have clear agreement and mutual expectations about their respective roles and responsibilities; about their financial liability; and about detection, interdiction, investigation, and interagency communication procedures. The state's phone system administrators need to correct these administrative weaknesses.

The reporting of both incidents to law enforcement authorities leaves something to be desired. Neither the law nor the administrative system imposed adequate and clear standards and procedures for timely and thorough investigation of the fraud incidents and timely reporting of the incidents to the proper law enforcement authorities. Current law is deficient in defining the responsibility of state officials and employees to report suspected fraud in the use of public property.

Deficiencies in House internal controls

The House's open office environment was, and remains, a security problem.

State and House policies on phone use were unclear and poorly communicated to members and staff. The House had few adopted policies on phone use, and state and House policies were not aggressively communicated to House members and staff. One policy as interpreted and implemented by House administrators -- that phone records were private and confidential -- adversely affected the detection and investigation of toll fraud.

The review of WATS phone bills by the House was inadequate. First, members and employees did not routinely see or review their individual WATS bills. Second, in the absence of review by individual users of their WATS bills, the responsibility fell to the director of HAS. But the director of HAS did not review phone bills aggressively, and the methods used by the director to review WATS bills proved to be ineffective in detecting fraud in a timely manner.

The responsibility for approving House expenditure abstracts (which authorize payment of House bills, including telephone bills) was not, and is not, clearly delineated in practice. The speaker and the chief clerk, who bear the legal responsibility for approving and signing expenditure abstracts, did not routinely review, sign, or even see the abstracts.

In the recent financial audit of the House, for fiscal year 1992, the auditors made many useful recommendations for improving financial controls. However, the 1992 audit report should have mentioned the phone fraud.

What has been done since 1991 to prevent recurrence?

In 1992, the House made sweeping changes in the design of House InWATS phone services. These changes increased the security of the House system substantially (although at increased cost and inconvenience to users). Of the 134 House members, 108 members now must use a "corporate home account" for InWATS calling. Members must use credit cards for long distance calling when away from home.

Admin improved security in 1992 (around-the-clock call monitoring, 80 percent fewer off-hours lines) and plans to make more security improvements available in 1993 and 1994 as it implements the new STARS system.

Admin has begun to take a more assertive posture as the state telephone system administrator. For example, Admin will now discontinue suspect access codes immediately, without consulting the agency involved.

The enactment of House File 1377 (Laws 1993, Chapter 370) makes the telephone records of legislators public data. This removes one impediment to detection and investigation.

The House and House administrators have largely, but not entirely, remedied the deficiencies in the review of WATS bills.

What more needs to be done?

Admin and the House should continue aggressively to adopt changes in telephone system technology to increase the protection of the state against toll fraud.

Admin should take the lead role, as system administrator, in an interagency effort to correct weaknesses in the administration of the state's telephone system, including those identified in this report.

The legislature should strengthen and clarify requirements for reporting breakdowns in internal controls and suspected fraud involving state property.

House leadership should take appropriate steps to further investigate the fraud and to secure restitution from the perpetrators.

HAS should consider increasing security on unattended telephones in the State Office Building by September 1, 1993.

By September 1, 1993, the House should officially adopt comprehensive policies on the use of telephones by House members and employees. These policies should define clearly what calls may be made at state expense and what reporting is required of suspected misuse. Consideration should be given to policies that restrict long distance calling in various ways. The policies should be communicated to members and employees in several specific, recommended ways.

The House should further increase the monthly scrutiny of long distance telephone bills, including the call detail and monthly totals of all long distance telephone usage. Long distance telephone bills should be reviewed monthly, both by individual members and employees and by House administrators and supervisors. House leadership and administrators should develop policies to guide this review.

The House should reevaluate the procedures used to prepare and review expenditure abstracts, particularly the roles and responsibilities of the speaker, leadership staff, the HAS director, and the chief clerk.

The House Rules Committee should define the scope of future financial audits. Future audit reports should be directed to the Rules Committee rather than the director of staff, and the Rules Committee should receive the reports in a public meeting. The audit report should be distributed to each member of the House.

Findings of the Special Committee

Organization of Findings. The Findings are organized into three sections: Phone System Design and Technology (page 6); Phone System Administration (page 12); and House Internal Controls (page 20).

Phone system design and technology

In 1991 the state experienced two substantial losses from telephone toll fraud. Exposure to toll fraud was partly a consequence of the phone system technology used by the state. This section describes the state's phone system, its benefits and weaknesses, and the changes that are being made to the system since the 1991 experience.

Weaknesses and benefits of the system

The House, along with the Senate and other state agencies, buys long distance telephone service from the Department of Administration (Admin), who is the state's telephone system administrator. Admin designs the system and contracts for services from commercial carriers.

In selecting phone system technology, Admin must balance competing considerations, chiefly financial risk from fraudulent use, cost of service to the state, and usability. During the last half of the 1980s, House members who needed to place long distance calls from outside of the office began using a new technology, provided by Admin, that permitted coded access to the state's WATS lines. Calls using this "InWATS" technology were no harder to place and much cheaper than credit card calls.

Events have shown that the choice of InWATS over credit cards, and deficiencies in the InWATS technology itself, exposed the state and the House to financial risk from toll fraud. In 1991, just two instances of fraudulent use of state InWATS access codes, one assigned to the Department of Natural Resources (DNR) and the other to the House, cost the state over \$140,000.

On the other hand, thus far the state's InWATS system has been fraudulently abused only rarely. The total known loss does not exceed \$150,000. Moreover, during this entire period, calls on the InWATS system were much cheaper than credit card calls, saving the state and the House money every year in operating expense. Admin estimates that the use of InWATS has saved the House about \$350,000 since 1984 and the state about \$500,000 annually since 1988, despite the fraud losses experienced in that period.

In preferring the InWATS system over a credit card system, it appears that Admin accepted increased risk to the state in return for substantially lower operating costs. On balance thus far, the decision has saved the state large sums of money. The committee concludes that the decision was a reasonable one, but that client agencies like the House and the DNR were not adequately informed about the risk and cost of fraud. (The latter conclusion is discussed in more detail in the next section, on "phone system administration.")

■ *The InWATs system*

Perpetrators of the telephone toll fraud against the House in 1991 used a code assigned to a House member that allowed access, from anywhere in the United States, to the state's WATS lines. This remote access to state WATS lines is called "InWATS" service.

InWATS calls are received by Remote Answer Units (RAUs), which are controlled by a commercial carrier (US West). The calls are routed by the RAUs into the NorthStar Network, the state's proprietary phone system. The NorthStar Network in turn connects the caller to outgoing long distance services operated by commercial carriers.

Admin is the administrator of this InWATS service. Admin controls the NorthStar Network and administers the related contracts with MCI, US West, and other commercial carriers. Other state agencies and the House and Senate essentially purchase InWATS services from Admin.

Admin began offering InWATS technology in the mid-1980s. Admin first provided InWATS service to the House and Senate in 1984, so that legislators could make long distance calls on the WATS system from home after business hours. (Before this, in the early 1980s, legislators who wished to place a long distance business call from outside of the office had two choices: they could connect to the state's WATS system during business hours, by calling the capitol operators; otherwise they used a telephone credit card or their personal phone and submitted the bill for reimbursement.) InWATS was a success because it was cheap and just as easy to use as a credit card. For these reasons, during the late 1980s, the House encouraged members to use the InWATS service rather than credit cards. In 1988, Admin made a similar service available to the executive branch.

The last major changes in the House phone systems, before the 1991 fraud incident, were in 1989. The House made the following changes: it allowed InWATS calls from anywhere in the United States rather than only from within the state; it eliminated the use of telephone credit cards issued to members by the House; and it replaced a single House InWATS access code used by all members with individual InWATS access codes for each member. These changes widened the area of service (and correspondingly increased financial exposure in case of toll fraud); reduced costs; maintained convenience to users; and increased the potential accountability of individual members for InWATS calls.

The potential for increased individual accountability was not realized, however, because the InWATS phone bills were not routed to individual members for review and approval (unlike credit card bills). Instead the entire House InWATS bill went directly to House Administrative Services (HAS). Individual members did not routinely see their monthly WATS bills.

■ ***Financial risks***

The decision by the House to replace credit cards with the InWATS system provided by Admin placed the House at increased financial risk from toll fraud.

Toll fraud practiced on proprietary WATS systems that allow remote access is a substantial and growing risk nationally. The Secret Service has estimated that toll fraud loss on systems like the state's InWATS system exceeds \$2 billion annually. Code breaking by computer "hackers" using electronic dialing devices and the sale of access codes can quickly cause enormous losses to unwary users.

Admin and a commercial carrier (MCI) testified that the state and the House assumed liability for fraudulent use of InWATS access codes. A carrier, they said, will accept liability for phone fraud only when the carrier can control access by continually monitoring calls on the carrier's system. A carrier will not accept liability for fraudulent use of systems accessible through RAUs, which the carrier cannot monitor or control. Consequently, the commercial carriers with whom the state contracts for long distance services had no financial incentive to encourage aggressive action on internal controls or to prevent or investigate fraud practices on the state system.

Admin and the Attorney General's office have both concluded that the state was legally liable to pay the phone bills for the fraudulent use of a DNR InWATS access code in 1991. They further agree that recovery from the carriers of any of the state's cost for unauthorized long distance calls using the DNR code is unlikely, based on the state's contract with the carriers and disclaimers in tariffs approved by regulatory agencies. (Letters to James R. Nobles, Legislative Auditor, from Commissioner Dana B. Badgerow, June 26, 1992, from Richard S. Slowes, Assistant Solicitor General, October 27, 1992)

■ ***System deficiencies***

The state's risk of toll fraud loss was increased by two deficiencies in the design and technical capabilities of the InWATS system. These deficiencies made it difficult for system administrators to detect and interdict toll fraud in a timely manner.

The first deficiency in system design and technology was that the NorthStar Network did not employ continual monitoring as a detection device. This caused delays in fraud detection and increased state costs, because Admin was able to detect fraud only when state WATS lines became overloaded, by which time the fraudulent use was already widespread and costly.

The second deficiency relates to billing practices. WATS bills arrived after mid-month in the month following the month in which calls were made. This lag in receiving bills from vendors clearly complicated and delayed detection. The DNR did not discontinue its code until its September WATS bill arrived in late October. When the House toll fraud was discovered, in mid-November, the most recent bill available to HAS was the bill for September, which did not reveal obvious fraud under the detection methods used at the time by HAS. (See below, "Internal house controls," for details.) In the House's case, detection was further complicated by concerns about data privacy and constitutional separation of powers, which led the House to require that the call detail in the phone bills be routed directly and only to HAS, rather than through Admin. (See below, "Inter-agency coordination," for more on this subject.)

■ *Fraud incidents and costs*

The state telephone system includes 48,000 phone stations. Admin reports five known toll fraud incidents on the system since 1988. Three were relatively minor, but the other two cost the state more than \$140,000.

Three of the fraud incidents caused relatively minor losses to the state. One in 1988, involving a stolen wallet, cost the state \$35. Another, in 1989, involving misuse by a child, cost the state \$2000. The state recovered costs for a third incident in 1990, involving a code stolen from a state employee and used by students at an arts school.

The other two incidents of toll fraud, both detected in the autumn of 1991, cost the state a total of over \$140,000 in a very short time. One incident involved a Department of Natural Resources (DNR) access code, the other a House of Representatives access code. The DNR incident cost the state nearly \$57,000; about \$55,000 of this cost occurred in just three days, from September 1 to September 3, 1991. The House incident cost the state approximately \$87,000; 76 percent of the cost occurred in a period of a few weeks in October and November, 1991.

Admin makes the following points concerning this experience. All five incidents appear to be the work of persons outside of state government who somehow gained the use of a state access code. Only one of the five incidents (the DNR incident) appears to have involved the distribution of the access code by organized call sale operators. Based on extensive testing by Admin staff, Admin has concluded that the state's InWATS codes never have been broken by a "hacker" using an electronic dialing device.

■ *InWATS savings*

The cost to the state from these toll fraud incidents thus far has been more than offset by reduced operating costs.

The total known cost to the state from toll fraud is about \$150,000. Admin estimates that the use of the InWATS system instead of credit cards has saved the state about \$500,000 annually since 1988. Admin estimates that the House has saved a total of

approximately \$350,000 since 1984 by using the InWATS system rather than credit cards. Admin estimates savings in 1992, under the new STARS contract with MCI, at over \$1 million per year.

Corrective actions

Over the years the House has addressed security problems as they arose. Before the 1991 fraud incident, for example, the House barred 900 calls and restricted international calls. Since the 1991 fraud incidents, the House has stressed security with its members and staff, adopted a new, much more secure remote access system provided by Admin, and routed more call detail information to members. Admin has made technical and system design changes that have increased the security of the phone system. Given the evident financial risks to the state, the committee concludes that Admin should continue aggressively to adopt changes in phone system technology to further increase the protection of the state against toll fraud, and the House should take full advantage of these new fraud detection and prevention capabilities.

■ *House actions*

In 1992, the House made sweeping changes in the design of its InWATS phone services. These changes increased the security of the House system substantially, although at a price: increased cost and, with some exceptions, increased inconvenience to users.

Changes in system design and technology since 1991 are summarized here. (See below, "House Internal Controls," for other changes made by the House since 1991, including bill routing systems.)

- > Of the 134 House members, 108 members now must use a "corporate home account" for InWATS calling. Under the corporate home account, service is available only from a specific phone station (e.g., the member's home phone). This dramatically reduces the potential for external fraud. It also shifts the financial risk to the commercial carrier. Because the carrier controls the device that detects whether the phone station is authorized to access the state's service, the carrier is responsible for use from an unauthorized station.
- > The other 26 House members continue to use the more vulnerable InWATS access code system because of local phone switching limitations.
- > When away from home, all members are instructed to use a personal phone credit card and submit bills for reimbursement. (Those with corporate home accounts have no other option.)
- > An additional 800 number available to members for InWATS calling is now routed to the Sergeant's office, which will connect members only to Centrex, not long distance numbers.

■ *Department of Administration actions*

Admin made improvements in the state's phone system in 1992 and plans to make additional improvements available to its client agencies in 1993 and 1994 as it implements the new STARS system. The committee concludes that, given the manifest risks, the House should continue to take full advantage of these new fraud detection and prevention capabilities as they become available. House administrators told the committee they intend to do so.

Admin testified that in 1992 it began continual, around-the-clock monitoring of system usage, seven days and week, so as to detect fraudulent use. Also, to accelerate detection and lower the state's exposure, Admin has reduced by 80 percent the number of InWATS lines available outside of regular business hours. Admin also testified that it has increased training and education and proposes tightened security measures when users leave state service.

Admin testified that beginning in mid-1993 it will make available other changes in phone system design and technology to increase security:

- > The current InWATS technology, using Remote Access Units (RAUs), will be phased out, replaced by a new credit card system. Calls using these new credit cards will cost slightly more than using RAUs, but still substantially less than phone credit cards issued to individuals.
- > The system will be able to restrict calls to certain calling areas, and to enforce automatic limits on costs incurred by each user.
- > Through in-house billing, the system will more easily provide for individual invoices to users, and it will allow consolidated carrier billing, credit card billing, "exception" reports, and rapid reporting of call detail to reduce detection delays.

Phone system administration

Changes in phone system technology are a necessary but not a sufficient answer to the state's toll fraud problem. The committee has found problems in the governance and administration of the state's phone system that need to be corrected as well. This section of the report summarizes the committee's findings on weaknesses in the general administration of the state's phone system; the next section summarizes the committee's findings on weaknesses in internal House administration.

Detection, interdiction, and interagency communications

The state's administration of the phone system did not compensate adequately for the delays in detection and interdiction that were inherent in design and technology. To the contrary, administrative weaknesses and confusion among the agencies involved appear to have contributed to even further delays in responding to incidents of fraudulent use.

The committee examined two incidents of fraudulent use of state InWATS access codes in some detail: one involved a DNR code, the other the House code. It is apparent in both cases that the agencies involved in these incidents do not have a clear and mutual agreement on important matters of system administration. Much confusion, uncertainty, and disagreement prevailed among the agencies -- about their respective roles and responsibilities; about their financial liability; and about detection, communication, and interdiction procedures. Agencies, including the DNR and the House, were not adequately informed about the risk and cost of toll fraud.

These administrative problems persist. The committee concludes that the state should not rely entirely on corrections in the technology and design of the phone system to reduce its toll fraud risk. The administrative weaknesses that permit such confusion and disagreement among the responsible agencies need attention as well.

■ *The DNR incident*

The fraud involving the DNR access code continued for almost two months after the problem was first detected and for three weeks after the abused access code was identified and traced to the Detroit Lakes office of DNR. This delay was the consequence of deficiencies both in system technology and system administration.

The DNR fraud began on the Labor Day Weekend, September 1-3, 1991, and continued until October 25, when the DNR requested Admin to discontinue the DNR access code. This nearly two month delay is the result of two factors: the time taken by US West in providing call detail to Admin, and miscommunication and misunderstanding when Admin contacted the DNR to request authority to discontinue the access code. The first of these problems is addressed by the technical changes described earlier. The second problem requires attention from state phone administrators.

On September 3, Admin was alerted to the fraud by overloaded state WATS phone lines. Admin immediately asked MCI to block international calls and calls from certain cities in the United States. This step clearly saved the state large sums of money. Almost all of the cost to the state from this fraud (about \$55,000 of \$57,000) occurred in the first three days. Had Admin not limited call areas, the total cost to the state would have been much greater.

Also on September 3, Admin requested from US West the call detail for the Labor Day weekend. Admin needed the call detail to identify the offending access code. US West did not provide call detail to Admin until October 4, which effectively delayed intervention by Admin for a full month.

Using the call detail, Admin was able to trace the fraud to a particular access code assigned to the Detroit Lakes office of DNR. On October 4, Admin notified the Detroit Lakes office. Admin did not notify the telephone coordinator in the DNR central office or the Bemidji regional office. DNR officials in the central office were not alerted to the problem until the bill arrived three weeks later.

The fraud was allowed to persist for three more weeks following this notification, because of a misunderstanding or miscommunication about the responsibilities of the two agencies. Not until October 25, 1991, the day that the Bemidji office of DNR received the WATS telephone bill for September, was the access code discontinued at DNR request.

■ *The House incident*

Admin and House staff believe that the fraud involving the House access code began in the spring of 1991, probably in March. It mounted slowly through the summer, and reached very high levels in October and November. Admin first discovered the fraud on November 14 and traced the abuse to House codes on November 20. The code was discontinued that evening, reactivated the following day for investigative purposes, and permanently discontinued later that day, November 21, at the request of House Administrative Services (HAS). The delay in detecting the fraud was the consequence of deficiencies in both system technology and system administration.

From January through August, 1991, the monthly WATS phone bill of the House varied between about \$15,000 and \$19,000. In September, the bill mounted to over \$23,000; in October, to well over \$36,000; in November, to \$59,000. Administrators failed to detect the fraud during this period partly because of the design deficiencies mentioned earlier (e.g., the absence of call monitoring) and partly because of bill review procedures used by the director of HAS. Comparison of the bills for three prior years does not reveal any pattern that would have alerted HAS to possible fraud. The change from individual credit card bills to combined InWATS bills made fraud detection by HAS more difficult. (See below "Review of phone bills" for more information.)

According to Admin testimony, Admin became aware of the fraud on November 14, again only because of overloaded WATS lines. Through a series of detection steps between November 14 and 20, Admin was able to eliminate from consideration the component of the state InWATS system used by executive branch agencies and identify the legislature as the source. On November 20, Admin was able to trace the misuse to House access codes.

On November 20 or 21, Admin notified the director of HAS, who is the House's telecommunications coordinator. Overnight on November 20, as a preventive measure, Admin shut down legislative InWATS and routed calls to a recorded message. On November 21, as a preventive and investigative measure, Admin reopened legislative InWATS but redirected all legislative calls from computer routing devices to operators. By interviewing callers, Admin telephone operators were able to identify the offending code. The director of HAS, by reviewing call detail reports, identified both the offending code and the member assigned to that code. (For reasons of data privacy, this information was not available to Admin.) The offending code was discontinued by Admin at the HAS director's request on November 21.

■ *Payment of costs*

The decision to pay the House's telephone bill for the fraud was made in late December 1991.

The responsible House administrators -- the director of HAS (David Kienitz) and the staff director (Larry Bothwell) -- testified that their initial view was that the House was not responsible for the bill and would not pay, and that the fraud should be aggressively investigated. The HAS director cooperated with Admin and MCI staff in investigating the fraud incident in November and early December, 1991. With the permission of the member to whom the code was assigned (Representative Welle, who also happened to be the newly-elected majority leader), the director of HAS turned over to Admin and MCI investigators call detail records. The director requested only that the staff in Admin maintain the confidentiality required by the data practices law. Admin reports that on or about December 2, after Admin staff identified a particular residential phone number in the Willmar area for further investigation, the director of HAS requested that the investigation not be pursued further at the time. But the director of HAS testified that he has no recollection of this discussion. Apart from this, testimony from Admin officials and House administrators was in agreement that House staff did not request the suppression of other facts in the case.

The two House administrators changed their minds about aggressive pursuit following a meeting on December 12, 1991, with representatives of the commercial carrier. Attending this meeting were: the director of HAS, David Kienitz; an Admin representative, Bonnie Plummer; and three MCI representatives and fraud investigators, John Henderson, Lance Springer, and Tom Schutz. At the meeting, the director of HAS sought to determine the likelihood of success from further investigation and subsequent law enforcement efforts. He also wanted to discuss the House's liability for payment. MCI representatives testified that they advised Admin

and the House that an investigation would have a reasonable chance of success in identifying culprits and that, depending on the amount of money involved, prosecutors might well be interested in pursuing the case. MCI also offered to investigate, free of charge. The director of HAS and the Admin representative, however, both came away from this meeting with the conclusion that further investigation was not likely to be successful in finding culprits and that, even if suspects were identified, successful criminal prosecution or civil recovery was unlikely. The director of HAS also concluded, on the advice of MCI and Admin, that the House was liable for payment.

In arriving at these conclusions, the director of HAS testified that he relied on the advice of those he regarded as the state's experts (Admin and MCI). The director did not consult legal counsel.

The director of HAS reported his conclusions to Welle and the director of staff in the House. Then Speaker Vanasek has stated subsequently that he was not informed of the problem, and the House's director of staff testified that he could not recall speaking to Vanasek on the matter. Representative Long (then regarded as "speaker-elect") was informed of the incident and the cost to the House probably sometime in December 1991 (date unknown).

After the December 12 meeting, the HAS director (Kienitz) informed Admin of the decision on the part of the House not to take the investigation further and to pay the bill (which was finally authorized on December 27, 1991, as part of an expenditure abstract that bore the stamped signature of Vanasek). (See "Approval of expenditure abstracts," below for details.) Admin reports that it considered the decision to halt the investigation as entirely the House's.

■ *Interagency coordination*

The history of these two incidents suggests that the agencies involved in administering the state's phone system do not have clear agreement and mutual expectations about their respective roles and responsibilities; about their financial liability; and about detection, interdiction, and inter-agency communication procedures. The state's phone system administrators need to correct these administrative weaknesses.

Admin takes a certain view of its role as the state's phone system administrator. It regards itself as a vendor of communication systems and technologies, and it considers state agencies who use the phone system to be customers. In its role as system administrator, Admin accepts responsibility for the security of the system. So, for example, Admin would accept financial responsibility if a computer "hacker" gained access by breaking into the system. But Admin believes that its customers (i.e., other state agencies) are responsible for the security of the codes assigned to them and that therefore these agencies should bear the entire financial responsibility for fraudulent use of the codes.

State agencies have quite a different view of Admin's role, at least in times of trouble. While Admin is inclined to rely on its customers to protect themselves, the agencies evidently look to the system administrator for aggressive, system-wide warning, detection, interdiction, and internal reporting services and for expert advice on investigation procedures. The HAS director testified on this point directly. The DNR has gone so far as to refuse to bear the financial liability for the DNR fraud, because the DNR considers Admin at least partly responsible. The Legislative Auditor's report on the DNR incident supported this DNR position.

This lack of clarity about agency roles and responsibilities adversely affected the state's response in these fraud incidents, in at least two respects. First, Admin's view of itself as a vendor and other agencies as its customers seems to have fostered a deferential attitude that inhibited Admin from enforcing aggressive, system-wide standards for responding to fraudulent use of codes (e.g., uniform fraud detection, interdiction, investigation, and interagency reporting procedures). Admin had no financial incentive to demand an aggressive response, because it believed itself to be free of financial responsibility.

Second, poor communication between agencies increased exposure and interfered with appropriate response. Admin did not give its customer agencies specific, written information about the costly fraud incidents that were occurring in late 1991. And communication between agencies during the fraud incidents was not entirely successful. In the DNR incident, Admin reported to DNR's telephone coordinator in the Detroit Lakes office, a fairly small office; neither the Bemidji office nor the central office were involved until the phone bill appeared in the Bemidji office. Admin had misgivings about delay in code cancellation but did not notify higher authority in the DNR. DNR officials seem to be offended by this procedure and assert that telecommunications coordinators in the Bemidji office or the central office should have been alerted. In the House incident, Admin reported to the House's telecommunications coordinator, the director of HAS, but then deferred to "House" decisions that were reported back by the director. When the director of HAS reported finally that the House had decided to halt further inquiry, Admin officials, despite some reported misgivings about the decision, chose not to pursue the matter with higher authority in the House (the speaker) or outside investigative authorities.

These weaknesses in interagency coordination were exacerbated in the House incident by concerns both about data privacy (House phone records were classified as private data) and about constitutional separation of powers. The director of HAS conveyed to Admin representatives his intention to protect private data and to ensure confidentiality and legislative independence. Admin's behavior toward the House as events unfolded was quite circumspect and deferential. Senior Admin officials, including the commissioner, were informed by Admin staff on November 22, 1991, of the fraud incident involving House phones. To protect the privacy of the data, as required, Admin staff did not pass on to Admin officials any information about the holder of the code or about call detail. Subsequently, when the director of HAS decided to halt the investigation, Admin did not press the matter. The commissioner of Admin testified

that Admin's behavior was in part a result of Admin's sensitivity to the requirements of data privacy and separation of powers.

Lately Admin appears to be taking a more assertive posture as system administrator. For example, if Admin detects fraudulent use of a code, it will now discontinue the code on its own initiative rather than waiting for an agency request. The committee encourages such assertiveness where it will help reduce the state's risk of phone fraud and increase the effectiveness of the state's response.

Law enforcement and external reporting

The committee concludes that the reporting of both incidents of fraud leaves something to be desired. The committee further concludes that neither the law nor the administrative system imposed adequate and clear standards and procedures for timely and thorough investigation of the fraud incidents and timely reporting of the incidents to the proper authorities. The agencies involved in these incidents did not disregard or disobey a legal notification requirement. However, the reporting obligations of Admin are far from clear in these cases, and the House appears to have no reporting requirement.

■ Agency behavior

In the DNR incident, Admin requested a full investigation by MCI, but the incident was not reported to the Legislative Auditor until early November 1991, more than two months after fraud was first detected by Admin and more than a month after the fraud was traced to a DNR code. Then it was the Auditor, not the agencies, who reported to outside law enforcement authorities. The media did not cover the DNR incident until the Legislative Auditor issued a report many months later, in July 1992. In the House incident, following several weeks of fraud investigation by Admin and MCI, House administrators decided to halt further investigation and pay the bill in mid-December 1991. The director of HAS so informed Admin. Neither Admin nor the House reported the incident further. The fraud was not reported to law enforcement authorities until over a year later. In March 1993, the House notified the Attorney General after the incident was reported in the media and new evidence came to light on the release of the access code.

At the time of the DNR incident, Admin notified only MCI and the DNR. The DNR notified the Legislative Auditor of the suspected fraud on November 8, 1991. Thus, the Auditor was not notified until two months after the fraud was discovered by Admin, a month after Admin traced the fraud to a DNR access code, and two weeks after the DNR code was discontinued. Admin notified the governor's office in mid- to late- November of the fraud and the investigation. Neither Admin nor the DNR notified law enforcement authorities; it was the Legislative Auditor who notified the Attorney General and also the Secret Service.

In the House incident, Admin notified only MCI and the House. As described earlier, House administrators cooperated with fraud investigation by Admin and MCI until they decided, in mid-December, to stop further investigation. House administrators testified that they made this decision because they concluded, after discussions with Admin and MCI staff, that further pursuit would serve no useful purpose. House administrators did not consult with legal counsel in this decision, nor did they report to outside law enforcement authorities until the notice to the Attorney General in March 1993, after the media began to report the fraud and new evidence emerged about the release of the access code.

House administrators testified that they did not halt the investigation to withhold, disguise, or cover up the fraud or facts pertaining thereto, except as required by data privacy law. Admin representatives testified that they were never asked by House administrators not to inform any office or law enforcement agency of the incident. (Admin did report that early in December, after Admin staff identified a particular phone number for further investigation, the director of HAS requested that the investigation not be pursued further. This discussion the director of HAS does not recall.)

■ ***Legal requirements***

The committee considers current law deficient in defining the responsibility of state officials and employees to report suspected fraud in the use of public property.

The statutory reporting requirements for public agencies who suspect fraudulent use of public property are as follow:

- > Section 181.932 protects all public employees who report wrongdoing, but it does not require reporting.
- > Employees and officials of political subdivisions are clearly required by Minnesota Statutes, section 609.456, to report "evidence of theft, embezzlement, or unlawful use of public funds or property" to the state auditor. This statute does not impose requirements on employees and officials of state government.
- > The requirement for state executive branch employees is less clearly stated. Section 43A.38 says that an employee in the executive branch "shall not use or allow the use of state time, supplies, or state owned or leased property and equipment for the employee's private interests or any other use not in the interests of the state." Section 43A.39 says that any employee who fails to comply with the provisions of section 43A.38 may be subject to disciplinary and criminal prosecution. Section 43A.39 requires "an appointing authority" to report suspected violations to the Legislative Auditor. When applied to the DNR incident, these sections appear to place the burden for reporting on the DNR rather than Admin.

- > The application of these sections in chapter 43A to the House incident is even more problematic. Section 43A.39, which requires notification of the Legislative Auditor of suspected violations, arguably applies to the legislature (probably inappropriately, because the Legislative Auditor is not a disengaged authority). But section 43A.39 has reference to the deeds proscribed by section 43A.38, which clearly applies only to executive branch employees. The committee has not found a similar provision that would apply to legislative officers and employees.

These laws were followed in the DNR incident. DNR properly reported to the Legislative Auditor (there is no time requirement), and the Auditor properly reported to law enforcement authorities. Admin was not required to report the fraud to outside authorities, because section 43A.39 puts the burden of reporting on the "appointing authority," i.e., the agency experiencing the suspected fraud.

With respect to the House incident, these laws do not require either Admin or the House to report to law enforcement authorities. The committee has found no law requiring the House officially to report the incident to outside law enforcement agencies. However, the committee believes sound management practice would suggest or require such reporting. Without such a legal requirement, House administrators hesitated to take action that could expose private data to outside scrutiny. Besides, House administrators have shown some confusion about whom, beyond MCI and Admin, they should have notified.

Several other general provisions of the law might apply in cases of fraudulent use or theft of public property or money. The application of these laws depends on facts which it has not been the committee's business to gather. The committee recites these laws for informational purposes only; the committee has no information suggesting that any of these sections apply to these incidents. Section 3.756 makes it a crime for a state officer to knowingly and willfully participate or assist in the preparation or presentation of a false or fraudulent claim. Section 609.43 makes it a crime for any public official or employee to make an official report or other like document having knowledge that it is false in any material respect. Section 609.455 makes it a crime for any public official or employee to allow or pay a claim or other demand that the official or employee knows is false or fraudulent. And section 609.465 makes it a crime for any person knowingly and with intent to present a false claim or demand for payment to a public official or employee.

Law enforcement authorities are currently working on civil recovery and on criminal prosecution. The committee considers this appropriate, and beyond the scope of this committee's charge and expertise.

House internal controls

This section describes the weaknesses in the House's internal control structures and procedures that contributed to the House's loss from the 1991 toll fraud incident: the open office environment; inadequate policies on phone use; inadequate review of phone bills; weaknesses in procedures for reviewing expenditure abstracts. The section also comments on the independent audit of the House for FY 1992, as it relates to the phone fraud incident.

Open environment

The House's open office environment was, and remains, a security problem. But the need for phone system security must be weighed against the importance of openness, public access, and effective working conditions.

As a matter of policy, the House maintains an office environment that is unusually open to outsiders. This allows public access to unprotected phones. As a result, some misuse of office phones no doubt occurs, but so far this has not been discovered to be a major internal control problem.

Since the 1991 incident, the House has taken steps to alert members and staff and to increase security. But the open environment remains a continuing concern, as do measures that sacrifice openness and work effectiveness to achieve greater security.

Policies on phone use

State and House policies on phone use were unclear and poorly communicated to members and staff. Since the 1991 fraud incident, although the House has taken some remedial action on phone policy, it has not addressed this deficiency to the committee's satisfaction. The committee concludes that the House needs to develop clearer policies on proper phone use and better procedures to ensure that policies are communicated and understood by all.

■ Policies

The House had few adopted policies on phone use, and state and House policies were not aggressively communicated to House members and staff. One policy as interpreted and implemented by staff -- that phone records were private and confidential -- adversely affected the detection and investigation of toll fraud.

State policies on phone use were not effectively communicated. The state phone book contains a brief policy statement on page 1 and a strong admonition against personal use of WATS lines on page 9. The book has contained such language for more than twenty years. However, the constitutional doctrine of separation of powers makes it unclear whether Admin rules do, or should, automatically bind the legislature or the

courts. Even if Admin policies do apply, the state phone book is not routinely distributed to new members until a new edition appears later in the year, and few people trouble to study the fine print in the phone book on such matters.

In these circumstances, it would have been wise for the House and House administrators to clearly articulate and communicate a policy on proper phone use. But written House policies on telephone use were few in 1991, and those few were poorly communicated to members and staff.

- > The director of HAS from time to time distributed memos, addressed to new members and staff, stating the policy forbidding use of WATS lines for personal calls.
- > Descriptions of WATS billing practices and admonitions against personal use of the phones have not appeared in recent years in generally distributed administrative policy statements in the House, nor in new employee manuals, nor in manuals distributed to legislators.
- > Neither have there been resolutions or other official actions by the rules committee defining or proscribing excessive or inappropriate telephone use. An exception was a House policy in the 1980s (when the House issued phone credit cards to members) that imposed a \$600 per year limit on long distance calls by members. This policy was so poorly communicated that its expiration in 1989 was unknown to many affected members and administrative staff for as long as two years.

At least one policy was clear in 1991: that the phone records of members were confidential and private. The House first adopted this policy in the 1970s, by Speaker Sabo's directive; it was later adopted in law in 1989. This policy adversely affected the detection and investigation of toll fraud involving House access codes. (See above, "Interagency coordination," and below, "Review of phone bills.")

■ ***Corrective actions by the House***

Since 1991, the House has only partly addressed these deficiencies in policy. The House still needs to develop clearer policies on phone use and better procedures to ensure that policies are communicated and understood.

The policy on privacy of telephone records has been reversed. In the 1993 session, the House successfully sought changes in data practices laws that prevented the public release of phone bills. The legislation passed and was signed by the Governor on May 24, 1993 (Chapter 370). This change in policy on public disclosure of phone bills brings with it the likelihood of ongoing public review of phone bills. This is appropriate and may provide further protection from fraudulent use of the phones.

The House has not developed policies defining appropriate and proper use of WATS calling by members. Unless the House acts to fill this policy vacuum, public

disclosure of member phone records is likely to result in unwarranted restraints on members' use of the WATS system for proper business purposes. Absent a House policy, members seeking to avoid uninformed media and public criticism of phone bills may be forced either to limit legitimate calls, thus doing a poorer job representing their constituents, or pay the cost of business calls from their own pocket. This is likely to work a particular hardship on members representing nonmetropolitan and rural districts.

Also, House administrators have not developed procedures that will ensure regular and clear communication of policies to all members and staff in the future.

Review of phone bills

The review of WATS phone bills by the responsible House administrators was inadequate in 1991. The director of HAS was responsible for ensuring that WATS phone bills were reviewed for accuracy and propriety, before the preparation of abstracts authorizing payment. The director did not review phone bills aggressively, and the methods used by the director to review WATS bills proved to be ineffective in detecting fraud in a timely manner.

Since 1991, the House and House administrators have responded effectively and have largely remedied this deficiency in internal controls, but more remains to be done to improve bill review, particularly with respect to in-office WATS bills.

■ *HAS bill review procedures*

In the absence of review by individual users of their WATS bills, the responsibility fell to the director of HAS. The director considered it inappropriate for him to review WATS bills for evidence of internal misuse, and the director's method of reviewing bills for evidence of external fraud proved to be ineffective.

In 1991, individual members did not routinely review and approve, or even see, their WATS bills, nor were they informed by House administrators of how phone records were reviewed by HAS. Members did, of course, review and approve credit card bills when they prepared reimbursement requests, but WATS bills were routed directly to HAS. This centralized routing of WATS bills chosen by HAS did not promote individual accountability for WATS calls, because unless members made special requests they never saw the call detail information which would have alerted them to fraudulent or inappropriate use. Centralized routing also increased the House's financial risk in case of toll fraud. Had monthly WATS bills been reviewed by individual members, the 1991 fraud would likely have been detected much earlier and cost the state much less.

In the absence of individual review of phone bills, the responsibility for ensuring that the House's phone bills were scrutinized for accuracy and irregularities fell to the director of HAS. The director of HAS, however, believed that House policy and the

law on data privacy precluded scrutiny and enforcement by staff. Accordingly, the director reviewed phone records minimally.

The director did not examine the call detail in WATS bills looking for internal House fraud (excessive or inappropriate use by members or staff). After the abandonment of the \$600 annual limit on long distance calls in 1989-90, the director of HAS did not have, nor did he propose, any policy defining inappropriate or excessive use of WATS to guide such a review by him. Without policy guidance from the House, the director did not consider it possible or appropriate for him to make judgments about excessive or inappropriate use by members or by staff in other offices.

The HAS director did review WATS bills looking for external fraud, but the method he used proved to be ineffective. After the \$600 annual limit on calls expired in 1989-1990, the HAS director no longer monitored the monthly cost of calls on individual codes. Instead, the director chose to examine only the total monthly WATS bill for the entire House as his method of detecting external fraud. This method could not have detected any but the most massive fraudulent use. Had the director been monitoring the call detail, or even the monthly cost of calls on individual codes, he would likely have detected fraud much earlier. Furthermore, because the phone bill appeared after mid-month in the month following the month in which the calls occurred, the bill came too late to allow timely detection of the explosive type of external fraud that occurred in October and November.

■ ***Corrective actions by the House***

The House has responded to the 1991 incident by correcting most, but not all, of these inadequacies in the review of WATS phone bills.

Bill routing for all InWATS long distance calls by members was changed, beginning in July of 1992. Now, each member must review and approve the member's bill, including call detail, before the House will pay. Initially, the billing system required members to pay the bill and then submit a signed reimbursement form that contained strong admonitions against using the WATS system for personal calls. This reimbursement system was cumbersome. Although some members still use it for some types of bills, most members (beginning in January 1993) sign and submit the bill, including the call detail sheet, for direct payment by the House.

This new InWATS bill routing system, by itself, does not reduce the potential for fraudulent access. But it increases the accountability of users, shifts the responsibility for monitoring usage from administrative staff to individual members, and substantially increases the probability of early detection of external fraud.

A similar system for individual review of monthly in-office WATS phone bills has not yet been implemented. The committee was assured by House administrators that it would be implemented this year.

The director of HAS changed his method of reviewing WATS bills in November of 1991, immediately upon learning of the fraud. The HAS director now scans the detailed call record of individuals. The HAS director looks primarily for "irregular" use from a phone station that would suggest external fraud. The method used is as follows: the director looks first for more than about 100 WATS calls recorded to a single phone station. He then looks up the name of the individual assigned to that phone and makes a judgment about whether that level of use by that individual is irregular. The criteria for making this judgment include: the caller's legislative position; residence (rural or urban); past patterns in phone use; and current legislative events (e.g., important bill, caucus election).

The HAS director still does not review call detail looking for internal fraud, for the same reasons as before: lacking a House standard, he does not consider it either possible or appropriate for him to make judgments about excessive or inappropriate use by members or by staff in other offices. This inadequacy should be corrected by adoption of House rules on usage that can be enforced by HAS.

The benefit of careful scrutiny of telephone bills is revealed by other costly billing errors discovered recently by the director of HAS. When he began to review prior telephone bills more closely after November 1991, the director detected billing errors that had caused the House to routinely make excess payments for long distance services. (The errors were the result of double billing for long distance calls. The double billing was caused by the failure of US West to discontinue charges for long distance calls on InWATS lines that were no longer used by the House after it began using individual InWATS access codes in 1989.) The House has subsequently recovered about \$40,000 in excess payments, for the period after May 1991. The House cannot recover on bills before this time, because the necessary call detail records no longer exist. The records were routinely destroyed by HAS after bill payment, for data privacy reasons.

Approval of expenditure abstracts

The responsibility for approving House expenditure abstracts (which authorize payment of House bills, including telephone bills) was not, and is not, clearly delineated in practice. The speaker and the chief clerk, who bear the legal responsibility for approving and signing expenditure abstracts, did not routinely review, sign, or even see the abstracts. Instead the abstracts were prepared, reviewed, and approved by HAS staff and by the leadership staff person with responsibility for House administration. This procedure has been followed, with minor variations, for nearly 20 years, and remains in place today. The committee has formulated no final judgment on whether this procedure is proper or, if it is not, what should replace it. However, the current arrangement sometimes makes it difficult to determine accountability for decisions that are reflected in House expenditure abstracts. The committee believes this should be a subject of further inquiry.

■ *Requirements*

Expenditure abstracts must bear the signature of the speaker and the chief clerk of the House.

Expenditure abstracts summarize, by accounting code, bills to be paid. The approval of the abstract is the last step in spending authorization. Before the preparation of the abstract, each bill has been reviewed and approved by someone with spending authority (a staff office director, committee chair, member, etc.).

Each abstract must bear the signature of the speaker and the chief clerk, before the abstract is sent to the Department of Finance for entry in the statewide accounting system and final processing of checks. The signatures of the speaker and the chief clerk are both required by House rule 7.01: "The speaker shall sign all abstracts for the payment of money out of the legislative expense fund of the House; but no money shall be paid out of said fund unless the abstract is also signed by the Chief Clerk of the House." In addition, rule 7.03 provides: "During a temporary absence of the Chief Clerk, the First Assistant Chief Clerk ... is authorized to sign ... abstracts...." Minnesota Statutes, section 3.099, subdivision 1, further provides as follows, with respect to member compensation: "On January 15 in the first month of each term and on the first day of each following month, the secretary of the senate and the chief clerk of the house of representatives shall certify to the commissioner of finance, in duplicate, the amount of compensation then payable to each member of their respective houses and its total."

■ *HAS procedures*

Since 1975, when responsibility for business administration was transferred from the chief clerk to a separate House office, HAS (or its predecessor office) has been responsible for preparing proper and accurate expenditure abstracts.

In 1975, the House created its first separate business office and transferred responsibility for the fiscal and business affairs of the House from the chief clerk to the director of the business office. Since 1985, in the administrative structure of the House, the director of this business office, now called HAS, has reported to the leadership staff person responsible for House administration, currently known as the director of staff.

HAS is initially responsible for preparing accurate and proper expenditure abstracts for forwarding to the proper authorizing agents for the House. According to the job description, the director of HAS "[r]eviews and approves for forwarding all ... expenditure abstracts, investigating questionable data as necessary." The current HAS director has customarily delegated responsibility for abstract preparation and review to subordinates within the office.

Since the creation of HAS in 1975, House abstracts have been processed for approval as follows: HAS --> leadership staff person responsible for administration (for

speaker's signature) --> HAS (for chief clerk's signature) --> Department of Finance. At one time, copies of bills and invoices accompanied the abstract as it was routed through this process. In the mid-1980s, the House computerized the documentation, so that now the abstract is accompanied by a detailed listing of expenditure items, amounts, and purposes.

■ *Leadership review and speaker's signature*

Under most speakers for the last 20 years, a leadership staff person has reviewed abstracts on the speaker's behalf and either signed or stamped the speaker's signature on the document. The problems with this arrangement are three. First, the practice does not conform strictly to House rules. Second, the delegation of responsibility from speaker to staff may not always be accompanied by the authority required to carry out the responsibility properly. Third, under conditions that occur with some regularity in the House, accountability for the spending decisions that are reflected in a given abstract can become quite blurred. These three problems are illustrated nicely by the abstract that reflected the decision, in December 1991, to halt the investigation and pay the bill for fraudulent use of House telephone services. The committee makes no final judgments on the review of abstracts by leadership and leadership staff, but the committee believes that the current arrangements need reevaluation.

The final decisions on abstracts are made by the majority leadership and its staff, not by the director of HAS. HAS forwards all abstracts to the speaker's office for the review and approval required by House rule.

The abstract that authorized payment of the telephone bills for October and November (the bills that included most of the loss from the fraudulent use of the House access code) was dated December 27, 1991. The abstract bore the signature of the speaker during this period, Robert Vanasek. It would seem clear from this that Speaker Vanasek, as the official responsible for approving the expenditure abstract, was responsible for, or at least informed of, the decision to abandon the effort to collect from fraudulent users and to pay the bill for the toll fraud.

In fact, it is not entirely clear who was responsible for the decision. Senior staff (the staff director and director of HAS) report that they looked not to Speaker Vanasek for decisions on how to handle the irregularity in phone bills, but rather to Representative Welle, because it was Welle's access code, and because at the time he was the newly-chosen majority leader. The director of staff was out of town on vacation in the last half of November. He has testified that he does not remember clearly who he notified, or when, after he was informed of the fraud upon his return early in December. After the December 12, 1991, meeting with MCI investigators (see "Payment of costs", page 14), the HAS director reported his conclusion (that the House was liable and further investigation was pointless) to the director of staff and to Representative Welle. Representative Long (then regarded as "speaker-elect") was informed by staff of the incident and the cost to the House sometime in December

(date unknown). Then Speaker Vanasek has stated subsequently that he was not. The director of staff testified that he could not recall speaking to Vanasek at the time.

Several factors combined to create this situation:

- > The administrative responsibilities of the speaker and majority leader, respectively, vary over time, depending on personal interests and relationships and on availability. Often the two share responsibility for decisions, one stepping in for another as necessary. Generally, the majority leader has a stronger role in matters relating to the rules committee's jurisdiction: personnel and payroll, budget, and payments to members and committees. The speaker has more responsibility in other administrative matters, including accounts payable, expenditures, and facilities, where the speaker's signature is required on abstracts. As the presiding officer, the speaker is also generally in a position to have the final word on any administrative matter.
- > The House rule requires the speaker to sign all abstracts. But most speakers during the last twenty years have not, in fact, personally reviewed and signed abstracts. Instead, most speakers have delegated the responsibility for reviewing routine abstracts to a leadership staff member. Speakers expect to be consulted on irregularities, and the leadership staff person is responsible for keeping the speaker informed. Since 1985, the leadership staff person responsible for this review has been the House director of staff, who is also the supervisor of the director of HAS. The current staff director reviews abstracts and supporting documentation personally on behalf of the speaker. Upon approval by the director of staff, either the director or the speaker's secretary stamps or signs the abstract for the speaker and returns the abstract to HAS.
- > The delegation of authority to accompany this responsibility to review abstracts is neither complete nor unambiguous. Consequently, senior staff exhibit some uncertainty about the extent of their authority to make independent decisions on abstracts, about whom to report to for decisions they do not feel authorized to make, and about how aggressive to be in insisting on decisions from busy leaders who are often absorbed in legislative activities.
- > These uncertainties in decision-making authority were complicated in last half of 1991, because House leadership was in transition. Speaker Vanasek had announced his retirement and was occupied with new responsibilities outside of the House. In July 1991, the majority caucus elected Representative Welle as majority leader; as such, Welle was consulted by staff and included in leadership decision-making during the last half of 1991. At the same time, the majority caucus selected Representative Long, then the majority leader, as the next speaker. But the speaker is a House rather than a caucus position; therefore Long did not officially hold the office until January 1992, when she was elected speaker by vote of the House. During the last half of 1991, Long was treated by leadership staff as speaker-elect. She continued to be paid, along with Speaker Vanasek, as one of the two majority caucus leaders. By late December 1991,

when the decision was made to discontinue the investigation and to pay the outstanding telephone bills in full, Vanasek had just days left to serve as speaker. This transition in leadership probably complicated or delayed the efforts of the administrative staff to secure appropriate review and decisions by leadership on how to handle the incident.

As a consequence of these forces, some systemic and some unique to the period in question, it is not completely clear who should be held accountable for the decision to halt the fraud investigation and pay the telephone bill containing the charges for the fraudulent use.

■ *Chief clerk's review*

Although the chief clerk's signature is still required on abstracts, the clerk has not had authority over House spending since 1975. For many years most HAS staff have routinely stamped the signature of the chief clerk on the abstract without the clerk's review.

The second required signature on abstracts is that of the chief clerk. In 1975, when the House created a separate office in charge of its business affairs and transferred the function from the chief clerk, House rules left the clerk with the responsibility for signing abstracts but without any concomitant authority over House expenditures. The clerk's signature became a formality without substance. Thus, until very recently, after an abstract was returned to HAS with the speaker's signature, most HAS staff routinely stamped the clerk's signature on the abstract. The clerk never saw, let alone signed or reviewed, the abstracts. This became a more common practice after the 1985 move to the State Office Building made it less convenient to get the clerk's signature. In recent weeks, the HAS staff has begun once more to bring abstracts regularly to the clerk for signature. But the signature of the clerk remains a formality rather than an effective internal fiscal control, because the clerk has no real authority to affect House spending decisions.

Independent audit of the House

The committee reviewed the recent financial audit of the House for fiscal year 1992. The auditors made a number of useful recommendations for improving financial controls. However, the committee believes that the audit report should have mentioned the phone fraud, and the committee believes that in the future the House should direct the audit report to the Rules Committee rather than the director of staff.

Independent auditing of the House was instituted by House administrators and leadership for the first time in 1992. The director of staff testified that he had recommended such auditing before the 1991 incident. The first audit was of fiscal year 1992 and was performed during the last half of 1992. The audit report was addressed to the director of staff, rather than the Rules Committee, and is dated

December 11, 1992, approximately a year following the phone fraud incident and the decision by the House to pay the bill.

The auditors and the director of staff testified that the director informed the auditors about the phone fraud incident and that the director and the auditors discussed the fraud. This occurred apparently toward the end of the audit work. On the basis of these conversations, without further inquiry, the auditors concluded that the fraud was external, not internal, that leadership was informed, that adequate remedial action had been taken, and that financial recovery of the loss was not possible.

The auditors recommended orally to the director an additional phone control measure: that all telephone bills should be routed to individual users for their review and approval. The committee has been informed that this control is being implemented, though it has not been fully implemented to date.

The audit report makes a number of useful recommendations for improving fiscal controls. The audit report did not, however, mention problems with phone management or the payment of \$87,000 in fraudulent phone bills. The committee believes that it should have. The Legislative Auditor testified that in this respect the audit did not conform to the Auditor's practice, and that his staff would be expected to report on such points.

Recommendations of the Special Committee

Telephone system design and technology

The Department of Administration (Admin) and House administrators should continue aggressively to adopt changes in telephone system technology to increase the protection of the state against toll fraud. House administrators should take full advantage of the new technology available as the STARS telecommunications system is implemented, including low cost credit card calling, restrictions on international calls, restrictions on calling areas, automatic calling limits, and faster, customized, and more complete billing reports. The House should consider technical modernization of the House telephone system; changes in the House system would improve both service and security.

Telephone system administration

Admin should take the lead role, as system administrator, in an interagency effort to correct weaknesses in the administration of the state's telephone system, including those identified in this report. In particular, Admin should address delays in detection and interdiction; problems in interagency communication; policies on agency financial liability; and uniform policies and procedures for timely investigation and internal and external reporting of fraud incidents.

External and internal reporting

The legislature should strengthen and clarify requirements for reporting of breakdowns in internal controls and suspected fraud involving state property. In examining the reporting requirements as they apply to state phones, the committee found general deficiencies in the law on these subjects that should be corrected.

- Legislation should be enacted that would strengthen and clarify the responsibility of all state employees and officials to report evidence of theft, embezzlement, or unlawful use of public funds or property to an appropriate law enforcement or independent auditing authority for further investigation. Section 609.456, relating to political subdivisions, provides a good model. The auditing authority, whether the state auditor or the legislative auditor, should be required to report any violations discovered during the investigation to the proper law enforcement authorities, along the lines provided for the legislative auditor in section 3.975.
- In addition, the House should establish internal structures and procedures that provide a means for people within the organization to report incidents where internal controls are being avoided or overridden. Attention should be given to the proper organizational position and authority of the officer, committee, auditor, or legal counsel that receives

such reports. The House's sexual harassment policies provide a useful model, both as to the development process and the final product.

- Finally, House leadership should ask Admin and MCI to investigate further the fraudulent use of the House code, for the purpose of identifying the perpetrators of the fraud, and should pursue any suggestions from MCI and Admin on obtaining restitution. Before proceeding with this, leadership should first notify the attorney general and the Ramsey county attorney, to ensure that such an investigation by MCI and Admin will not duplicate or interfere with investigations already undertaken by law enforcement authorities.

Open office environment

House Administrative Services (HAS) should consider increasing security on unattended telephones in the State Office Building by September 1, 1993. The committee suggests that HAS consult with experts from Admin and vendors to develop security measures that would prevent easy use of telephones for long distance calls by persons other than the assigned users. Care should be taken so that security measures do not impair public access or effective working conditions in House offices.

Measures that should be considered include: requiring individual access codes or cards for long distance calls; blocking long distance calls from accessible work-stations like receptionist desks; blocking international calls from any telephone without use of an access code or card; limiting call destinations to those normally used on legislative business.

House telephone policies

By September 1, 1993, the House should officially adopt comprehensive policies on the use of telephones by House members and employees. Consideration should be given to the following points:

- The policies should clearly define the types of calls that may be made at state expense. The policies should include explicit policies on personal or nonbusiness use. Special consideration should be given to the treatment of business calls to the district made by members who are away from home on legislative business and to the treatment of calls to home made by members and employees who are away on legislative business. Procedures should be adopted for reimbursing the House for the nonbusiness portions of such calls.
- The policies may establish reasonable limits on the amount of long distance business calls by each member. These limits must be structured so as not to interfere with members' ability to do their jobs as legislators.

- Consideration should be given to restricting international calls. World-wide calls are a major risk in toll fraud incidents. Members and employees who need to make international calls could be accommodated either through a reimbursement process, in cases where the need for such calls arises infrequently, otherwise by means of special codes or cards.
- The policies should require that a member or employee must report unauthorized use of House telephones to an appropriate authority within a limited time. (See above, "External and internal reporting.")
- The policies should be delivered to each member and employee at the beginning of service in the House and at least annually thereafter. They should also be incorporated in member and employee manuals or handbooks and in the Members Directory and Official Directory of the legislature published biennially at the beginning of each legislative session.

Review of telephone bills

The House should further increase the monthly scrutiny of long distance telephone bills, including the call detail and monthly totals for individual long distance telephone usage. This should be accomplished as follows:

- Each member and full-time permanent employee should receive and review, each month, a copy of the call detail and cost for their long distance calls. Individual review of long distance phone bills would serve many purposes: It would foster individual accountability and remind people of House policy. It would trigger reimbursements to the House for any personal usage (as discussed above). It would increase the likelihood of early detection of fraudulent use of House long distance phone services and increase the probability of successful prosecution and recovery of costs.

If this capability cannot be provided by the vendor or Admin as a part of the routine billing process, House Administrative Services (HAS) should physically separate and photocopy the call detail to accomplish the same result.

Provision must be made for timely review of bills by individuals. Members and employees should be expected to review bills within 45 days. Those who do not submit their InWATS and credit card bills in the time allowed should be expected to pay the bill personally; the House should not pay for the calls or reimburse in such cases.

- Besides individual review of long distance bills, HAS should continue monthly scrutiny of the call detail in long distance bills. In addition, departmental supervisors should be expected to review long distance bills for their departments. This monthly administrative review is necessary to enforce any House limits on long distance calling. It should also be used to detect suspicious aberrations in the use of open phone stations, to monitor use of phone stations not assigned to permanent, full time employees, and to discover invalid charges for telephones and lines not used by the House.

To assist administrative review, the billing process should provide printouts of long distance phone bills by appropriate departments or divisions of the House. Department heads and supervisors should conduct the review of employee bills and departmental phone stations. HAS should conduct the review of member bills and phone stations not assigned to a department.

House leadership or the Rules Committee should establish standards and procedures to guide members and HAS in reviewing member bills. House administrators should establish standards and procedures to guide employees and supervisors in reviewing employee bills. The procedures should require that irregularities be reported to appropriate authorities within the House and that copies of the report be provided to the member or employee affected. (See above, "External and internal reporting.")

Approval of expenditure abstracts

The House should reevaluate the procedures used to prepare and review expenditure abstracts. Particular attention should be given to the roles and responsibilities of the speaker, leadership staff, the HAS director, and the chief clerk.

Annual independent financial audit

The House should continue its practice of engaging an independent auditor to conduct a financial audit of the House. The audit should be conducted at least each biennium. The scope of the financial audit should be established by action of the Rules Committee. In establishing the audit scope for future financial audits, the Rules Committee should consult with the legislative auditor. The audit report should be addressed to the Rules Committee and should be reported to the Rules Committee in a public meeting. The audit report should be distributed to each member of the House.

Work of the Special Committee

First meeting, March 30, 1993:

- AGENDA: Organizational and informational.
- INFORMATION RECEIVED:
 - ▶ Organization of Special Committee
 - ▶ Letter to House Leadership requesting information
-

Second meeting, April 6, 1993

- AGENDA: James Nobles, Legislative Auditor - Discussion and suggestions as to what assistance Legislative Auditor could provide.
- INFORMATION RECEIVED:
 - ▶ Response from House leadership (administrators)
 - ▶ Letter to Legislative Auditor requesting assistance
 - ▶ Chronology of WATS Access System
-

Third meeting, April 13, 1993

- AGENDA: Bernard Conlin, Assistant Commissioner, Intertechnologies Group, Department of Administration - overview of Intertech
- Bill Schnellman, Director, Telecommunications Division, Department of Administration - explanation of Legislative WATS and Staff WATS systems
- Dana Badgerow, Commissioner of Administration
- Bonnie Plummer, Network Manager, Business Technologies Division
- INFORMATION RECEIVED:
 - ▶ Letter from Chair of LAC limiting Legislative Auditor's assistance
 - ▶ Description of telephone systems used by the House since mid 1980s
 - ▶ Chronology from Department of Administration regarding events in November and December 1991

- ▶ Handwritten chronology of events from Department of Administration
- ▶ Documents from member orientations regarding House phone policy.

Fourth meeting, April 14, 1993

AGENDA: Reviewed draft of the Special Committee Report on House Telephone Controls. Setting agenda for balance of meetings.

Interim Report of Special Committee, April 14, 1993 Attachments separately distributed April 15, 1992 (see page 37).

Fifth meeting, April 20, 1993

AGENDA: Tom Todd, Director, House Research - Summary of Internal Control Structure and Procedure.

David Kienitz, Director, House Administrative Services - discussion of department's procedures regarding phone charges.

INFORMATION RECEIVED: A) House Research -- Summary of Internal Control Structure and Procedure

Sixth meeting, April 22, 1993

AGENDA: David Kienitz, Director, House Administrative Services

Alice Ann Murphy-Grusin, Administrative Assistant, House Administrative Services - answered questions on phone charges

INFORMATION RECEIVED: B) Telephone expenditures by month paid

Seventh meeting, April 23, 1993

AGENDA:

Jim Snyder, MCI, Office of Corporate Systems Integrity,
Wash. D.C. - overall responsibility within MCI for anti-
fraud initiatives

Tom Schutz, Senior Investigator, MCI - Chicago Office of
Systems Integrity

John Henderson, MCI - Technical Support Manager, State of
MN Account Team

Steve Laible, KPMG Peat Marwick - discussion of Audit of
House of Representatives

INFORMATION RECEIVED: C) Statement by MCI
D) Call detail report from MCI

Eighth meeting, April 26, 1993

AGENDA:

James Nobles, Legislative Auditor - DNR Audit of toll fraud

John Asmussen, Deputy Legislative Auditor, Financial
Audits Division

Bill Schnellman, Director of Telecommunications,
Department of Administration

Bonnie Plummer, Product Manager, Network Voice
Manager, Telecommunications, Department of
Administration - follow up questions

David Kienitz, Director, House Administrative Services -
answered questions

INFORMATION RECEIVED: E) Questions answered by DOA
F) Report of the Legislative Auditor regarding DNR Toll
Fraud
G) House Research - Public Reporting of DNR Telephone
Fraud Incident

Ninth meeting, April 28, 1993

AGENDA:

Larry Bothwell, Director of Staff, Majority Caucus -
recollections of the toll fraud and recommendations for
avoiding future phone abuse

Bill Schnellman, Dana Badgerow, Department of
Administration - follow up questions

John Henderson, MCI - follow up questions.

INFORMATION RECEIVED:

- H) House Research -- History of Internal Control Structures
and Procedures in the House since 1975
- I) Assessment of Telephone Systems/Services for the
House - DOA
- J) Letter to DOA requesting transfer of past phone records
- K) Form for Cancellation of phone code
- L) "Dialing for Dollars"

Tenth meeting, May 25, 1993

AGENDA:

Review draft of Special Committee Report

List of Documents

Documents distributed to all members with the interim report of the committee on April 14, 1993:

- ▶ Organization of Special Committee, House Resolution No. 5
 - ▶ Letter to House leadership requesting information
 - ▶ Response from House leadership (administrators)
 - ▶ Letter to Legislative Auditor requesting assistance
 - ▶ Letter from Chair of LAC limiting Legislative Auditor's assistance
 - ▶ Description of telephone systems used by the House since mid 1980s
 - ▶ Chronology from Department of Administration regarding events in November and December 1991
 - ▶ Handwritten chronology of events from Department of Administration
 - ▶ Documents from member orientations regarding House phone policy
- A) Report to the Special Committee on House Management on House Telephones, Summary of Internal Control Structure and Procedure by Tom Todd, House Research, April 20, 1993 (expanded and corrected in #H)
- B) All Telephone Codes Expenditures by Month Paid prepared by House Administrative Services, April 22, 1993
- C) Statement of MCI Telecommunications Corporation before the Special Committee on House Management and Administrative Practices, April 23, 1993
- D) Synopsis, Call Detail Report and Conclusion from Tom Schutz, MCI, April 26, 1993
- E) House Management Practices Committee; Chair: Rep. Thomas Pugh, Questions and Answers, April 26, 1993
- F) Special Review of Unauthorized Long Distance Telephone Calls, Department of Natural Resources, prepared by Office of the Legislative Auditor, July 1992
- G) Information on the Public Reporting of the DNR Telephone Fraud Incident, prepared by Tom Todd, April 22, 1993
- H) History of Internal Control Structures and Procedures in the House Since 1975, prepared by Tom Todd, House Research, April 28, 1993 (including corrections to #A)
- I) Assessment of Telephone Systems/Services for the House, prepared by the Department of Administration, April 28, 1993

- J) Letter to Department of Administration requesting transfer of past phone records dated March 18, 1988. Response letter from the Commissioner of Administration dated March 18, 1988.
- K) Sample cancellation form from Department of Administration.
- L) "Dialing for Dollars," April 30, 1993
- M) Telephone costs by month incurred, 1991-1992, prepared by House Administrative Services, May 3, 1993
- N) Administrative memoranda and materials relating to the DNR incident, submitted by DNR
- O) Letter from Attorney General on DNR incident, October 27, 1992
- P) The STARS contract
- Q) Minutes of meetings
- R) 1993 data privacy law changes

Report to the Special Committee on House Management Practices

on

House Telephones

Summary of Internal Control Structure and Procedure

I. General Internal Control Environment, 1985-1991

Policies

With some exceptions, the House did not adopt clear policies on telephone use or communicate them effectively to members, managers, and staff.

The state telephone book contains a strong statement forbidding the use of WATS service for personal calls and stating that phone bills will be audited and individuals will be subject to legal sanctions.

Written House policies on telephone use are few. There appear to be no resolutions or other official actions by the rules committee on telephone use. Descriptions of WATS billing practices and admonitions against personal use of the phones have not appeared in recent years either in new employee manuals or in manuals distributed to legislators. The House Employee Benefits book contains only one statement allowing limited personal calls to employees in travel status overnight.

The one definite and formal House policy statement regarding telephone use was abandoned at the end of 1988. This policy established a \$600 annual limit on phone calls by members using House credit cards. The standard applied only to credit card calls, not to in-office WATS calls. The rules committee resolution establishing the policy apparently was adopted for the last time in 1987; it was not adopted in 1989 and therefore expired at the end of 1988. (Apparently the limit was allowed to expire in part because it discriminated against members from rural areas and in part because the House was then replacing House credit cards with a new WATS phone system which assigned individual access codes to all members.)

Apart from this \$600 limit on certain types of calls, which was no longer in effect in 1991, the House did not adopt any definition of "excessive" or "inappropriate" phone use to guide managers in reviewing WATS bills.

State and House policy, such as it was, was not communicated to members and staff as clearly and effectively as it could have been. The statement in the state phone book appears in small print on the last of nine pages of detailed instructions about how to use the phone system. Communication to members and staff about House policy occurred mostly in occasional memos from the director of HAS admonishing new members and staff to use WATS lines only for "official legislative business" or "official House business." These memos were addressed and distributed only to new members and staff, generally at the beginning of biennial sessions. In addition, the director of staff and the director of HAS provided oral instructions to individuals or groups as they had the need or opportunity.

The removal of the \$600 limit illustrates the communication problem. The rule setting the \$600 limit was allowed to lapse at the end of 1988. But references to the rule still survived in orientation materials distributed to members in the 1991 session. Moreover, the office responsible for managing phone bills -- House Administrative Services (HAS) -- remained ignorant of the change in policy and continued to employ the \$600 limit for some time (possibly until the end of 1990). HAS finally abandoned the effort when it realized that House policy no longer supported it and when it became apparent that there was no way to enforce it after the House adopted individual WATS codes in place of credit card reimbursements.

One clearly understood House policy may have inhibited close review of member phone bills. As a matter of policy and practice, the House generally regarded member phone bills as very private and confidential information, relating to how members represented their constituents. This attitude (which managers shared) seems likely to have inhibited managers in reviewing member phone bills aggressively.

Managers did not take it upon themselves to recommend stronger control standards and policies to leadership; at least they did not do so formally and in writing. Managers tended to assume that recommendations for sterner standards regarding phone use, particularly as applied members, would not be welcomed or accepted by members or leadership on behalf of members. Managers tend to interpret House actions (e.g., the abandonment of the \$600 cap, in April 1989, and the replacement of the phone bill reimbursement system, in January 1992) as confirmation of their assumption.

Governance by Members

Essentially the responsibility for internal governance of the House is delegated by the House to two members. In some circumstances, this may create difficulties in maintaining proper internal controls.

As the presiding officer of the House, the speaker is formally responsible for internal House administration. However, in recent years speakers have customarily delegated these responsibilities to the majority leader (who the speaker has appointed to chair the rules

committee). The Speaker expected to be kept informed and brought in on important decisions.

The House had no structure or procedure (e.g., ongoing involvement of counsel, external auditor, audit subcommittee) for the responsible staff or leadership to use in circumstances where there is a chance that internal controls might be inappropriately overridden by senior officials. The rules committee does not appear to have an active role in evaluating and setting policy nor does it appear to exercise active oversight in internal House management.

During the last half of 1991, when the breakdown in internal controls occurred, House leadership was in transition. This likely created some unusual and temporary confusion about who had the responsibility and authority for making decisions. The speaker of the House, having announced his retirement, was occupied with other matters and took a less active role than usual in internal House affairs. In mid-July 1991, the majority caucus selected a new majority leader, Representative Welle, who replaced Representative Long, who in turn functioned as the "speaker-elect" until January of 1992.

Management

Responsibility for reviewing and approving House bills, including phone bills, before payment rests both with the Director of House Administrative Services (HAS) and the Director of Staff, Majority Caucus. But for decisions on many important management issues and for decisions on irregularities, especially those involving members, these managers depend upon leadership, particularly the majority leader; on some occasions, managers may have difficulty getting leadership to attend to these matters.

Since 1985, the director of staff is the person that majority caucus leadership has relied on for the overall management and administration of the House. The director is accountable primarily to the majority leader and the speaker.

The HAS director is in charge, generally, of the business affairs of the House. In particular, the HAS director is responsible for reviewing and approving all expenditure abstracts (which are expenditure summaries by accounting object code) and for investigating questionable data as necessary. The HAS director is formally accountable to the director of staff, but often reports directly to and confers directly with leadership.

Both the director of HAS and the staff director review all abstracts, along with detailed supporting documentation, on House expenditures. They do not review individual bills and invoices, except for questionable items. They each report raising questions with other staff managers or members on specific items regularly (i.e., every week). Normally, however, the review of abstracts is a routine double-checking process, because most spending has been approved previously by someone (a member or staff manager) with authority to do so. When

the staff director is satisfied, he stamps the speaker's signature, as required, on the abstract. The speaker does not normally review abstracts.

Managers may consult legal counsel (in House Research) on occasion, but such consultation is not routine.

The requirement that the chief clerk sign abstracts was not, and is not, an effective internal control. The clerk's signature on abstracts is required by law for payrolls and by rule for payments to vendors. Since the mid-1970s, when the responsibility for House finance and administration was transferred from the chief clerk to HAS, the clerk's signature has been a formality without substance. HAS simply stamped the required signature on the abstract; the clerk never saw or reviewed the abstract.

Important matters of management and administration may sometimes languish in uncertainty between leadership and top management. The responsible managers lack authority to make critical management decisions, or they feel that they do. Formal job descriptions assign responsibility, but little authority goes with it. The structure and culture of the House make it very difficult, even for senior staff managers, to police or govern members or other staff with collateral authority. By custom and usage, therefore, and also as a matter of democratic principle, managers look to elected leaders for critical decisions. The managers understand that they must confer with and request final decisions from leadership on important, non-routine, or irregular matters.

The managers generally look to the majority leader for decisions on internal administrative matters. They seek to keep the speaker informed and normally only bring in the speaker on particularly important or difficult decisions.

But leaders are often, and justifiably, focused on other matters. The primary responsibility and interest of legislative leaders tends to be on matters of public policy, not internal House administration. Sometimes leaders are not available to make decisions. Also managers perceive that leaders are generally not eager to tackle administrative issues, especially difficult ones involving other members. As a result, sometimes, important management and administrative decisions may not be addressed in an aggressive or timely fashion.

II. Phone systems, 1985-1991

In-Office Long Distance Calling

The in-office phone system is physically more open than would be the case in a typical office setting. This probably results in some abuses that are difficult to trace.

At least since the mid-1980s, in-office WATS calls have been recorded to the phone station from which the call originated. For each call, the bill for in-office WATS shows the phone station, the date and time of the call, the length of the call, and the charge.

But the open physical environment in the House offices inhibits tight controls. As a matter of custom and policy, House offices are more open to the public than would be the case in most business environments. Phones are regularly left unguarded, and outsiders may take advantage of this, either by using WATS or by direct-dialing to call long distance.

Also House phones are inter-linked in such a way that many phone stations in the House can be accessed by someone calling from other locations. Phone calls can be placed from three locations in the case of phones linked to members, and in as many as a dozen locations in the case of phones linked to leadership.

Remote-access WATS

In April 1989, the House changed its phone system in a way that saved money and increased the potential accountability of members for remote-access long distance calls.

The House turned from a system in which all House members used one code for remote-access WATS to a system in which each member was assigned an individual code. Under the old system, the WATS phone bill received by the House could not show who made the call, whereas under the new system adopted in 1989, each member's remote-access WATS calls were recorded to the member's office phone number on the WATS bill received by the House.

Credit Cards

The individual WATS codes adopted in 1989 also replaced the use of House-issued telephone credit cards, which saved money but may have reduced member accountability.

The change saved money, because calls using the credit cards were not WATS calls but more expensive direct dial calls. But as a practical matter the change probably also reduced individual members' sense of accountability. The credit card bills went directly to members for signature before being paid, whereas under the new system the whole WATS bill went to HAS and members did not see their individual call records.

The 800 Number

The 800 number that members used to reach the capitol when WATS services were unavailable probably reduced member accountability for some long-distance telephoning.

Until recently, this number was answered by capitol operators. Calls to this line -- unlike remote-access WATS calls after April 1989 -- were not attributed to the individual member making the call. For a time, the calls were not even paid by the House, but from a general capitol phone budget. Apparently, it was customary for some members to use this number to connect to WATS.

III. Phone Bill Review: Standards and Procedures, 1985-1991

The bill routing system for WATS bills did not encourage individual accountability: the entire bill, both for calls made from office and remotely, went to HAS directly; individuals never saw nor reviewed their bills. The HAS director did not review phone bills aggressively, and some of the methods used by the director proved to be ineffective.

During the 1985-86 period, HAS monitored WATS calling on each in-office phone. When the monthly total exceeded \$30, HAS called the phone and left a message to alert (not reprimand) the person assigned to that phone. This \$30 standard for in-office use was eliminated in 1987 and was not replaced.

The HAS director did not believe it was proper for him to examine the call detail in phone bills looking for internal fraud or misuse (i.e., inappropriate or excessive use by members or staff). This respected the prevailing attitude that these records were private and confidential. Also the HAS director did not consider it either possible or appropriate, in the absence of a House standard like the \$600 cap, for him to make judgements about excessive or inappropriate use by members or by staff in other offices. In short, the HAS director relied on staff and members to follow the state and House policy allowing WATS only for business purposes.

The method used by HAS to detect external fraud appears, in retrospect at least, to be ineffective. After the abandonment of the \$600 standard in 1989-1990, the HAS director used the bottom line (the total monthly House WATS bill) as the primary method of detecting external fraud. This can now be seen to have been ineffective, because the review could not detect any but massive external fraudulent use. Had HAS been routinely studying the call detail of individuals, the external fraud would almost certainly have surfaced much earlier.

The bottom-line review employed by HAS was also ineffective because it was not timely (at least for the explosive type of external fraud that the House experienced in November, 1991). The bills for one month arrived late in the following month; and sometimes were not

reviewed and approved by HAS for sometime thereafter. Thus the September bill was the most recent bill available to HAS when the fraud was discovered in mid-November.

IV. Changes in House Controls Since November 1991

Internal Control Environment

The general control and management structure is not substantially changed. Particular policies have been changed recently, and the House has begun to articulate and communicate some phone policies more effectively.

Phone Systems

In 1992, the House adopted new phone system controls, which cost more in both money and time but increase members' accountability and reduce the House's financial risk from fraud.

In July of 1992, the House adopted a new system for remote-access WATS service. Under this system, most House members have a "corporate home account" for WATS calls. The member can use the code only from specific remote stations (home, lake home, etc.). Telephone company computers make the assignment to the member's office phone by detecting the phone station that originates the coded call. This reduces the chance of rampant external fraud. Also, because the phone company controls the assignment of calls, the vendor assumes liability for fraud losses.

Members are instructed to use their personal phone credit cards when away from home and submit the bills for reimbursement. Accountability is high for these credit card calls, but they are more expensive than WATS calls.

Some members (30 in 1992, now 26) still use the individual WATS access code system, because the local phone service is not capable of making the computerized assignment required for the corporate home account.

Also beginning in July 1992, remote-access WATS phone bills were re-routed to increase member accountability. Instead of the WATS bill for the entire House going to HAS for payment, each member receives an individual monthly remote-access WATS phone bill. Under this system HAS is not supposed to pay unless the member signs and submits the bill (both the cover sheet and the detailed call record sheet).

Initially, from July 1992 to January 1993, the House used a pure reimbursement system: the member paid the bill, signed a reimbursement form (that contained strong admonitions against personal use), and submitted the form and the bill to HAS for reimbursement. This

reimbursement system was objectionable to members and something of an administrative headache for HAS. Beginning in January 1993, therefore, the system was changed: the bill still goes to the member, but the member no longer must pay the vendor and request reimbursement; instead the member may sign and submit the bill to HAS and the House pays the vendor directly.

These arrangements have created some difficulties, which serve to illustrate the balance that must be struck between stricter internal controls, designed to reduce abuse, and administrative complexity. Because some members did not receive bills, or failed to submit bills as required, the House has been constantly in arrears to the vendor for the remote-access phone bills of members (as much as \$1500 for the bills of about 12 members, currently \$400 for 6 members).

Recent changes in the administration of the 800 number used by members for remote-access to centrex phones also have probably increased member accountability for long distance calls. Beginning in mid-1992, members calling the 800 number reached not the capitol operators but the Sergeant's office. The Sergeant will connect the member only to a centrex number; the Sergeant will not make a long-distance WATS connections for the member. (But the staff person to whom the Sergeant connects the member might make such a connection. If this occurs, the member's call would not be attributed to the member.)

To minimize the risk of outsiders misusing office phones, HAS has recently requested members and staff, when absent for long periods, to either lock their offices or disconnect their phones. This illustrates, again, the trade-off between effective performance of the job and strict administrative controls designed to reduce risk.

Bill Review Standards and Procedures

Beginning in November, 1991, after the breakdown in internal controls was discovered, the HAS director instituted new review standards and procedures designed to reduce the risk of external fraud. However, the HAS director still does not review bills for internal fraud (i.e., inappropriate or excessive use by members and staff), for the same reasons as before. The bill routing system for in-office WATS calls remains the same: individuals do not see their monthly bills. This probably does not contribute to a sense of personal accountability for in-office calls.

The HAS director now scans the detailed call record of individuals, both for in-office WATS and remote WATS calls. The HAS director looks primarily for "irregular" usage from a phone station that would suggest outside fraud. The method used is as follows: the director looks first for more than about 100 WATS calls recorded to a single phone station. He then looks up the name of the individual assigned to that phone and makes a judgement about whether the use by the individual is irregular. The criteria for making this judgement include:

the caller's legislative position; residence (rural or urban); past patterns in phone use; and current legislative events (e.g., internal caucus elections).

If the HAS director finds what he considers an irregularity, he contacts the person responsible for an explanation. In the last year and a half, the director has never found an unexplainable irregularity or fraud using this review process.

The HAS director still does not review bills for internal fraud (i.e., inappropriate or excessive use by members and staff), for the same reasons as before. He continues to rely on members and staff to obey the policy forbidding use of in-office WATS lines for personal calls. Thus, for remote-access and credit card bills, once the member has signed and submitted the bill, HAS pays it without question, automatically.

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Todd -- Outline for report on internal House controls on telephones

A. General control environment

1. Use of phones, state and House policies

- a) The state telephone book contains a strong statement in small print on page 9 forbidding the use of WATS service for personal calls and stating that phone statements will be audited and individuals who misuse the service will be subject to applicable legal sanctions.
- b) Written House policies on telephone use are few. There appear to be no resolutions or other official actions by the rules committee on telephone use. Descriptions of WATS billing practices and admonitions against personal use of the phones have not appeared in recent years either in new employee manuals or in manuals distributed to legislators.
- c) The House Employee Benefits book states that employees in travel status overnight are entitled to reimbursement for actual, documented personal telephone expenditures of up to \$2 per night. This is based on a standard used by state agencies. Presumably this policy would extend to members as well, to allow members to communicate by telephone with their homes.
- d) Memos. New members and staff have been instructed, in occasional memos from the director of HAS, to use WATS lines only for "official legislative business" or "official House business." These memos have been distributed to new members and staff at the beginning of biennial sessions and also to members when phone system changes occurred. For example, a February 27, 1989, memo addressed to all new House members and staff, stated that the charge for WATS calls "is determined by the length of the call. The use of WATS line calling is strictly for official House business. NO personal calls may be made using the WATS lines."
- e) The \$600 yearly cap
 - 1) During the late 1980s and early 1990s, members were informed, in materials describing member benefits and privileges, that House policy imposed a \$600 annual cap on each member's remote-access WATS bill. This cap did not apply to WATS calls direct from the office phones.
 - 2) The materials distributed to members stated that this policy was established by resolution of the rules committee. Such a resolution was apparently passed during the mid-1980s, for the last time in 1987. HAS staff, however, understood that such a policy existed; and until late 1990, HAS monitored member telephone bills accordingly and reported overruns to members.
 - 3) The cap was dropped about the time the House replaced the credit card reimbursement system with a new phone system with individual WATS access codes for each member.
- f) The director of staff and the director of HAS have provided oral instructions to individuals or groups on specific issues as they feel it is needed.

2. Structure

a) Governing body

- 1) Speaker. The House speaker is ultimately responsible for internal fiscal controls in the House. As the presiding officer of the House, elected by vote of the full House, the speaker is responsible for preserving order, controlling physical space and facilities, and signing all abstracts for the payment of money. (Rule 7.01) (An "abstract" is essentially a summary of total payments authorized to be made, organized by accounting categories or codes; it is described in more detail below.)
- 2) Majority leader. The speaker appoints the chair of the rules committee. Traditionally, the chair of the rules committee has been the majority leader, who is elected by the majority caucus. In recent years (at least since 1987), the speaker's attention has tended to be focused on policy and external matters; the speaker has delegated to the chair of

the rules committee general responsibility for dealing with internal management and administrative matters like personnel and spending. However, the Speaker is kept informed of management and administrative issues and decisions as they arise, is commonly brought in on important issues and decisions, and, as the presiding officer, retains ultimate decision-making authority.

b) Director of Staff, Majority Caucus.

- 1) In practice, at least since 1985, this is the staff person relied upon by majority leadership for management and administration of the House.
- 2) Responsibility. The primary objective stated in the director's job description is "[t]o provide management planning and staff coordination over all aspects of Majority Caucus support-service activities." In practice, however, the director is the person relied upon by the majority for overall management and administration of the House.
- 3) Accountability. The director's job description makes the position accountable to "majority caucus leadership." The director understands this to mean the majority leader and speaker. In practice, the director also confers with other caucus leaders, minority caucus leadership, and members as appropriate. The two majority caucus leaders have delegated to the staff director authority to act on their behalf on routine administrative and management matters and decisions. The director understands that he must confer with or request decisions from majority leadership on important, non-routine, or irregular matters. The director generally looks first to the majority leader for decisions on administrative matters and keeps the speaker informed.

c) Director of House Administrative Services (HAS)

- 1) HAS. HAS is the House office responsible for performing certain House internal administrative and business functions (comptroller, financial records, accounting, purchasing, payroll and accounts payable, and some personnel functions).
- 2) Responsibility of the Director.
 - a) The director of HAS is responsible for planning and directing these HAS functions and for managing the HAS staff "... in a manner consistent with established leadership expectations and approved operational authority."
 - b) The HAS director is also responsible for "recommending policies and procedures for leadership approval..." relating to the effective performance of HAS functions, which include review of expenditures.
- 3) Accountability. In the formal management structure of the House the director of HAS is accountable to the Director of Staff, Majority Caucus. The HAS director's job description describes this relationship as follows. The HAS director:
 - a) Helps achieve the "established expectation of Director of Staff"
 - b) "Confers with Director of Staff ... to receive counsel and direction for HAS"
 - c) "Prepares thoroughly documented financial reports for the review of the Director of Staff, providing interpretation and additional data as requested."
 - d) "Participates with Director of Staff in strategic planning of HAS functions, with prime responsibility to help facilitate written goals, objectives and clear expectations of the office."
 - e) "Keeps Director of Staff informed of important developments"
- 4) The director of HAS commonly confers with and reports directly to leadership on issues and decisions within his purview. The director of staff expects the HAS director to inform him on important matters and to include him in important decisions.

d) Chief Clerk

- 1) The clerk is required by law to sign payroll abstracts (MS sec. 3.099), and by House rule to sign abstracts of payments to vendors (Rule 7.03).
- 2) At one time the clerk performed most of the financial functions now performed by HAS. Since HAS was established in the mid-1970s, however, the clerk has not had any authority or responsibility for House expenditures generally.

3. Procedure, routine bills

a) First step: Authorization to spend

- 1) Someone in the House with authority to make or approve spending decisions within certain parameters must authorize the expenditure. Generally these persons are: department directors or other lead staff persons, the speaker, majority and minority leaders, committee chairs, or a member. One of these persons must review and sign the order, invoice, or bill, indicating that the proposed expenditure is an approved expenditure or that the service or material identified in the bill has been received.

b) Second step: Approval by HAS director to pay the bill

- 1) The second step in the payment process requires the director of HAS to review and approve all expenditure abstracts. The HAS director's job description states that the director "[r]eviews and approves for forwarding all ... expenditures abstracts, investigating questionable data as necessary." This is normally a routine procedure, inasmuch as most expenditures have been authorized or approved already by someone with that authority.
- 2) An "abstract" is essentially a summary of House expenditures to be made. The summary is organized by budget categories or "object codes" (e.g., number 202 is phone bills). Physically, the abstract is a large sheet of pink paper. The date and the entity, the House, appear at the top; below is a column of object codes, with the total amount of the expenditure shown for each code, and a grand total for the abstract. There may be many such abstracts prepared in a single week.
- 3) The HAS director has four assistants who prepare and process expenditure abstracts. Generally speaking, one of these assistants handles employee payroll, another handles member payroll, a third handles payments to vendors, and a fourth handles payments to individual members or staff (e.g., reimbursements).
- 4) Along with each abstract, the HAS staff prepares the documentation supporting the abstract. The supporting documentation consists of a computer printout listing all of the invoices, bills, reimbursement requests, etc. that are summarized by the abstract. For each item on the list, the printout displays the name of the payee, a brief description of the cost (the description that appears on the check stub), and the dollar amount. If a single payment on the list contains several separate expenditure items, the separate items that make up the total for that payment are also listed. (For example, a member might receive one payment for various separate expenditures like parking, motel, phone, etc.)

c) Third step: Approval by the director of staff to pay the bill

- 1) After approval of the abstract by the HAS director, the abstract and supporting documentation go to the director of staff for review and approval.
- 2) This is normally a routine procedure, inasmuch as the expenditures have been authorized or approved already by someone with that authority. The director of staff does not see the actual invoices, bills, and reimbursement requests, unless he has a question based on his review of the abstract and supporting computer summary.

d) Fourth step: Speaker's signature authorizing payment

- 1) If the director of staff approves the abstract, he stamps the speaker's signature on it, initials it, and returns it to HAS.
- e) Fifth step: Preparation of the warrant report and warrants by HAS
 - 1) HAS now prints a warrant report on the abstract. The warrant report lists each warrant (check) by number, along with the payee, the date, and the amount of the check.
 - 2) HAS also prints the actual checks at this time.
- f) Sixth step: Chief clerk's signature authorizing payment
 - 1) The procedure used by HAS in recent years has been to stamp the clerk's signature on the abstract. The clerk did not actually review or sign the abstracts, or even see them.
 - 2) In recent weeks, HAS has begun delivering the abstracts to the chief clerk for signature, after the abstracts have been approved by the speaker and before they are delivered to the Department of Finance. The clerk now requires that HAS provide him not only with the abstract but with copies of the warrant report listing the individual checks by number, amount, and payee. But the clerk still does not actually review or evaluate the expenditures before signing the abstract.
- g) Seventh step: Processing by the Department of Finance
 - 1) HAS delivers to the Department of Finance the abstract, the warrant report, the warrants, and the actual invoices, bills, reimbursement requests, etc.
 - 2) Finance reenters the expenditure data in the statewide accounting system.
 - 3) Finance stamps the Treasurer's signature on the warrants.
- h) Eighth step: Posting by HAS
 - 1) Finance returns the warrants to HAS for posting.
4. Procedure, when an expenditure irregularity is suspected
 - a) Director of HAS. The HAS director is responsible for "investigating questionable data as necessary" and reporting the matter to the director of staff and leadership (the majority leader first, the speaker if necessary). In the course of investigating, HAS may question the authorizer of the expenditure. This happens generally one or two times a week. Depending on circumstances, the HAS director may deal on a matter only with the authorizing agent, the director of staff, or on important matters with leadership directly.
 - b) Director of staff. The director of staff is also responsible for investigating and reporting questionable matters to leadership (the majority leader first, the speaker if necessary). It is not unusual (perhaps once a month) for the director to question an authorizer on an expenditure. When it involves staff, he typically goes directly to the staff or supervisor. When it involves members, or a particularly serious matter, he typically goes to leadership first (the majority leader first, the speaker if necessary), then to the member.
 - c) Leadership. Final decisions on questionable expenditures are referred upward by the director of HAS or the director of staff. The staff provides data and advice, but considers such decisions to be the responsibility, generally, of the majority leader. The speaker is kept informed and brought into important or difficult decisions.
 - d) Counsel. The director of HAS, the director of staff, or leadership may consult with House counsel (in House Research), if they consider it necessary. Counsel is not routinely included.
5. Phone bills, chief clerk's responsibility and procedure
 - a) Phone bills from the phones in the House chamber are sent by the vendor directly to the clerk rather than HAS. The clerk, understanding that review of phone bills is the responsibility of HAS, forwards the bills to HAS without examination.

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- b) Phone bills are included in the abstracts that must, by House rule, bear the signature of the chief clerk. The procedures used to affix the signature of the clerk are those described above under "general control environment."
- 6. Phone bills, HAS responsibility generally
 - a) The HAS director is responsible for reviewing and approving all House expenditure abstracts, including telephone abstracts, and for investigating any irregularities in the data. This is explicitly stated in the director's job description.
 - b) After July 1, 1992, members are responsible for reviewing and approving their long distance phone bills for calls originating from outside phones.
 - c) The HAS director has two administrative assistants who, as part of their job, assist in processing phone bills. These assistants rely on the HAS director to review bills for irregularities and to authorize payment. Although some language in the job descriptions of these assistants suggests a responsibility to review bills for accuracy, completeness, and propriety, in practice the assistants view this work as a clerical task aimed at processing expenditure abstracts expeditiously and keeping accurate and complete files and records. They do not consider that they have the authority or responsibility to review bills for irregularities.
 - d) After reviewing and approving the telephone bills, HAS includes the amounts in the draft abstracts, which are then submitted to the staff director for review and approval under the procedure described under the earlier section on the "general control environment."
- B. Long distance telephone control procedures
 - 1. The following describes in more detail the control and standards procedures used by HAS and the House, in the past and currently, in reviewing and approving long distance telephone bills.
 - 2. From 1985 to April 17, 1989
 - a) The phone system
 - 1) For in-office WATS calls, the call was recorded to the phone station from which the call originated. The phone bill received by HAS for in-office WATS calls showed, for each call, the phone station, the date and time of the call, the length of the call, and the charge. This billing system has continued unchanged to the present.
 - 2) For remote-access WATS calls by members, all House and Senate members used one code, and the costs were split between the two bodies, with the House receiving a bill 2/3 of the total. The phone bill received by HAS did not (could not) show who made the call, or from where; it showed only the date and time, the length of the call, the charge, and the destination city and phone number.
 - 3) During this period, the House also issued members a personal credit card, intended for business use when WATS lines were not available (e.g., lines busy or when the member was calling from out of the state). The calls using the card were not WATS calls, but rather more expensive direct dial calls. Under this credit card system, the members would receive the bill directly from the vendor and submit the bill to HAS for payment. HAS paid the vendor directly.
 - b) HAS review procedures and standards
 - 1) In general, HAS relied on members and staff to follow state and House policy forbidding personal use of the phones. HAS did not review the destination of calls and had no means to judge which calls were "appropriate."
 - 2) Throughout the period, the House imposed a \$600 annual limit on each member's phone credit card. HAS enforced this standard as follows: HAS kept a running total of each member's credit card bill. When the total approached \$600, HAS alerted the member.

When the total exceeded \$600, HAS informed the member and quit paying the member's credit card bill.

- 3) During the 1985-86 period, HAS also monitored WATS calling on each in-office phone. When the monthly total on the phone exceeded \$30, HAS called the phone and left a message intended to alert (not reprimand) the person assigned to that phone. This \$30 standard was eliminated in 1987. In the absence of a House standard for identifying "excessive" WATS use, the HAS director considered that any HAS standard constituted an inappropriate and uninformed personal judgment about how members should represent their constituents and how staff should do their jobs.
 - 4) Throughout the period, HAS reviewed the total "bottom-line" WATS charge to the House on a monthly basis. The purpose of this review was to detect, in a timely way, evidence of external fraud (unauthorized use of access codes).
 - 5) Telephone bill review was not a high priority job within HAS. Close monitoring of details of these bills (which can be inches thick) takes a lot of time, and staff had many other duties. Telephone bill analysis was done when and as time permitted.
3. From April 17, 1989, to November, 1991 (when the fraud was discovered)
- a) In April of 1989, the House adopted a new system for remote access WATS calls.
 - 1) Each House member was assigned an individual code for access to WATS.
 - 2) The code allowed access to WATS from anywhere in the US, not just from Minnesota.
 - 3) When the member used the code, the call was recorded to the member's in-office phone number.
 - 4) This system was adopted in part to save money by encouraging more use of WATS service. Until this time, as explained earlier, when members were away from the office they did a lot of (expensive) direct dial long distance calling, using credit cards issued by the House.
 - 5) The House stopped issuing phone credit cards to members and stopped paying these bills directly. Members with personal credit cards could still apply to HAS for reimbursement for business calls using their card.
 - b) HAS review procedures and standards
 - 1) Each month, after mid-month, HAS received the House WATS bill for the previous month. The bill came in the form of a thick computer printout. The printout listed all WATS calls, whether made from the in-office phone or by remote access code. The calls were listed in numerical order, by in-office phone numbers. For each call, in addition to the in-office phone number, the print out showed: the month and date of the call; the length of the call; the charge; the destination city and phone number; and, for member phones, whether the call originated from the member's in-office phone or had been recorded to that phone from a remote access call.
 - 2) For in-office WATS calls, HAS reviewed only the bottom-line total for the House. This continued the standard of review used before 1989, when members all had the same code. The purpose of this review was to detect in a timely way evidence of external fraud (unauthorized use of access codes). HAS did not review the detailed call record data or total on individual in-office phones, considering that it did not have any means of judging appropriateness of calls.
 - 3) Until approximately the end of 1990, HAS continued to review the individual remote-access WATS call records of members, using the \$600 limit even though the limit had expired. HAS reviewed the individual call records (which were available under the

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new system of individual access codes) and alerted members when they exceeded the limit.

- 4) The \$600 limit was abandoned at the end of 1988.
 - a) Members from outside the metropolitan area considered it unfair. Members in rural areas often had to use long distance to reach constituents from home, and many members living in rural areas regularly exceeded the limit. Furthermore, metro members could drive to the Capitol and call from their in-office WATS line without limit.
 - b) Also, because HAS was no longer paying credit card bills for members, HAS had no ready means of enforcement.
 - c) At the beginning of 1991, a new staff person took over the job of processing phone bills in HAS. The procedure for checking the \$600 limit was no longer a part of the job.
- 5) In the absence of a review standard defined by the House to replace the \$600 limit, the HAS director adopted the same standard then in use for in-office WATS calls: he reviewed only the total bottom-line House WATS bill, for the purpose of detecting a rise in the total that suggested external fraud.
- 6) Telephone bill review was not a high priority job within HAS. It was done when and as time permitted.

4. From November 1991 to June 1992

- a) The phone system remained the same, but HAS instituted new review standards and procedures.
- b) After the breakdown was discovered, the HAS director began scanning the detailed call records of all individuals, both for in-office WATS and remote WATS calls.
- c) The standard used by the HAS director
 - 1) HAS did not look for "inappropriate" use of phones (by examining destination phone numbers or length of calls). HAS continued to rely on members and staff to obey the policy forbidding use of WATS for personal calls.
 - 2) HAS looked instead for "irregular" usage from a phone station that would suggest outside fraud. The method used was as follows: HAS looked first for more than about 100 WATS calls recorded to a single phone station. HAS then looked up the name of the individual assigned to that phone. HAS then made a judgement about whether the use by the individual was irregular. The criteria for making this judgement included: the caller's legislative position; residence (rural or urban); past patterns in phone use; and legislative events (e. g., internal caucus elections).
 - 3) If HAS found an unexplainable irregularity, it contacted the person responsible for an explanation. HAS has never found an unexplainable irregularity using this method.

5. From July 1992 - present

- a) On July 1, 1992, the House adopted a new phone system for remote-access to WATS service. This system is in effect today.
 - 1) Most House members have a "corporate home account" for use from home.
 - a) A member calling from home (or lake home, or other office) uses a WATS access code. All members use the same code, but telephone company computers attribute the call to the member's office phone number. The computers make this assignment by detecting the phone station that originates the call,

- b) The advantage of this system is that it reduces the House's financial risk. Because the code can only be used from home phone stations, the chances of external fraud are much reduced. Also the vendor (AT&T) controls the computer making assignments and thus assumes liability for external fraud. The disadvantage is that calls cost more than on the old WATS access code system (but still less than using a personal credit card). The system also creates some extra costs for the House: for minisessions it can cost \$1000 to make WATS lines available to members with the corporate home account.
- 2) Some members (30 in 1992, now 26) still use the individual access code system (because the local phone service is not capable of making the computerized assignment required for the corporate home account).
- 3) Some members prefer not to use the WATS service available from their homes. Instead they use regular direct dial long distance service from their homes and submit their personal home long distance bills with an indication of which calls were business calls.
 - a) The House reimburses these members. The cost is higher than for WATS calls, but the total dollar amount is low.
 - b) Members do this for a variety of reasons. Some find the separate billing from the House account to be a nuisance, either because they don't make a lot of long distance calls from home or they already have complicated billings from several long distance carriers. Members with the WATS access code system object to using it, because it requires entering about 15 digits to complete a call, and the system is notoriously touchy.
- 4) When members are away from home, they are instructed to use personal telephone credit cards. (The 26 members with WATS access codes, however, can make cheaper WATS calls from anywhere in the US.) Members sign and submit credit card bills to HAS for reimbursement in the same fashion as at-home WATS bills.
- b) HAS review standards and procedures
 - 1) The bill goes directly from the vendor to the member's home address. The corporate home account bill looks like an ordinary telephone bill: it has a cover total sheet and a detailed call record sheet (showing, for each call, the date and time, the length of the call, the amount charged, and the city and number of the destination phone). The access code bill looks more like a computer printout than a phone bill; it also has a cover summary sheet (showing the member's name, the vendor (Mn Telecomm), and the word "invoice" at the top), and a detailed call record sheet (showing, for each call, the member's 296-number, the date and time of each call, the length of the call, the amount charged, and the city and number of the destination phone).
 - 2) The House has used two systems for paying these bills.
 - a) From July 1992 - January 1993, the House used a reimbursement system.
 - i) The member paid the bill and submitted it to HAS with a reimbursement form.
 - ii) The form stated the House policy, i.e., that reimbursement was only permitted for "long distance calls relating to official legislative business." The form also had a place for the dollar amount requested for reimbursement. The form had a place for the member's signature, under a statement: "I declare under the penalties of perjury that this request contains calls relating to official legislative business only and that no part has been previously submitted."
 - iii) Members objected to the reimbursement system. Also the system was difficult for HAS to administer.

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- b] Beginning in January 1993, the House changed to a direct payment system (for most members).
 - i] The bill still goes to the member. But the member does not pay the vendor and request reimbursement; instead the member signs and submits the bill, and the House pays Mn. Telecomm.
 - ii] Some members prefer to use the old reimbursement system. HAS reimburses these members.
- 3) HAS will not authorize payment (or reimbursement) unless the member signs and submits the bill (both the cover summary sheet and the detailed call record sheet) to the HAS. This is in accordance with recommendations of the House's external auditor.
- 4) Some members have not submitted signed bills, as required. The House has been up to \$1500 in arrears to Mn. Telecomm., for the bills of about 12 members who have not submitted signed bills. Currently, this stands at \$400 for 6 members.
 - a] The bill for the corporate home account cumulate the total owed, month to month, so the latest bill includes unpaid amounts from prior months (without interest). Thus, if a member signs the latest bill, HAS would regard the signature as good for the total amount, including prior month's billing (even though the required call detail record has been lost for the prior months).
 - b] The bill for the members using the access code does not show cumulative amounts, only the amount for the current month. Thus, if a members fails to turn in the monthly bill as required, both the call detail and the monthly total are lost.
- 5) HAS does not review or evaluate these remote access WATS bills and reimbursement requests from members. HAS relies entirely on members to determine what is an acceptable level of cost and also to determine which of these calls meets the House standard ("official legislative business" only). In effect, the member's signature and submittal of the bill for payment or reimbursement satisfies the House's standard. Staff pays submitted bills without question, automatically.
- 6) HAS processes member requests credit card reimbursement in the same automatic fashion.
- 7) In-office WATS calls
 - a] HAS continues to review the detailed call record of in-office WATS calls, using the same standard as described above, for the period from November 1991 - June 1992.
 - b] In the year and a half since beginning this review process, in November 1991, HAS has never contacted anyone about inappropriate use or discovered misuse of in-office WATS lines through this review process.
- c) In 1993, HAS developed a new computer database program (using Paradox) that will keep track of the monthly WATS remote and credit card phone bills of each member, in a fashion similar to the tracking system that was in place in the late 1980s.
 - 1) This program was used to produce the 1991-92 phone bill totals that the House released during the last month.
 - 2) The program is not in use yet as an ongoing record-keeping tool, because HAS has not decided yet whether the entry should be recorded to the month the call was made by the member and charged to the House, or the month that HAS receives the signed bill from the member. (Often bills from members are submitted many months after the fact.) The data entry procedures is also related to another decision still to be made by the House: whether the House will institute any controls on member phone use (e.g., a time limit for submission of phone bills by members).

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C. Long distance direct-dial (i.e., dialing 9-1-XXXXXX)

1. In addition to direct-dial bills submitted by members using credit cards, HAS receives two bills for direct-dial long distance calls made from office phones (one bill from AT&T, the other from US West).
2. These bills indicate the phone used to make the call, the date and time, the length of the call, the charge, and the destination city and phone number.
3. Review standard. The HAS director considers an irregular bill to be one that is over \$10 from a single office phone in one month. HAS calls the person assigned to that phone to discourage the use of direct dial and encourage the use of the cheaper WATS system.
4. The use of direct-dial from the office may be appropriate under some circumstances (e.g., if all WATS lines are busy).
5. The amount of money spent for long distance direct dial is small, usually rising slightly with each new legislature. HAS considers the intermittent overuse of direct long distance dialing to be the result mostly of ignorance (by outsiders using the phones or by poorly trained new members and staff).

D. 800 calls

1. The House is billed for the public information 800 number, which is answered in the House information office.
2. The other 800 number is the one members use to reach capitol centrex numbers.
 - a) Until mid-1982, the number was answered by capitol operators. Since mid-1992, this number is answered in the Sgt. at Arms office during working hours.
 - b) Calls on this line were, and are, not attributed to the individual member making the call. The calls were paid out of the capitol operator budget; now they are paid by the House. Apparently, until recently it was common for some members to use this number to connect to WATS; such a call was not attributed to the member (as it would have been after April 1989 if the member had used remote-access codes to WATS).
 - c) Currently, the Sgt. at Arms will not make a long-distance WATS connection for a member calling on this line. But the staff person to whom the Sgt. connects the member might make such a connection. If this occurs, the member's call would be billed to the House and would not be attributed to the member.

E. Changes in House controls in response to the November 1991 fraud incident

1. The general control and management structure is not substantially changed. Particular policies have been changed recently, and the House has begun to articulate and communicate policy more clearly.
2. Phone system changes
 - a) In July 1992, the House adopted a new phone system for remote-access WATS service. This system costs more in both money and administration time, but it increases the member's accountability and reduces the House's financial risk from fraud.
 - 1) Under this system, most House members have a "corporate home account" for WATS calls. The member can use the code only from specific remote stations (home, lake home, etc.). Telephone company computers make the assignment to the member's office phone by detecting the phone station that originates the coded call. This much reduces the chance of rampant external fraud. Also, because the phone company controls the assignment of calls, the vendor assumes liability for fraud losses.
 - 2) Some members (30 in 1992, now 26) still use the individual access code system because

the local phone service is not capable of making the computerized assignment required for the corporate home account.

- 3) Members are instructed to use personal phone credit cards for House when away from home and submit the bills for reimbursement. Accountability is high for these calls, but they are more expensive than WATS calls.
- b) Also beginning in July 1992, remote-access WATS phone bills were re-routed to increase member accountability. Instead of the WATS bill for the entire House going to HAS for payment, each member began to receive an individual monthly remote-access WATS phone bill. Under this system HAS will not pay unless the member signs and submits the bill (both the cover sheet and the detailed call record sheet).
 - 1) From July 1992 to January 1993, the House used a pure reimbursement system: the member paid the bill, signed a reimbursement form that contained strong admonitions against personal use, and submitted the form and the bill to HAS for reimbursement.
 - 2) The reimbursement system was objectionable to members and an administrative burden for HAS. Beginning in January 1993, the bill still goes to the member, but the member no longer must pay the vendor and request reimbursement; instead the member signs and submits the bill to HAS and the House pays the vendor directly.
 - 3) This arrangement has created some difficulties, which serve to illustrate the trade-offs between internal controls and administrative hassles. Because some members did not receive bills or failed to submit bills as required, the House has been as much as \$1500 in arrears to the vendor for the bills of about 12 members (currently \$400 for 6 members).
- c) Recent changes in the administration of the 800 number used by members for remote-access to Centrix phones have probably increased member accountability for long distance calls. Beginning in mid-1992, members calling the 800 number reached not the capitol operators but the Sergeant's office. The Sergeant will connect the member only to a Centrix number; the Sergeant will not make a long-distance connection for the member. But the staff person to whom the Sergeant connects the member might make such a connection. If this occurs, the member's call would not be attributed to the member.
- d) To minimize the risk of outsiders misusing office phones, HAS has recently requested members and staff when gone for long periods to either lock their office or disconnect their phone. This again illustrates the trade-off between job effectiveness and internal controls designed to reduce risk.
3. Bill review standards and procedures.
 - a) He now scans the detailed call record of individuals, both for in-office WATS and remote WATS and long distance calls.
 - b) The HAS director looks primarily for "irregular" usage from a phone station that would suggest outside fraud. The method used is as follows: HAS looked first for more than about 100 WATS calls recorded to a single phone station. HAS then looked up the name of the individual assigned to that phone. HAS then made a judgement about whether the use by the individual was irregular. The criteria for making this judgement included: the caller's legislative position; residence (rural or urban); past patterns in phone use; and legislative events (e. g., internal caucus elections).
 - c) If the HAS director finds what he considers an irregularity, he contacts the person responsible for an explanation. In the last year and a half, the director has never found an unexplainable irregularity.
 - d) The HAS director still does not review bills for internal fraud (i.e., inappropriate or excessive use) by members and staff, for the same reasons as before. HAS continues to rely on members and staff to obey the policy forbidding use of in-office WATS lines for personal calls.

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For remote-access and credit card bills, once the member has signed and submitted the bill, HAS pays it without question, automatically.

- c) The bill routing system for in-office WATS calls remains the same: individuals do not see their monthly bills.
4. In 1993, HAS developed a new computer database program that it can use to keep track of the monthly long-distance phone bill of each member, in a fashion similar to the tracking system that was in place in the late 1980s.
- a) This program was used to produce the 1991-92 phone bill totals that the House released during the last month.
 - b) The program is not in use yet as an ongoing record-keeping tool, because HAS has not decided yet whether the entry should be recorded to the month the call was made by the member and charged to the House, or the month that HAS receives the signed bill from the member. (Often bills from members are submitted many months after the fact.) The data entry procedures is also related to another decision still to be made by the House: whether the House will institute any controls on member phone use (e.g., a time limit for submission of phone bills by members).

STATEMENT OF MCI TELECOMMUNICATIONS CORPORATION
BEFORE THE SPECIAL COMMITTEE ON HOUSE MANAGEMENT
AND ADMINISTRATIVE PRACTICES

April 23, 1993

Mr. Chairman,

Thank you for the opportunity to address the Special Committee on House Management and Administrative Practices and assist the Committee in its inquiry into the State's Telecommunications Systems.

My name is Jim Snyder, and I employed by MCI in the Office of Corporate Systems Integrity, in Washington DC which has overall responsibility within the company for anti-fraud initiatives. Appearing with me today are Tom Schutz, Senior Investigator from the Chicago office of Systems Integrity and John Henderson, Technical Support Manager for the State of Minnesota MCI account team.

Mr. Chairman, as you know this matter is under investigation by the Minnesota State Attorney General's office, and the Ramsay County Attorneys Office. MCI is cooperating fully with these investigations. In addition to providing records which have been requested, representatives of MCI have met with officials from both agencies to discuss the role of MCI with the expectation of an equitable resolution of this matter.

I would respectfully request the indulgence of the Committee if the MCI representatives decline to discuss in this forum issues, the public discussion of which, would impede the progress of the proceedings by either the Attorney General or the Ramsay County Attorney.

Mr. Chairman, telecommunications toll fraud, such as that which affected the Minnesota State legislature is generally known as "Customer Premise Equipment (CPE) fraud" because it takes advantage of "remote access functions" in equipment that is provided and operated by the customer or an entity selected by the customer.

The problem of CPE fraud is significant and affects the customers of all telecommunications carriers in the United States. In testimony before the United States House of Representatives Subcommittee on Finance and Telecommunications, the Special Agent in Charge of the Financial Crimes Division of the United States Secret Service testified that CPE fraud in the United States exceeds \$2 billion annually.

MCI is committed to combatting this problem and to this end has instituted a multifaceted approach that involves an extensive awareness program, technical analysis of customer traffic in an effort to identify unauthorized calls, security equipment provided by third party vendors to supplement features resident in Customer Premise Equipment, and insurance provided by third party insurers.

I have supplied to the Committee, Mr. Chairman, several copies of two MCI videos which MCI provides to telecommunications managers and others in order to educate them about the threat posed by CPE Fraud. I would encourage the members of this Committee to watch the videos since they describe the nature of CPE fraud and some of the preventative measures which can be implemented. I have also provided to you informational brochures which we also distribute to customers.

The toll fraud which is the subject of these hearings, resulted from the abuse of a "remote access function" that was resident in a Centrex system. In examining how this fraud might have occurred, it is important to understand that a Centrex is a piece of Customer Premise Equipment which MCI does not sell, service, operate, or otherwise control.

The State's Centrex system provides the connection between the telephones in various State office buildings and the public telephone network operated by US West and the various long distance carriers.

The remote access capability of the Centrex, which has been referred to in these hearings as a WATS service, enables a caller who is away from his/her office telephone to make local and long distance calls through the Centrex to the desired location.

In essence this feature replicates the function of telephone calling

cards in that it permits callers to complete calls. Just as a calling card code issued by a telephone company is checked by a computerized validation system before the call is completed, the authorization code entered by a caller using the State's system is validated by the Centrex to insure that the caller has entered a valid authorization code.

The systems operated by all the major long distance carriers to monitor calling card codes, are staffed 24 hours a day, 365 days a year to detect fraudulent and unauthorized usage. The carriers are able to perform this monitoring function because they control all aspects of the validation process, from determining the length of the authorization code (typically 14 digits) to monitoring the frequency of use of the code. Because MCI controls the validation process with respect to the calling card codes it issues, MCI will assume the financial liability associated with lost or stolen MCI calling card codes.

MCI did not and does not have visibility into the operation of the State's Centrex remote access function, and, therefore, had no opportunity to monitor the usage of assigned Centrex remote access authorization codes. Because the validation of the access code entered by callers was performed by equipment that is outside the control of any long distance carrier, MCI was unable to monitor how often any particular code was being used, or otherwise monitor individual codes for fraudulent or unauthorized usage. This inability to view how any particular authorization code is being used severely limits the ability of any long distance carrier to detect unauthorized usage on this type of service.

It is, of course, impossible for any telecommunications carrier to determine the validity of each of the thousands of calls which are handled by a customer's equipment on a daily basis. Even assuming that telephone company employees monitored the content of each and every call, which would not only be impossible but would be highly improper, it still would be very difficult to determine which calls were appropriate and which calls were not authorized by the customer. There is nothing which outwardly distinguishes an individual fraudulent call from a call which is authorized by the customer.

All of the major long distance carriers, including MCI, have implemented programs and systems that attempt to address the

problem of unauthorized remote access calling from customer equipment. These programs analyze a customer's phone traffic and attempt to identify anomolous calling patterns which might indicate that a customer's telephone equipment is being used by unauthorized persons.

Each of these programs have inherent limitations in that the identification of fraudulent use is dependent upon the observation of patterns of calls such as high call volumes to foreign destinations, off-hours calling, long duration calls and so on. These programs are imprecise and require an observable amount of unauthorized calling to occur before the problem can be identified. The volume of calls coming from any given customer location can fluctuate widely on a daily basis and the more legitimate calls that are placed from the customer's system, the longer it takes to discern a pattern suggesting that fraudulent calls are occurring.

Even when the carrier's programs identify anomolous calling patterns indicative of fraud, the carriers can only make educated guesses regarding whether observed traffic patterns are, in fact, legitimate or fraudulent. For example, MCI might detect a significant increase in the daily volume of calls from the House Centrex system, which, as I pointed out, is often one of the indicators of fraud. However, the increase in call volume might have a legitimate explanation as well. For example, an increase in traffic might be attributable to Representatives and staff conducting a major effort to call constituents about a particularly controversial legislative proposal.

MCI has and will be presenting to the Office of Administration a wide variety of options to counter the threat posed by CPE fraud. Working together with the Office of Administration, MCI will help identify the best solution to meet the unique needs of the State of Minnesota in terms of security, convenience and cost.

For example, one possible solution to the need of state officials to securely make telephone calls while away from their offices would be the use of telephone credit cards such as the MCI VNET Card. As noted previously, because MCI controls the validation process on all calls which are made using MCI cards, MCI will assume the financial liability on calling cards which are lost or stolen.

Mr. Chairman, it is the position of MCI that in addition to providing technical controls and systems to minimize the occurrence of fraud, there must also be the proactive investigation and prosecution of those who commit telecommunications fraud.

To this end, in 1991, MCI investigations resulted in the arrest of over 200 individuals for telecommunications fraud. Last year, this number increased to over 250 arrests.

MCI has taken a leading role in the education of law enforcement in the investigation of telecommunications and related crimes. For example, representatives of MCI's Office of Corporate Systems Integrity have instructed at such courses as Special Agent Training Courses for agents of the United States Secret Service, the FBI, the Federal Law Enforcement Training Center in Glynco, Georgia, the New York District Attorneys Office, the South Carolina Criminal Justice Academy and, police officers in the State of Minnesota.

The Office of Corporate Systems Integrity is staffed by dozens of former Secret Service and FBI agents and police detectives. It is their responsibility to assist MCI customers in the investigation and presentation of cases to law enforcement officials.

In this case, Investigator Schutz met with representatives of the Department of Administration and House Administrative Services to advise them that he would render whatever assistance was required in order to pursue all available avenues of prosecution.

Mr. Chairman, this concludes the opening statement of MCI. Investigator Schutz and Mr. Henderson, who also was in attendance at the meeting with the representatives of the Department of Administration and House Administrative Services are present to respond to the questions of the Committee.

Research Department

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Minnesota House of Representatives

April 28, 1993

TO: Members of the Special Committee on House Management Practices

FROM: Tom Todd, Director

RE: History of Internal Control Structures and Procedures in the House Since 1975

The attached document is prepared in response to a request from the Special Committee to summarize and clarify the historical development of internal control structures and procedures in the House.

The document includes some clarification and corrections to my earlier report, dated April 20, 1993.

Like the earlier report, this document relies exclusively on administrative staff as sources. The information now comes from one or more interviews with about a dozen House staff, past and present; many have also reviewed earlier drafts of this document.

Among the more salient points in the document are the following (references are to the attached outline):

- On the sharing of duties between the speaker and majority leader (B.1)
- On the concept of a central, nonpartisan "House Administration" office, intended to segregate finance/administrative staff functions; the origin of this idea in a consultant's report in the early 1980s; the partial implementation of the idea in the early 1980s; and departures and variations on the theme since 1985 (D.1-3; E.1-4; F.2-3)
- On changes in the staffing of fiscal control functions in the business/finance office; the departure of one of the two key fiscal control staffers in 1985 (the person who had controlled the preparation and review of accounts payable and reimbursement abstracts); the elimination of that position, also in 1985; and the

development of personnel and information computer services functions (C.1-2; D.4; E.5-6; F.4-5)

- **On internal expenditure controls that precede the preparation of expenditure abstracts (B.2)**
- **On changes in practices in reviewing expenditure abstracts; the practice of two speakers (Searle and Jennings) who apparently reviewed and signed personally at least expense abstracts (i.e., accounts payable and reimbursements); the decline, especially after 1984, in personal signature on abstracts by the Chief Clerk; the practice, before the mid-1980s, of attaching copies of actual invoices to expense abstracts; and the replacement of invoices with computer generated documentation in the mid-1980s (C.2; D.4; E.6; F.5)**
- **On the privacy of phone bills and the \$30 standard for notifying users of in-office WATS service (B.4)**

April 28, 1993

Tom Todd, House Research

Historical Development of Internal Control Structures and Procedures in the House, 1975-1992

Organization

1. Section A -- Introduction
 2. Section B -- General Control Features
 3. Section C -- 1975-80
 4. Section D -- 1981-84 (the Sieben period)
 5. Section E -- 1985-86 (the Jennings period)
 6. Section F -- 1987-present
- A. This document is prepared in response to a request from the Special Committee on House Management Practices. The request was to summarize and clarify the historical development of internal control structures and procedures in the House.
1. This document includes some clarification and corrections to my earlier report dated April 20, 1993.
 2. Like the earlier report, this document relies exclusively on administrative staff as sources.
- B. Additional perspectives on general control features for the entire period:
1. The administrative responsibilities of the speaker and majority leader, respectively, have varied somewhat over time, depending in part on personal interests and relationships. Often the two share responsibility for decisions. Generally, the majority leader has a stronger role in matters relating to the rules committee's jurisdiction -- over personnel and payroll, budget, and payments to members and committees. The speaker has more responsibility in other administrative matters, including accounts payable, expenditures, and facilities. As the presiding officer, the speaker is also generally in a position to have the final word on any administrative matter. Routine administration of internal controls has always been delegated by leadership to staff, who generally do the job without a lot of oversight or intervention.
 2. For most expenditure categories, the preparation of abstracts was, and is, only the last step in spending authorization and verification. Before even reaching the House administration staff responsible for preparing abstracts, most invoices must be reviewed and signed by someone outside of House administration with spending authority (e.g., a director of another office, committee chair, member, etc.). A few invoices go directly to House administration (e.g., bills for some types of phone usage) for review and approval internally in House administration.
 3. The finance staff makes available to leadership: (a) an accounting of payments made to each member, (b) an accounting of House expenditures by category. These documents, or the data from which they are developed, were and are public information, available to others and the press on request. Practice has apparently varied over the years in how often, how regularly, and how widely circulated this information has been. Some staff think that the information was more widely and regularly available in earlier years than in more recent times.
 4. On phone bills:
 - a) From the mid-seventies, the staff did not review WATS phone bills in detail, because the speaker (Sabo) had directed that the bills were private data. The staff kept closer account of

reimbursements for long distance credit card calls. The staff also tried to limit expensive direct-dial long distance calls.

- b) Some staff have said they remember a \$25-30 trigger for notifying users (by means either of a phone message or a form-memo) about in-office WATS use. The message was a "for-your-information" notification only; apparently it was fairly inconspicuous, since recipients don't remember it. This practice seems to have begun in the late 1970s, extended until the mid-1980s, and fallen into disuse after 1987.

C. 1975-1980

1. The House Finance Office was established by Speaker Sabo in 1975. Fiscal functions and staff were transferred from the Chief Clerk.
 - a) D Kienitz was appointed director.
 - b) Two key fiscal control staff (one for accounts payable, reimbursements, and the budget; the other for payroll and personnel) were transferred from the Chief Clerk.
 - c) Several subordinate clerical staff reported to the two fiscal control staff.
2. The two fiscal control staff reviewed all expenditure documents, checked on questionable items, prepared expense and payroll abstracts, and secured the required signatures.
 - a) Kienitz did not normally review these materials, not at least in any detail.
 - b) The abstracts went to the speaker's office for signature. Some staff remember bringing supporting documentation (the bills, invoices, and reimbursement forms), others remember just bringing the abstracts.
 - c) Speaker Sabo's administrative assistant reviewed the abstracts and any documentation. The speaker may actually have signed the abstracts, but relied on the staff's prior review. Speaker Searle, on the other hand, preferred to review and sign abstracts personally.
 - d) The staff then took the abstracts to the chief clerk for signature. Only if the clerk was not available did they use a stamp. Because all House offices were still in the Capitol, they generally were able to get the clerk to sign.

D. 1981-1984 (the Sieben period)

1. Stanton Associates conducted a management study during 1981, which was presented to the rules committee in July, 1981; the committee adopted the recommendations in part.
 - a) Stanton recommended the creation of a personnel system -- to include systematic job audits, compensation ranges, performance reviews, etc.
 - b) In administrative matters, Stanton envisioned a segregation of the functions of fiscal/administrative staff from the functions of caucus leadership staff.
 - c) Stanton recommended the creation of a nonpartisan "House Administration" office, headed by a "House Administrator" responsible for all financial controls and records, budget, personnel administration, purchasing and supply, facilities and space, the House Information office, information systems and computerization, and House educational services. Stanton's report described the purpose of this job as follows: "To manage and coordinate the financial and administrative functions of the Minnesota House ... in a manner which will ensure financial controls are maintained, and quality and nonpartisan services are provided members and staff. Will effectively implement and coordinate the bipartisan administration of the compensation program and related policies for staff employees."
 - d) Stanton envisioned a unified administrative structure for the House, in which all House staff offices, partisan as well as nonpartisan, would report to the nonpartisan House Administrator, on administrative matters.

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2. Sieben hired J Pederson as "House Administrator" (starting about January 1982). Pederson reported directly to the Speaker and also on occasion to the rules committee.
 - a) Pederson headed a small office called "House Administration."
 - b) He hired an administrative assistant whose job increasingly focused on the personnel system. He also hired an information systems administrator to deal with computerization. Both reported directly to Pederson.
 - c) Pederson was the chief financial officer of the House. He oversaw the House Finance Office; Kienitz reported to Pederson. Pederson presented the annual budget to the rules committee and prepared summary reports on expenditures as required.
 - d) The internal organization of the House Finance Office remained much the same as before.
 - e) Pederson was House administrator for three years (1982-84). He was occupied, especially for the first two years, in implementing the Stanton recommendations on a personnel system (job audits, compensation ranges, performance reviews, etc.). For much of last two years, he was occupied in planning and managing the reconstruction of the SOB (a project completed at the end of 1984).
 - f) Pederson intended, and believed the speaker intended, to implement the Stanton recommendation for a more unified, House-wide administrative structure. Pederson used a "Staff Directors Advisory Group" as a device to improve communication among managers and to formulate advice to leadership on administrative policy and procedure. Under Pederson, this group met regularly and included staff directors from both partisan and nonpartisan offices.
3. Although the structural developments generally moved toward the administrative structure envisioned by Stanton, it did not fully implement that structure. Among the relevant points:
 - a) The chief administrator's office was physically separated from the majority caucus and the leadership corner.
 - b) Duties were somewhat segregated.
 - 1) Pederson's responsibilities were limited to administration: facilities, business and finance, budget, information systems/computers, purchasing, travel, personnel, etc.
 - 2) He reported to the speaker and leadership, but he was not part of leadership staff. Pederson was not the majority caucus staff director (which was the job of A Benson, who reported to the majority leader, Eken.)
 - 3) Nor was Pederson used by the majority caucus as a legislative strategist.
 - c) On the other hand, the speaker's executive assistant (M Novak), not Pederson, reviewed and approved expenditure abstracts.
 - d) Stanton had recommended a nonpartisan office. Pederson had a partisan background, along with high level administrative experience in state agencies. (The speaker believed both were important in the job.)
4. In House Finance, the same two fiscal control staffers continued to review all expenditure documents, prepare expense and payroll abstracts, and secure the required signatures.
 - a) The abstracts went first to Kienitz for his signature (a new step, required by Pederson).
 - b) Then the abstracts went to M Novak, the speaker's executive assistant, who reviewed the abstracts and supporting documentation. For the expense abstracts, the supporting documentation continued to consist of copies of the actual bills, invoices, and reimbursement forms.

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- c) Novak signed the abstract for the speaker and initialed it. The speaker did not see or review it, unless Novak brought something irregular to his attention.
- d) Then the abstracts went to the clerk for his signature, as described above for the period of the late 1970s.
- e) The office acquired its first computer capability late in this period.

E. 1985-86 (the Jennings period)

1. The new majority leadership rejected the House Administration concept and the segregation of administrative/fiscal staff functions. They preferred to keep control of administrative matters in the leadership corner. They also thought that House Administration had been superimposed on House Finance and that the two offices were not well integrated and coordinated.
2. House Administration was abolished as an office, and Pederson was not rehired in January of 1985. Pederson's duties were divided between P Hess (the chief majority staffer) and C Shearer (who replaced Kienitz as the director of House Finance, now renamed the Office of Legislative Management).
3. Hess's title was "executive director, majority caucus" but he was also variously styled as the caucus chief of staff or staff director. Hess was promoted from within the IR caucus staff.
 - a) Hess had three primary responsibilities:
 - 1) Like Pederson, he oversaw general House internal finance, administration, and management functions. Shearer reported to Hess.
 - 2) Unlike Pederson, he was the majority caucus staff director.
 - 3) Unlike Pederson, he was a key majority caucus legislative strategist.
 - b) Unlike Pederson, Hess's office was in the leadership corner.
 - c) Other leadership staff reported to Hess. They worked mostly on legislative activity and also functioned as personal assistants to leadership.
 - d) The effect of this was to dissolve the segregation of duties between majority leadership staff and House administration that had been recommended by Stanton and partly established during the Pederson period.
4. Hess retained the Staff Director's Advisory Group as a device for senior management communication about administrative policy and procedure.
5. Shearer was director of the Office of Legislative Management, reporting to Hess.
 - a) Shearer had Kienitz's responsibilities, plus Pederson's budget responsibilities. Shearer had a partisan background and administrative experience, having been the head of a state agency in another state.
 - b) Some of the existing staff (generally those perceived to have political affiliations) were not rehired in January of 1985. In addition, one of the two key fiscal control staffers in the office voluntarily transferred to the chief clerk's office. The general result:
 - 1) The fiscal control staff who left (transferring to the chief clerk's office) had the job of reviewing expenditure documents and preparing expense (accounts payable and reimbursement) abstracts, and also had general House budget monitoring responsibilities. This person was not replaced; Shearer took over part of this job herself with the help of other staff.
 - 2) The other fiscal control staffer, for payroll and personnel, remained. This job began to focus more on payroll and benefits (which were growing increasingly complex), rather than personnel generally.

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- 3) Pederson's administrator for personnel was retained, reporting now to Shearer.
 - 4) The information systems (computer) administrator was retained, reporting now to Shearer. (However, in 1986, this job was redefined somewhat and changed hands.)
 - c) This was a time of budget cutting, and Shearer was heavily occupied with budget analysis and financial controls for Hess. Hess relied on her for detailed knowledge and review of House spending.
 - d) The office was audited by Stanton and various positions were upgraded in 1985. Stanton's structure envisioned the following created three administrative positions in the office (in addition to the supply and facilities manager): (1) fiscal services; (2) personnel; (3) information (computer) systems. This structure was never fully implemented with respect to fiscal services administration.
6. The review of abstracts continued much as before, except:
- a) Shearer evidently reviewed at least some abstracts in more detail than had been Kienitz's custom. Shearer did not review payroll abstracts. But some think she personally reviewed expense (accounts payable and reimbursement) abstracts and supporting documentation (which had been the job of the departed fiscal control staffer). This fiscal control activity would have been consistent with her management style and Hess's expectations. Others, however, think she was more occupied with state and House budget issues and did not personally review individual bills and invoices in any detail.
 - b) More expenditure records were being computerized, and the computer staff began to have a more important role in expenditure documentation.
 - 1) The computer staff developed monthly reports for majority leadership on expenditures and the budget.
 - 2) Documentation for expense (accounts payable and reimbursement) abstracts was improved by computerization. Before this time, documentation for expense abstracts consisted either of a simple list of checks with amounts and payees (a warrant report), or copies of all the actual bills and invoices. Now Hess began getting a detailed computer printout listing all of the invoices, bills, reimbursement requests, etc. for each abstract. For each item on the list, the printout displayed the name of the payee, a brief description of the cost (the description that appears on the check stub), and the dollar amount. If a single payment on the list contained several separate expenditure items, the separate items that make up the total for that payment were also listed. (For example, a member might receive one payment for various separate expenditures like parking, motel, phone, etc.)
 - c) The staff delivered the abstracts and supporting documentation to the leadership corner. Hess normally reviewed expense (not payroll) abstracts and the supporting computer printout and gave them to the speaker's secretary for the speaker's signature.
 - d) Evidently the speaker normally reviewed and signed expense (not payroll) abstracts personally, because Hess remembers getting calls from the speaker asking about specific expenditure items. Some staff remember delivering abstracts directly to the speaker for signature, but only when Hess was not available.
 - e) Stamping the chief clerk's signature became more common, in large part because the clerk was now in the Capitol whereas other House offices had moved to the SOB. The move made it more inconvenient and time-consuming to get to the clerk for a signature.
- F. From 1987 to the present
1. This period was the subject of my earlier report. The following summarizes new information and perspectives:

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2. The separate, House Administration office of the Pederson period was not revived. The administrative responsibilities of Pederson/Hess went to L Bothwell, whose title is "director of staff." Bothwell had worked for the caucus for years, most recently (1985-86) as minority caucus staff director.
 - a) Bothwell's office, like Hess's (and unlike Pederson's), is in the majority caucus leadership corner.
 - b) Like Hess's job, Bothwell's job combines that of House administrator (roughly Pederson's job) and staff director of the majority caucus (not Pederson's job).
 - c) But (unlike Hess, more like Pederson) Bothwell's job is more purely administrative: it does not include caucus legislative strategy.
3. The role of the Staff Directors Advisory Group diminished; and the group met less regularly than was the practice before 1987.
4. The Office of Legislative Management was renamed House Administrative Services.
 - a) Kienitz returned to replace Shearer. Kienitz reports to Bothwell, as Shearer did to Hess.
 - b) The personnel staffer and the remaining fiscal control staffer (for payroll and benefits) continued with much the same jobs as before.
 - c) Kienitz did not revive the fiscal control position for accounts payable and reimbursements. (This was a position in the old Kienitz office, before 1985, which had been eliminated by Shearer.) The responsibility for preparing accounts payable and reimbursement abstracts now is split between two other HAS staff, employed at lower responsibility levels and reporting directly to Kienitz.
 - d) The information systems administrator remained, and an assistant was added in 1987. Computerization gradually grew more important in fiscal record-keeping.
5. The preparation and review of expenditure documents and abstracts remained much as in 1985-86, except that:
 - a) Kienitz does not normally review expenditure abstracts and supporting documentation, except now for telephones. (Before 1985, Pederson required Kienitz's signature on abstracts, but since 1987 this has not been the practice.)
 - b) The speakers have not normally personally reviewed or signed abstracts. (Searle and Jennings are apparently the only speakers who have done this.)
 - c) The practice of stamping the clerk's signature became very common, though not universal. The clerk signed payroll abstracts regularly, but did not sign other kinds of abstracts regularly until very recently.

Billing Month	Credit Cards	House Phones (1)	WATS Lines	Date Paid	WATS	Phone Repairs (3)	MACs (2,3)	Monthly Total
Jan 1991	\$89.83	\$9,171.34	\$14,667.85	3/91				\$23,929.05
Feb	\$45.57	\$12,718.68	\$15,943.02	3/91		\$813.00	\$980.00	\$30,500.30
Mar	\$111.39	\$10,619.55	\$15,978.88	4/91		\$228.00	\$340.00	\$27,277.86
Apr	\$1.47	\$10,354.08	\$17,370.66	5/91		\$346.00	\$190.00	\$28,262.26
May	\$37.38	\$10,086.54	\$16,927.39	6/91			\$1,291.72	\$28,343.10
Jun	\$263.44	\$9,830.26	\$15,444.68	8/91				\$25,538.47
Jul	\$53.34	\$9,208.32	\$19,128.91	8/91				\$28,390.66
Aug	\$673.38	\$9,316.04	\$17,399.72	10/91				\$27,389.25
Sep	\$373.66	\$9,336.34	\$23,246.29	10/91			\$10,000.00	\$42,956.40
Oct	\$174.95	\$9,471.32	\$36,554.81	12/91				\$46,201.21
Nov	\$214.56	\$9,247.99	\$58,989.75	12/91				\$68,452.43
Dec	\$387.97	\$9,279.84	\$11,946.56	1/92		\$17,677.23		\$39,291.61
Total 1991	\$2,426.94	\$118,640.30	\$263,598.52			\$19,064.23	\$12,801.72	\$416,532.61
% To Total	0.583%	28.483%	63.284%			4.577%	3.073%	100.000%
Jan 1992	\$343.05	\$9,251.12	\$15,225.95	2/92				\$24,820.14
Feb	\$178.59	\$9,909.58	\$3,313.05	6/92		\$100.00		\$13,501.29
Mar	\$6.01	\$9,318.39	\$3,313.05	6/92		\$120.00		\$12,757.52
Apr	\$164.86	\$9,432.07	\$3,313.05	6/92				\$12,910.05
May	\$53.44	\$9,107.33	\$7,864.74	7/92				\$17,025.59
Jun	\$291.99	\$8,465.90	\$8,403.95	8/92				\$17,161.93
Jul	\$1,319.22	\$8,153.04	\$8,300.25	9/92				\$17,772.61
Aug	\$1,558.51	\$9,524.90	\$7,049.04	10/92		\$11,736.31		\$29,868.87
Sep	\$1,845.31	\$7,677.33	\$8,039.43	10/92				\$17,562.18
Oct	\$2,330.91	\$8,390.44	\$7,685.70	11/92				\$18,407.17
Nov	\$2,566.01	\$8,207.19	\$5,746.05	12/92				\$16,519.38
Dec	\$2,401.92	\$8,196.64	\$4,949.51	1/93				\$15,548.08
Total 1992	\$13,059.82	\$105,633.93	\$83,203.77			\$11,956.31	\$0.00	\$213,854.79
% To Total	6.107%	49.395%	38.907%			5.591%	0.000%	100.000%

Notes:

1. House Phones include base phones charges plus direct dialed long distance calls
2. MACs means Moves, Additions, and Changes
3. Billings were based on a negotiated contract with the House, payable when summarized statements were submitted



STATE OF MINNESOTA

OFFICE OF THE ATTORNEY GENERAL

HUBERT H. HUMPHREY III
ATTORNEY GENERAL

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ST. PAUL, MINNESOTA 55106
TELEPHONE: (612) 297-1050
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October 27, 1992

James R. Nobles
Legislative Auditor
Centennial Building
St. Paul, MN 55155

Dear Mr. Nobles:

By letter dated July 7, 1992, you referred to our office an audit report on a special review of unauthorized long distance telephone calls charged to the Department of Natural Resources Detroit Lakes office. We have reviewed the matter and, for the reasons stated below, have determined that no action to recover the funds is advisable.

The report concerns almost \$57,000 in unauthorized long distance telephone calls charged to the Department of Natural Resources Detroit Lakes office. Your office investigated and concluded that no State employees were responsible for the unauthorized calls. Rather, an unknown person in some unknown manner illegally obtained the access codes for the Detroit Lakes office long distance service. Your report does not recommend seeking recovery from any State employees.

The Department of Administration wants the Department of Natural Resources to pay the full bill for the calls. The Department of Natural Resources claims that the Department of Administration is at least partially at fault. Your report suggests that liability should be shared among the DNR, the Department of Administration, MCI and U. S. West.

Our review indicates that recovery from MCI or U. S. West is extremely unlikely. Our attorneys who work in the utilities area know of no cases that would support such a recovery. Phone companies have strong disclaimers in their tariffs, and in other circumstances courts have rigidly enforced the disclaimers because the tariffs are approved by regulating agencies. Based on this low potential for success, we do not believe it makes sense to pursue recovery against MCI or U. S. West.

Finally, we do not think we should get involved in the dispute between the Departments of Administration and Natural Resources. We see their dispute as essentially a budgeting/bookkeeping matter between two executive agencies that should be resolved at that level, without the expenditure of legal resources.

James R. Nobles
October 27, 1992
Page 2

Thank you for sending us the report. If you have any questions or concerns please contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard S. Slowes", with a long horizontal flourish extending to the right.

RICHARD S. SLOWES
Assistant Solicitor General

(612) 296-6473

cc: John R. Tunheim
slow:vx5

AN ACT

NOTE

This is the final version
of the bill that will be
transmitted to the governor's
desk. Check House Index Department
for updated status (35-6646)

1

2 relating to public administration; making telephone
3 records of public officials public data; providing
4 oversight for administrative expenses; regulating
5 administrative rulemaking procedures; amending
6 Minnesota Statutes 1992, sections 3.055, subdivision
7 1; 3.841; and 14.10; Laws 1989, chapter 335, article
8 1, section 15, subdivision 3; proposing coding for new
9 law in Minnesota Statutes, chapters 3; and 10.

10 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MINNESOTA:

11 Section 1. Minnesota Statutes 1992, section 3.055,
12 subdivision 1, is amended to read:

13 Subdivision 1. [MEETINGS TO BE OPEN.] Meetings of the
14 legislature shall be open to the public, including sessions of
15 the senate, sessions of the house of representatives, joint
16 sessions of the senate and the house of representatives, and
17 meetings of a standing committee, committee division,
18 subcommittee, conference committee, or legislative commission,
19 but not including a caucus of the members of any of those bodies
20 from the same house and political party nor a delegation of
21 legislators representing a geographic area or political
22 subdivision. For purposes of this section, a meeting occurs
23 when a quorum is present and action is taken regarding a matter
24 within the jurisdiction of the body. Each house shall provide
25 by rule for posting notices of meetings, recording proceedings,
26 and making the recordings and votes available to the public.

27 Sec. 2. Minnesota Statutes 1992, section 3.841, is amended

1 to read:

2 3.841 [LEGISLATIVE COMMISSION TO REVIEW ADMINISTRATIVE
3 RULES; COMPOSITION; MEETINGS.]

4 A legislative commission for to review of administrative
5 rules, consisting of five senators appointed by the committee on
6 committees of the senate and five representatives appointed by
7 the speaker of the house of representatives shall be appointed.
8 Its members must include the chair or vice-chair of the
9 committees in each body having jurisdiction over administrative
10 rules. The commission shall meet at the call of its chair or
11 upon a call signed by two of its members or signed by five
12 members of the legislature. The office of chair of the
13 legislative commission shall alternate between the two houses of
14 the legislature every two years.

15 Sec. 3. [3.984] [RULE NOTES.]

16 Subdivision 1. [REQUIREMENT.] The head or chief
17 administrative officer of an agency, as defined in section
18 14.02, subdivision 2, shall prepare a note containing the
19 information required by subdivision 2 on every bill containing a
20 grant of rulemaking authority to that agency. The chair of a
21 standing committee receiving a bill on rereferral from another
22 standing committee shall request that: (1) the rule note be
23 amended to reflect any amendment of the grant of rulemaking
24 authority made to the bill; or (2) a rule note be prepared by
25 the agency if a grant of rulemaking authority has been added to
26 the bill.

27 Subd. 2. [CONTENTS.] The note required by subdivision 1
28 must treat separately each grant of rulemaking authority
29 contained in the bill and must include a detailed explanation of:

30 (1) the reasons for the grant of rulemaking authority;

31 (2) the persons or groups the rules would impact;

32 (3) the estimated cost of the rule for the persons or
33 groups specified pursuant to clause (2); and

34 (4) the areas of controversy anticipated by the agency.

35 The note must be delivered to the chair of the standing
36 committee to which the bill has been referred or rereferred, the

1 chair of the legislative commission to review administrative
2 rules, and the chairs of the committees in each body having
3 jurisdiction over administrative rules.

4 Subd. 3. [ADMINISTRATION.] The commissioner of finance is
5 responsible for coordinating this process, for assuring the
6 accuracy and completeness of the note, and for assuring that
7 rule notes are prepared, delivered, and updated as provided by
8 this section.

9 The commissioner shall prescribe a uniform procedure to
10 govern agencies in complying with this section.

11 Sec. 4. [10.43] [TELEPHONE USE; APPROVAL.]

12 Each representative, senator, constitutional officer,
13 judge, and head of a state department or agency shall sign the
14 person's monthly long-distance telephone bills paid by the state
15 as evidence of the person's approval of each bill.

16 Sec. 5. [10.44] [LEGISLATURE AND OTHER OFFICIALS;
17 BUDGETS.]

18 The budgets of the house of representatives, senate,
19 constitutional officers, district courts, court of appeals, and
20 supreme court must be submitted to and considered by the
21 appropriate committees of the legislature in the same manner as
22 the budgets of executive agencies.

23 Sec. 6. [10.45] [BUDGETS; INFORMATION.]

24 The budgets of the house of representatives, the senate,
25 each constitutional officer, the district courts, court of
26 appeals, and supreme court shall be public information and shall
27 be divided into expense categories. The categories shall
28 include, among others, travel and telephone expenses.

29 Sec. 7. [10.46] [TELEPHONE RECORDS PUBLIC.]

30 Long-distance telephone bills paid for by the state or a
31 political subdivision, including those of representatives,
32 senators, judges, constitutional officers, heads of departments
33 and agencies, local officials, and employees thereof, are public
34 data.

35 Sec. 8. [10.47] [TELEPHONE SERVICE; OVERSIGHT.]

36 Each member, officer, or employee in the legislative,

1 judicial, and executive branches shall report any evidence of
2 misuse of long-distance telephone service to the chief officer
3 of the legislative body, judicial branch, executive office, or
4 executive agency, and to the legislative auditor when
5 appropriate. The legislative auditor shall investigate and
6 report on evidence of misuse of long-distance telephone service
7 of legislators, judges, constitutional officers, heads of
8 executive departments and agencies, and state employees and,
9 where appropriate, refer the evidence to other authorities.

10 Sec. 9. [10.48] [EXPENSE REPORTS.]

11 The house of representatives and senate shall by rule
12 require detailed quarterly reports of expenditures by the house
13 of representatives and senate to their respective committees on
14 rules and legislative administration. Each constitutional
15 officer, the district courts, court of appeals, and supreme
16 court shall submit detailed quarterly reports of their
17 expenditures to the legislative auditor. These reports are
18 public information.

19 Sec. 10. Minnesota Statutes 1992, section 14.10, is
20 amended to read:

21 14.10 [SOLICITATION OF OUTSIDE INFORMATION.]

22 When an agency seeks to obtain information or opinions in
23 preparing to propose the adoption, amendment, suspension, or
24 repeal of a rule from sources outside of the agency, the agency
25 shall publish notice of its action in the State Register, mail
26 this notice to persons who have registered their names pursuant
27 to section 14.14, subdivision 1a, 14.22, or 14.30, and shall
28 afford all interested persons an opportunity to submit data or
29 views on the subject of concern in writing or orally. Such
30 notice and any written material received by the agency shall
31 become a part of the rulemaking record to be submitted to
32 the attorney-general or administrative law judge under section
33 14.14, 14.26, or 14.32. This notice must contain a summary of
34 issues that may be considered by the agency when the rule is
35 proposed, a statement of the agency's intentions regarding the
36 formation of an advisory task force on the subject, and, if a

1 task force is to be formed, a list of the persons or
 2 associations the agency intends to invite to serve on the task
 3 force. The notice must also include a proposed timetable
 4 outlining when the agency intends to form the advisory task
 5 force, when it could be expected to complete its work, and how
 6 long the agency anticipates the rulemaking process taking.

7 Sec. 11. Laws 1989, chapter 335, article 1, section 15,
 8 subdivision 3, is amended to read:

9 Subd. 3. Information Management

10 \$ 5,836,000 \$ 5,759,000

11 Summary by Fund

12 General \$ 1,678,000 \$ 1,601,000

13 Special Revenue \$ 4,158,000 \$ 4,158,000

14 The appropriation from the special
 15 revenue fund is for recurring costs of
 16 911 emergency telephone service.

17 \$201,100 the first year and \$205,800
 18 the second year must be subtracted from
 19 the amount that would otherwise be
 20 payable to local government aid under
 21 Minnesota Statutes, chapter 477A, in
 22 order to fund the local government
 23 records program and the
 24 intergovernmental information systems
 25 activity.

26 \$1,000,000 in contributed capital is
 27 transferred from the computer services
 28 fund to the telecommunications fund.

29 The commissioner shall study the
 30 feasibility of contracting for disaster
 31 recovery services from nonstate sources.

32 ~~Notwithstanding any law to the~~
 33 ~~contrary, legislators' telephone~~
 34 ~~records are private data.~~

35 Sec. 12. [LCRAR RULEMAKING REPORT.]

36 No later than February 15, 1994, the legislative commission
 37 to review administrative rules shall submit a report including
 38 its recommendations to the governmental operations and gaming
 39 committee of the house of representatives and the governmental
 40 operations and reform committee of the senate on the following
 41 topics:

42 (1) a list of all delegations of rulemaking authority to
 43 state agencies that indicates which of those are grants of
 44 general rulemaking authority and which are narrowly drawn,

1 specific authorizations;

2 (2) the use made of broad delegations of rulemaking
3 authority, the purpose served by this use, and the relationship
4 of broad delegations with other delegations of authority in the
5 promulgation of rules;

6 (3) an evaluation of the continued need for these
7 delegations of general rulemaking authority;

8 (4) an evaluation of the continued need for delegations of
9 rulemaking authority to quasi-independent boards or commissions;

10 (5) recommendations for establishing statutory criteria to
11 be used in preparing rule impact statements including those in
12 Minnesota Statutes, sections 14.11 and 14.115, for agricultural
13 land, small businesses, and local governments or the removal of
14 requirements for these impact statements;

15 (6) recommendations for development of more complete
16 information on the economic and other impacts of proposed rules
17 on directly affected parties and on agencies required to enforce
18 the rules, how to determine when these impacts are significant
19 enough to require greater efforts at assessing impacts, on ways
20 this information might be obtained from affected parties and
21 developed by agencies, whether this information should be
22 included in the statement of need and reasonableness, and how
23 the information might be distributed before the proposed rule is
24 published;

25 (7) criteria to be used by legislative committees for the
26 granting of exemptions to the rulemaking requirements of
27 Minnesota Statutes, chapter 14;

28 (8) recommendations on which fees should be set or changed
29 by rule or statute; and

30 (9) methods to improve the coordination of rulemaking in
31 the executive branch.

32 Sec. 13. [INVESTIGATION OF RECORDS.]

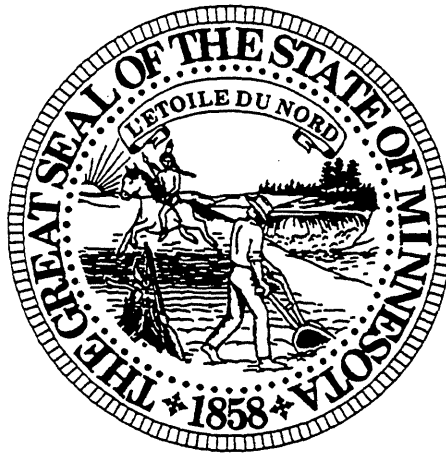
33 Legislators' long distance telephone records as to bills
34 paid by the state, including WATS service, for 1991, 1992, and
35 1993 shall be provided upon request made in accordance with
36 Minnesota Statutes, section 8.16 or 388.23, to the attorney

1 general or county attorney with jurisdiction, or to the United
2 States attorney under the procedures of the appropriate federal
3 rules, to the extent necessary to complete any investigation.
4 Failure to comply with a request without just cause subjects the
5 person who fails to comply to contempt of court.

6 Sec. 14. [EFFECTIVE DATE.]

7 This act is effective the day following final enactment,
8 except that section 12 is effective July 1, 1993; sections 4 and
9 9 are effective October 1, 1993; sections 3 and 10 are effective
10 January 1, 1994; and section 2 is effective January 1, 1995.

**ATTORNEY GENERAL'S REPORT
ON THE
UNAUTHORIZED USE OF REP. ALAN WELLE'S
STATE TELEPHONE ACCESS CODE**



**State of Minnesota
Office of the Attorney General
Hubert H. Humphrey III**

June 7, 1993

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ANALYSIS AND RECOMMENDATIONS

- 1. The Legislature's business affairs should be subject to the same internal controls and monitoring as other state agencies.**

Virtually all of the toll fraud in this instance would have been avoided had anyone been minding the store, or if the current House system for monitoring phone bills had been in place. While the House had accepted the Department of Administration's recommendation that members have individual personal identification numbers and separate billings, House Administration dropped the ball by not doing anything meaningful with the information, while the House's insistence on keeping its records confidential made it impossible for the Department of Administration to help. House leadership deserves credit for moving swiftly, in the wake of the November 1991 incident, to impose individual accountability through a telephone credit card reimbursement system, but additional reforms are necessary:

- a. Precise written policies defining authorized use of the phones should be developed and enforced.**

The policy should clearly identify the authorized users and what constitutes authorized use. House and Senate managers must take care that all members and staff are regularly instructed in the policy and must resist pressure for free phone use from lobbyists and other unauthorized users. The failure to maintain such a policy, the ambiguity about the identity of authorized users, and House Administration's disregard of the State operators' warnings of abuse, all contributed to the toll fraud in this incident.

- b. The Legislature should establish broader rules about member conflicts of interest, to ensure that members do not participate in decisions which may affect their own personal interest.**

At the time Rep. Welle participated in the decision about whether to pay the phone bill, he was in a position to affect that decision not as a member but as the incoming chair of the House Rules and Administration Committee, which has jurisdiction over House business affairs. While Welle did not invoke his power as Majority Leader and Rules Committee

Chair, Kienitz was aware that the decision involved not only Rep. Welle, a member, but Rep. Welle, Kienitz's boss.

Welle should have been sensitive to this potential conflict and removed himself from any decision making. Whether Welle thought he might be liable for any of the bill is ultimately irrelevant--as the member whose account was affected, his participation in the handling of this matter creates what in retrospect is an obvious conflict and an appearance of impropriety. Under current law, House members are only required to disqualify themselves from voting on matters in which they have personal, financial interests. Minn. Stat. § 10A.07. The Legislature needs a broader rule which requires members and staff to disqualify themselves from other kinds of decision making which may affect their personal, business or family interests.

c. The Legislature should increase member accountability for phone use by consolidating phone billings.

Despite adopting the individual phone credit card system which made members accountable for their INWATS use, it is still difficult to know the total extent of member long distance usage. Under the current system, members only see bills for their credit card calls, not for calls they and their staffs make from State phones, or which are transferred to long distance numbers through House phones. All member and staff bills should be reviewed and the bills should be consolidated. The fragmented billing system makes it impossible to get a complete picture of members' long distance usage.

d. The Legislature should adopt a records retention policy with respect to all its management and fiscal records.

In the past, House phone records were routinely shredded after processing. Unlike other State departments and branches of government, the House had no reasoned, management-based records retention policy. Although other aspects of House business were outside the scope of this investigation and report, if other House administrative and fiscal affairs are not subject to written record retention policies, the House leadership should look into this issue and develop a records retention policy accordingly.

- e. **The House and Senate must open themselves to constructive criticism and suggestions from other branches of government.**

One of the most intangible but important contributors to the State's loss in the Welle incident is the Department of Administration's lack of assertiveness over the phone bill. The lack of assertiveness springs from what Commissioner Badgerow has aptly described as the "culture of deference" to the Legislature. As a newcomer to State government in late 1991, she succumbed to the practice of too many executive branch managers: Don't challenge the Legislature. The Department of Administration's acquiescence in the House's instructions to tolerate obvious misuse of the INWATS system, and the Department's decision to pay the House's long-distance bills, graphically illustrate how this deference, based in fear of retaliation through reduced appropriations, contributes to the making of bad decisions by State managers. Such symptoms will not disappear until the Legislature stops setting itself apart as an untouchable entity unto itself and becomes instead a member of a team which wins when it best serves good government and the people of Minnesota.

- 2. **The Department of Administration must review the way it buys telecommunications services, adopt a more aggressive posture toward the phone companies in its administration of long distance contracts, and increase efforts against toll fraud.**

Two striking things about the handling of this matter are the extent to which MCI and US WEST stack the deck against their own customers, and the way the critical Department and Legislative personnel failed to challenge the companies. The Welle and DNR incidents raise serious questions about the State contracts and how the State buys telecommunications services; and while the Department acted quickly in November 1991 to mitigate the harm from phone fraud, more resources should have been directed towards prevention. Specifically:

- a. **The Department should restructure State phone contracts to ensure phone company accountability.**

The structure of the telecommunications contracts left no carrier fully accountable for operations. MCI had long distance, US WEST had local service and long distance switching, yet neither was made accountable for security services. Instead, the phone companies made

the same profit on fraudulent calls as on authorized calls, and both disclaim legal or ethical responsibility for customer losses they could have prevented.

- b. The Department should demand additional security services from long distance carriers.**

Long distance carriers have the technology to monitor such details of phone usage as incidence of calls through a given personal identification number. There is no evidence that the telephone companies offered such security services, nor that the Legislature requested any such assistance. Had such monitoring been in place in 1991, both the DNR and legislative toll fraud would still have happened, but would probably have cost the State a fraction of what they ultimately did. Toll fraud cannot completely be eliminated, but contracting for additional security monitoring services from the long distance carriers seems likely to pay for itself through fraud avoidance alone.

- c. Network Services should keep legislative phone records on the same basis as those of other branches of government.**

This recommendation is consistent with putting the Legislature on the same footing as other branches of government. In addition, the Department should study the feasibility of getting and keeping point-of-origin call detail on a regular basis, and should do so if it appears to be cost effective.

- d. The Department should redouble its internal security efforts which should include mandatory instruction in telephone security and toll fraud avoidance for state agencies.**

The Department has taken steps in this regard in the past, but in light of events it is clear that those efforts need to be stepped up. The additional internal security should include regular monitoring by all State departments and branches of government.

- e. The Department must be more aggressive in administering its long distance contracts.**

The Department in this case gave the appearance of having deferred not only to the House of Representatives, but to the phone companies. For a State agency to pay a bill such as those arising out of the 1991 toll fraud incidents without even consulting its attorneys is

unacceptable. The fact that a key Department of Administration official is a former US WEST employee may have contributed to the Department's passivity toward US WEST and MCI.

3. **All state agencies which have been the victims of fraud, or are involved in substantial contract issues, should seek legal advice from their counsel in the Attorney General's office.**

While the Attorney General's most visible role is as a law enforcer in the consumer protection, antitrust and criminal areas, and as a public policymaker, the majority of attorneys in the Attorney General's office function as attorneys for the State. They serve the people of Minnesota by advising agencies in just such matters. However, at no stage of either the legislative or DNR INWATS toll fraud matters was the Attorney General's Office even informed of events, let alone consulted to protect the State's rights.

4. **The phone companies should be required to share the cost of long distance fraud with their customers.**

Companies like US WEST and MCI can shift the entire cost of phone fraud to their customers, as they did in this case, because the current legal and regulatory system permits them to do so. One glaring example of the way the playing field tilts toward the phone companies is the exemption of phone company credit cards from statutes limiting consumer liability for unauthorized use.

The Federal Truth and Lending Act, 12 U.S.C. § 1601, et. seq., and parallel State law, Minn. Stat. §§ 325G.02-05, allocate the risk of unauthorized use between consumers and card issuers. Both laws limit consumer liability for unauthorized use of financial transaction cards, or lost or stolen cards. See Minn. Stat. §§ 325G.03-.04 (1992). However, telephone company credit cards are specifically exempt from the State law limiting consumer liability. Minn. Stat. § 325G.02, subd. 2 (1992).

We see no persuasive policy or other reason why telephone companies should be treated any differently than other card issuers. While it can be argued that the rate payers of regulated local service companies should not be required to bear the cost of fraud, there is no such argument for less regulated long distance carriers. Phone companies are in a much better

position than consumers to detect and prevent many kinds of fraudulent use, and to mitigate the harm. They do not do so because they have no incentive. Indeed, the phone companies claim as much profit from fraudulent calls as from legitimate ones.

In this case, US WEST and MCI were in a position to detect the toll fraud long before the system shut down on November 14. The Department of Administration is at fault for not "buying smart." US WEST and MCI are at fault for not more aggressively implementing fraud control and detection systems to protect their customers and the integrity of the telecommunications system. Finally, the legislative and regulatory system is at fault for permitting special phone company exemptions which let the industry profit from fraud it could prevent. The Attorney General will strongly pursue a change to Minn. Stat. § 325G.02 in the next legislative session. As this incident clearly demonstrates, such a change is long overdue.

INTRODUCTION AND SCOPE OF THE REPORT

On March 17, 1993, the news media reported that \$50,000 of unauthorized long distance telephone charges were charged to the account of House Majority Leader Alan Welle during the fall of 1991. In response to the reports, on March 18, 1993 the Speaker of the House wrote to Attorney General Humphrey asking him to investigate the House's handling of the incident. In a separate letter, also dated March 18, the House Minority Leaders requested an investigation by both Attorney General Humphrey and United States Attorney Thomas Heffelfinger. The respective letters are Appendices 1 and 2 to this memorandum.

The purpose of the Attorney General's investigation was to discover any misconduct by State employees or officials in the origin of the unauthorized calls or the subsequent handling of the matter. This report sets out the facts found by the investigating team. Inevitably, there is conflicting evidence on many points, some important, some not. This report does not attempt to list all inconsistent statements, or reconcile every detail, but rather to tell what happened and cite the essential supporting evidence.

Finally, this report does not analyze the many and complex criminal and civil liability issues which arise out of this matter, or discuss specific strategies for recovering money. Doing so might jeopardize future legal actions. The report does, however, analyze events and offer strong recommendations to change State telecommunications policy and management systems.

DISCOVERY OF THE UNAUTHORIZED USE

The Phone System Overloads; Administration Pulls the Plug and Tells the House

On November 13, 1991, the Department of Administration's Telecommunications Network Services Group began to receive complaints of busy signals on the State's assigned WATS lines. Network Manager Bonnie Plummer began an investigation to find out why the system was overloaded. Appendix 3, a three-page outline prepared by Telecommunications Director Kathi Lynch and dated November 22, 1991, sets out the daily chronology of her

department's investigation, beginning with complaints of busy lines in the afternoon of Wednesday, November 13. Lynch prepared the outline for a briefing of Commissioner of Administration Dana Badgerow and Asst. Commissioner Bernie Conlin. The outline deals with an earlier incident of toll fraud committed against the Department of Natural Resources (DNR) in September and October, 1991, and the "legislative INWATS" fraud. The chronology of Network Services' legislative INWATS investigation, excerpted from Lynch's outline, is as follows:

- * 11/13 p.m. Complaints of busy lines
- * 11/14 p.m. Confirmation on busy lines of "non-state" calling
- * * *
- * 11/18 - LEGISLATIVE INWATS 7-LINE RAU [remote access unit] "down."
- * * *
- * 11/20 - Complaints of "busy" Discovery of source of probable fraud
- * 11/20 pm By our request, LEGISLATIVE INWATS shut down, route calls to standard recording
- * 11/21 - House and Senate offices notified
- Legislators calling in on LEGIS "HELP" line - told of probable fraud problem
- * 11/21 - LEGIS INWATS 1-800 # change
- "IRS" collect info from callers
- House (ofc mgr) identifies possible "source" ID of abuse. (Help from "owner" of code to review bills and place start of abuse as March '91.)

The outline reflects that Network Services acted promptly to reduce the toll fraud on November 15, by restricting access to Minnesota-originated calls, and cut it off altogether on November 20, by shutting off the legislative INWATS lines. In addition, Plummer wrote a general memorandum to State agency managers on November 14, 1991 warning them about potential toll fraud and suggesting preventive measures. See Appendix 4.

The Lynch outline establishes the date on which Bonnie Plummer of Network Services first told the House of the problem: she called House Administrative Services Director David Kienitz on November 21, 1991, the morning after Network Services shut down the legislative INWATS service and began routing legislative calls through the general State lines. (Appendix 13 at 2.) In their initial interviews, both Kienitz and Plummer stated that Plummer alerted Kienitz on November 14, based on Plummer's assumption that she called Kienitz the day the overload was discovered. Plummer has since deferred to Lynch's contemporaneous outline and chronology. Moreover, the November 14 date is inconsistent with Plummer's recollection that it took some time to isolate the legislative INWATS system as the source of the overload (although she says she suspected the House right away).

November 21 was also the day Kienitz wrote a memo to all House members, telling them that because of "some problems with the legislative WATS card calling system" the access numbers had been changed. See Appendix 5. The Kienitz memo corroborates the Lynch outline on this important question of when the House first learned of the fraud: Someone in his position would logically want to notify his "customers" about problems and service changes as soon as he learned about them.

Welle Learns About The Toll Fraud From Kienitz And From His Son And Nephew

When Plummer called Kienitz on November 21, 1991 and said "We've got a problem," she knew the source was a House member, but not which one. Kienitz soon found out, though, by consulting his hard copy records for the most recent available month--September--and identifying Welle's as the problem access code. Kienitz that same day contacted Welle, although whether he called Welle directly or communicated through Scott Croonquist no one is now sure.

It is also unclear whether Welle was in St. Paul or Willmar when he first learned about the problem. Whether Welle was in St. Paul or Willmar, however, it was probably that same night when he discovered that his son, BW, was the source of the problem. While he does not remember the date, Welle recalls talking to his wife about the toll fraud connected with his

access number and seeing a stricken expression on his son's face. When Welle asked his son if he knew anything about the matter, BW admitted that he had used the number himself, and had given it to his cousin MH and two junior high school friends in Willmar.

Welle's nephew, MH, provides the clearest evidence fixing November 21 as the date Welle learned how the number got out. MH associated the discovery with his cousin's confirmation. He remembered speaking to BW on the telephone about his own family's plans to visit Willmar for the confirmation, which he recalled was in late November, "probably before Thanksgiving." MH said he recalled the phone conversation taking place on a Thursday because he was trying to arrange to get to Willmar early for a long weekend with the Welles.

After a conversation between the cousins, BW said "Hang on, my dad wants to talk to you." Welle then came on the line and asked whether MH had obtained his WATS number--MH replied that he had--and whether he had given it to anyone else--which MH again answered in the affirmative. Welle reportedly said that some people had talked to him about a problem with the unauthorized use. That weekend, in Willmar, the topic came up again, and MH recalls his uncle saying that if the story came out it could "cost him his position."

As noted above, Welle himself has said he does not recall the date--and indeed originally believed the discovery came a month or more later. However, after hearing about his nephew's recollection of events, and after talking to his wife and son, Welle agreed that BW's involvement may have come to light around the time of BW's November 24, 1991 confirmation. BW was less certain, stating that MH also visited Willmar in December, possibly early in Christmas break, and suggested that MH may have confused the two visits.

It seems natural that, having learned that day from Kienitz that his access number had been used to commit thousands of dollars of toll fraud, Welle would have raised the topic with his family on November 21. This logic strongly suggests that MH's recollection of the timing of the phone call with his cousin and uncle was correct.

Welle apparently did not tell anyone outside his family that he knew of BW's and MH's involvement until some months later. Welle thought he told Croonquist soon after he learned of his family's involvement, but Croonquist believes he learned in February of 1992. Croonquist, Welle's chief aide and confidant since the fall of 1989, says he had no idea during the time House staff was deciding what to do with the bill that Welle's son was the source of the leak. Bothwell recalls someone asking Welle, during the 1991 investigation, whether Welle had given the number to anyone else, and being told that Welle gave it to his wife to call him on legislative business--a common and authorized use of the House lines.

Welle also told Sen. Dean Johnson that he had had a problem with his phone, and believed that he had also told Johnson about BW and MH. Johnson, however, has stated publicly and repeated to us that while Welle told him about the problem generally, he did not mention the involvement of his son and nephew. Welle does not challenge Johnson's statement.

NETWORK SERVICES' INVESTIGATION AND THE DECISION TO PAY THE BILL

The Internal Investigation And Welle's Failure To Disclose The Source Of The Fraud

On November 21, with the damaged controlled, Plummer asked Kienitz for Welle's billing "detail" and Kienitz relayed the request to Welle, who authorized their release. In late November, Welle reviewed the September House billing records to try to determine which calls were authorized. He sat for a time in Kienitz' office and wrote names next to numbers he recognized on the first several pages of the September bill. The vast majority of the September calls, however, were not his, and he quickly realized the size and difficulty of the task.

For reasons that are now unclear (but may be because Welle recalled a warning about the size of his phone bill), it was speculated that the unauthorized use went back as far as March 1991, and, as a result, Kienitz gave Plummer the March and September records to review.

Despite a Thanksgiving weekend spent reviewing phone records, Plummer's attempt to trace the source of the fraud hit a dead end in college dorm rooms and Willmar pay phones. Without the source, hopes for recovering money and identifying possible targets of prosecution began to dim.

At no point during the investigation of the toll fraud, or while the decision to pay the bill was pending, did Welle disclose that he knew the source of the fraud. Given the phone companies' intervening destruction of call origin records, and the inevitable loss of other evidence through fading memories, this omission has made it practically impossible for the Attorney General's office to trace the progress of the fraud. Welle's failure to disclose his knowledge of the fraud is arguably the most serious aspect of this entire matter.

One piece of evidence suggests that Welle may have taken an affirmative step to hinder the investigation. According to Plummer, Kienitz asked her not to follow one investigative lead. Working with the now-destroyed call origin records, Plummer saw a call which she believed to be from a Willmar residence. Rather than call the number, however, Plummer consulted with Kienitz. Kienitz reported back the member's request that she not call the Willmar number, and the member's statement that his card had been lost. (Appendix 6) In the same conversation, according to Plummer, Kienitz also refused her suggestion that the matter be turned over to law enforcement, saying that the House preferred not to pursue the matter.

In his testimony to the House Special Committee, Kienitz essentially confirmed Plummer's account of this conversation. He said that he would not have made a decision not to investigate a lead on his own, but that he cannot remember whom he consulted. Welle, the person Kienitz would logically have consulted, has denied that he told Kienitz not to pursue any investigative lead.

The Decision To Pay The Bill; Welle's Conflict Of Interest

With the internal investigation seemingly stalled, those involved were left with the question of what to do with the phone bill. Plummer knew from her experience as a US WEST employee, and from the DNR incident, that most long distance contracts, and the concomitant PUC-approved tariffs, placed the risk of fraudulent use on the customer. However, neither she nor anyone else consulted an attorney about either toll fraud incident.

Recollections and perceptions differ so much about who decided to pay the bill, and how that decision was arrived at, that it is difficult to assign responsibility. That difficulty is compounded by confusion about roles. When Kienitz turned to Welle on November 21, 1991, he saw Welle as not only the member whose access code had apparently been stolen, but also as the Majority Leader-Elect and, by virtue of that position, Chair of the House Rules and Administration Committee. The Majority Leader is the member responsible for House policies and administration and, aside from the Speaker, Kienitz's ultimate employer.

Welle's new position, and Long's elevation to Speaker, came about because the incumbent Speaker, Robert Vanasek, had resigned his leadership position. By December 1991, he had stopped functioning as Speaker, but because the next Legislature was not in session, there had been no formal transition of power. Thus, while Kienitz may have reasonably viewed Welle as his new boss, the lines of authority and responsibility were unclear. Welle had not formally assumed his leadership position. He still saw himself as the Chair of the Health and Human Services Committee, and Dee Long as the Majority Leader and House Rules Chair. Welle says he was working into the Majority Leader job, but had not assumed it either in form or substance; the Rules Committee did not meet at all between the 1991 and 1992 sessions, and he had taken no action as the person responsible for House Administration. He says he therefore failed to recognize the conflict of interest inherent in his dual role as the person with de facto power to decide on behalf of the House, and the person who might benefit individually from the decision. According to Welle and Croonquist, it did not occur to either of them at the time that Welle had a conflict.

Kienitz and Plummer Meet With MCI

Whoever had the ultimate authority, it was Kienitz and Plummer who handled the actual groundwork for making the decision. As the people most closely involved, they brought MCI into the picture. On December 12, 1991, they met with MCI Fraud Investigators Tom Schutz from Chicago, John Henderson of Minnesota, and Lance Springer of Des Moines. Over lunch at Chi Chi's, Schutz and Springer said that this fraud episode appeared not to be a professional job. They contrasted the pattern of calls with that displayed in the Department of Natural Resources toll fraud incident which began over Labor Day weekend, approximately three months before.

In the DNR case, a huge volume of calls began quite suddenly on September 1, 1991, leading to the conclusion that the fraudulent use was orchestrated by a professional who sold the access code. Investigators in the DNR case eventually concluded that the number was stolen from the Detroit Lakes DNR office and disseminated to California, where it was sold to potential users. The Secret Service was called in, but the investigation hit a dead end. Because the Department believed that the long distance tariff made the customers responsible for fraudulent charges, the Department of Administration ultimately decided to pay the \$56,692 in unauthorized charges to the DNR access code. A summary of the Legislative Auditor's July 10, 1992 report on the DNR incident is attached as Appendix 7.

In the legislative case, the phone calls increased relatively slowly over time until exploding in October 1991. See Appendix 8.

While there have been conflicting accounts of the Chi Chi's meeting, the thrust of what happened appears to be as follows: Kienitz reportedly asked the MCI investigators their opinion about the chances of prosecuting anyone, or of getting the money back. They responded that the chances were "slim and none," but offered to continue their investigation if the State wanted them to. Kienitz and Plummer both report that they believed MCI had done a significant investigation on its own, although MCI has since denied doing so. Based on the "slim and none" assessment, Kienitz and Plummer declined the offer of help, both

rationalizing--with Kienitz probably taking the lead in the decision--that further investigation would be pointless. Kienitz also asked whether the State had to pay the phone bill, and the MCI people responded that the State did. Neither Kienitz nor Plummer challenged MCI's assertion.

The five also speculated about how the access code got out. The MCI investigators told a number of stories about how professional criminals get personal numbers by recording touch tones, looking over people's shoulders at pay phones ("shoulder surfing"), or using computers to attempt calls by systematically varying access codes until they find one that works. The MCI evaluation that they were not dealing with a professional thief jibed with Plummer's analysis of selected phone records, which showed a pattern of local calls originating from pay phones at Willmar Community College, and from a gas station near Willmar. One guess, which Kienitz says Welle knew of but did not challenge, was that one of Welle's students at the school in Willmar somehow obtained the number.

The decision to pay the MCI bill proceeded on two tracks after the Chi Chi's meeting. Kienitz returned to Welle and, he says, in a series of conversations reported that MCI's assessment was that there was no meaningful chance to prosecute anyone or to recover any money, and that the State was liable for the bill. Based on that assessment--that the State was stuck and there was nothing anyone could do about it--Welle, Croonquist, and Kienitz report reaching a consensus that the House should pay its phone bill to the Department of Administration. Kienitz informed Bothwell, who had held up payment of the October bill, but who now reluctantly included the October and November charges in the House's December 27, 1991 abstract. (Appendix 9)

By House custom and usage the abstract was signed by the House clerk in the name of then-Speaker Robert Vanasek. However, the decision not to challenge the bill was effectively made by Welle and Kienitz. No other members participated in the decision, including Vanasek or Long. Long knew from Bothwell that there had been a significant toll fraud and that an investigation was under way but did not learn that the stolen PIN number was Welle's

until a month or two after the discovery. She did not know that Welle's son or nephew were involved until after the matter became public on March 17, 1993.

The Department Of Administration Declines To Challenge The Phone Bill

The Department of Administration began its own internal review when Kienitz called Plummer a day or two after the December 12 Chi Chi's meeting and told her that the House would pay the bill. Kienitz also asked her not to give the numbers which would identify the member in question to Plummer's Commissioner.¹ As the December 27, 1991 abstract reflects, the House pays its bill to the Department of Administration, and that Department contracts with and is ultimately responsible for dealings with the telecommunications vendors. (Appendix 9) As a matter of contract and of telecommunications policy, the nature of the phone system to begin with, and the ultimate decision to pay any phone bill, resides in the Commissioner of Administration.

Plummer told her superior, Kathi Lynch, about the MCI meeting, and that MCI would do whatever further investigation the company could. Lynch had briefed her bosses, Assistant Commissioner Bernard Conlin, and Commissioner Dana Badgerow on November 22, 1991, and despite what Lynch described as the staff's preference to be active in such matters, Commissioner Badgerow decided to defer to the House's decision not to pursue the matter. Badgerow says she did not know the identity of the member in question. Badgerow also says that she briefed the Governor's Deputy Chief of Staff, Patsy Randell, on the DNR toll fraud incident.

At no point during the decision making in this, or the earlier DNR incident, did anyone in the Department of Administration consult the Attorney General's Office. Although Plummer refers to general advice from our Office that such tariffs are enforceable, we have counseled the Department not to pay extraordinary bills such as the September through

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1. Plummer claims that while she had the number, Kienitz never revealed the identity of the member, telling her only it was someone "in leadership." Plummer also knew, from her analysis of the phone records, that the problem originated in the Willmar area, but said she never tried to figure out who it was.

November House bills, but rather to negotiate, if for no other reason than because paying the bill dramatically weakens the negotiating position. The Department of Administration, in the fact summary submitted to the Special Committee on House Management Practices, and the Special Committee's Report, also refer to a letter from Assistant Solicitor General Rick Slows to the State Auditor. The letter, which refers to the apparent enforceability of the contracts with regard to the DNR toll fraud incident, was written in October 1992, long after the decision to pay the DNR and House toll fraud bills.

The Department of Administration's failure to challenge the phone companies may have been influenced by Plummer's sympathies toward US WEST, her former employer. As a US WEST employee, Plummer oversaw the distribution of access codes to the State. In an interview with an Attorney General investigator, she characterized the State's liability for phone fraud as "too obvious to mention."

At no point during the decision making did anyone in the House consult an attorney, including House counsel Joel Michael, who, despite hearing some rumors of a problem phone bill, did not know specifics until the story began to break in March 1993.

At no time after the discovery of the toll fraud on November 14, 1991 did anyone involved report the matter to a law enforcement agency.

THE SOURCE OF THE TOLL FRAUD **AND THE DISTRIBUTION OF THE ACCESS CODE**

Interviews with Welle, with his son BW, nephew MH, and MH's friend, TD, reveal how Welle's number came to be misused. Welle posted the number on his kitchen bulletin board in Willmar, telling his son he could use it if he needed to talk to his father in St. Paul.

BW used the number several times to call his father in St. Paul, soon memorizing the number and calling procedures. His father had told him that he could use the number to call him in St. Paul, but did not give him any further instructions, or say how not to use the number. BW can't recall when he first used the number for other purposes, but says his calls were mostly for rides home from school or the golf course. He does recall giving the number to his cousin, and also to two junior high classmates, KB and PB, both of whom have told BW that they did give it, or may have given it, to others in Willmar. BW said he gradually stopped using the number in 8th grade, and believes he last used it in the spring of his 8th grade year, 1991. He knew it was supposed to be for his dad's office use, but thought it was a "free thing" from the government.

MH recalls how he got the number. He was visiting the Welles in the summer of 1989 or 1990 (Welle places the visit in 1990) when he and his cousin were at the country club. BW, who had the procedure memorized, used it to call home for a ride, and told MH how the system worked. Assuming that the year was 1990, MH was then 15; his cousin BW was 12. Like BW, MH thought the access code was "some kind of a free deal." MH estimated that he used the card two or three times per month--mostly to call for a ride home from after-school activities--from the time he got it from BW until April 24, 1991. MH felt increasing misgivings about using the number as time wore on and his understanding of such matters increased. He specifically recalls the last time he used the number because he was on his way home from the State debate tournament, and he called his parents to tell them he had won second place.

MH says he gave the access code to only one other person, his friend TD. After the problem came to light, MH talked to TD and asked him about TD's own use of the card. MH said that TD admitted to him using the number a lot more than MH, with 100 times being TD's best estimate. MH theorizes that the number was widely circulated as a result of TD's dissemination.

When interviewed, TD's estimate was lower. He did admit placing a number of calls to a friend at Interlochen College, in Interlochen, Michigan. Analysis of the early calls suggests that TD was indeed responsible for a widening number of calls to college campuses. Many calls were made to a 647 exchange which the St. Thomas phone directory shows as listed to TD's sister, and there were many other 647 numbers soon after the first calls attributable to TD's sister. In addition, the many calls to Interlochen began just before a widening number of calls to other college campuses.

THE EXTENT OF THE UNAUTHORIZED USE

The extent of the fall, 1991 activity clearly suggested widespread distribution of the code. (On a hunch, Plummer asked a State employee acquaintance who subscribed to on-line computer services to check his bulletin boards. He easily found the number on a computer bulletin board.) For several reasons, however, it is impossible to calculate precisely the cost of the unauthorized use.

First, as noted above, the unauthorized use began before November 1990, the month of the earliest available records. Assuming that it began in the summer of 1990, and given the relatively flat progression of misuse in the early months (see Appendix 8), it seems unlikely that the very early misuse accounted for more than \$1,000.

Second, even if records were available, it is highly unlikely that the legitimate calls could be identified at this late date. The subtraction of legitimate calls would probably not be significant, however, since in previous years Welle's phone bill had never averaged as much as \$50 per month. The total November 1990 through November 20, 1991 bill on Welle's account is \$90,509.29. Subtracting \$650, a hypothetical amount for legitimate calls (13 months at \$50 per month), and adding an even more speculative \$500 for pre-November 1990 misuse, yields a figure very close to the previously reported \$90,000.

That figure, however, is the cost to the House, not ~~to~~ the State. Welle's bills reflect the Department of Administration 1991 "coverage" charge to State agencies of \$.20/minute for

domestic and Canada, and \$1.15/minute for international calls. The actual cost to the State would vary based on the type of calls made, with intrastate INWATS calls actually being somewhat more expensive than interstate calls (.0986/minute vs. .0975/minute). The magnitude of this difference does not seem likely to be large.

In summary, the precise cost of the Legislative INWATS toll fraud is impossible to determine, given the state of the records, with a figure between \$90-91,000 being a good estimate.

INVESTIGATION OF THE ORIGINATION OF THE FRAUDULENT CALLS

On the afternoon of Thursday, March 18, the Attorney General's Office sought and received Rep. Welle's permission to release his entire 1991 phone records. Administrative Aide Aliceann Murphy-Grusin retrieved and collated the records. We were told then that pre-January 1991 records had been destroyed some time ago, but Murphy-Grusin later located and provided Welle's November and December, 1990 records.

On March 19, Speaker of the House Dee Long wrote a memorandum to all House members and staff directing them to fully cooperate with the investigation. (Appendix 10)

Welle's phone records, like those of other House members, show the member's identification number, the month and day of the call, the connect time, duration, charge, number called, and city called. (E.g., Appendix 11) However, the available records do not list the number or city of origin. We served administrative subpoenas on the phone companies, but have received neither call origination data nor pre-November 1990 information. The long distance carrier, MCI subsidiary Teleconnect, and the billing agent, US WEST, which actually generated the records, told us that the call origination data, and the pre-November 1990 bills no longer exist.

Late in 1991 US WEST did produce records detailing calls charged to Welle's number for selected months in 1991. The information was produced at the request of the Department of Administration. However, Bonnie Plummer, the Department's Network Services Manager,

who received the records, threw them out in a routine office cleaning in November 1992. The lack of call origination information has made it practically impossible to trace the origin of unauthorized calls and, therefore, the identity of the people who made them. The unavailability of these or similar records has made it impossible to determine precisely when the unauthorized calls began, or to calculate their total cost.

Since March 18, we have interviewed numerous people about the origin of the unauthorized phone calls and the actions of State officials and employees after the unauthorized use was discovered. A list of persons providing information appears at the end of this report.

We also requested all available documentation relating to the unauthorized calls and the State's handling of the matter. Unfortunately, there is relatively little documentary evidence apart from the voluminous phone records, which are themselves incomplete.

STATE TELEPHONE SYSTEM

Background of the Contracts

US WEST originally issued authorization codes as a way to keep track of calls for billing in a system which only allowed remote access through a live operator. At the beginning, the potential for "toll fraud" was virtually non-existent because the codes were used only at desk telephones and "remote access" was obtained by the use of the live operator system.

However, as the live operator system was phased out and the State relied more and more on the US WEST remote access system and codes, US WEST did nothing to update its authorization code system. By 1991, when the use of live operators was eliminated entirely, toll fraud was commonplace and other carriers were adding security protections to access codes.

US WEST and MCI, as sophisticated telecommunications companies were in a position to advise the State on code protection and to offer the State additional protection from fraud. For example, like other carriers, US WEST could have provided an "exception report" through its billing service by which it would have flagged unusual usage of any particular

billing code. US WEST could also have required each individual to have an access code (at negligible cost to the State) and installed security which would have prevented simultaneous code use (MCI will be providing such a system to the State through the STARS project). While the phone companies' liability in this matter remains unresolved, clearly the companies should have been more aggressive in identifying possible fraud and protecting their customers.

General Operation of the State Phone System

Under Minn. Stat. § 16B.46 the Department of Administration purchases telecommunications services for State agencies, including the Legislature. 1-800 and outgoing intrastate and interstate long distance services are purchased from Teleconnect (a wholly owned subsidiary of MCI). Some private intrastate long distance lines are purchased from AT&T. Local service, certain equipment and billing services are purchased from US WEST. Each of these companies charged different rates for the different services. The rates charged by US WEST and AT&T were "flat" - call volume or distance did not make a difference in what the State paid for the service. All of Teleconnect's charges varied with minutes of use, and those rates were different depending on whether the call was in Minnesota or out-of-state.

Administration's Telecommunications Division orders 1-800 lines for all State agencies requesting 1-800 service. There are a total of 196 lines available for the State. The 1-800 number, including seven lines ordered by the Legislature, was one of the first 1-800 systems ordered. It was to be used to provide members of the Legislature with "remote access" to the State's telephone system. The Legislature was assigned seven "ports" (lines) to handle calls over its 1-800 number. If those ports were all in use, the calls rolled over to a spare group of 50 ports assigned to the Department of Administration.

The House and Senate used the same 1-800 number to reach the State telephone system. However, the House had authorization codes for each member, while in the Senate everyone used and continues to use the same authorization code. Individual access codes allowed the House to get call detail for each member, a feature recommended by Administration at the time the system was adopted in order to promote greater accountability. With respect to the

Senate, because the access code is the same for every member, it is not possible to tell from telephone records which member places which long distance call through the remote access 1-800 number.

THE HOUSE PHONE SYSTEM

The Mechanics of Calling

From April 1985 until June 1, 1992, the House phone system permitted members and staff to make non-toll local calls through the State Centrex system (6-XXXX); outgoing, long-distance calls from State phones (8 + area code + 7-digit number); and point-to-point calls, generally toll calls, through the INWATS 1-800 number.

With the 1-800 number, a representative could dial in, reach the State's system and use a six-digit authorization code to dial out to any telephone number. The only limitations were that 1-900/976 service was blocked, and, because of the DNR toll fraud incident, international calls were blocked after September 1991. In order for US WEST to bill for the 1-800 lines by authorization codes, US WEST sells remote access "authorization codes" to the State through the Centron XL contract. Administration provided a master tape to US WEST but did not identify to whom each authorization code number was assigned.

Only members, not staff, had the access codes for what was referred to as the "incoming" WATS or "INWATS" line. All of the unauthorized calls which are the subject of this report were made on the INWATS system.

Until May 1, 1991, the system worked as follows. During the day, if a member of the Legislature dialed the 1-800 number, a live operator completed the call. The outgoing call was placed by the operator using the State (Centron/Centrex) network. At night the live operator was not available and calls went directly into a US WEST switch. The US WEST computer system verified the access code and completed the call.

After May 1991, the Legislature decided to stop using a live operator during the daytime hours because members were getting too many busy signals when they called the 1-800

number. Instead, at the Legislature's request, all INWATS calls were routed to the US WEST switch and the codes verified by the US WEST computer system. Because calls would be processed faster without the live operator, both Administration and the Legislature expected to see some increase in calling volume on the 1-800 number; and, in the summer of 1991 there was a slight increase in the House's total telephone bill.

After May 1991, a member placed remote access calls as follows:

- 1) dial 1-800-XXX-XXXX, to get a remote access unit, which gave a dial tone (signaling it had been transferred to the US WEST Centron/Centrex State system);
- 2) enter 8-area code-XXX-XXXX;
- 3) enter a six-digit personal identification number (PIN) ("authorization code")

A graphic illustration of the system, prepared by the Department of Administration in connection with its review of the unauthorized calls, is Appendix 12.-

Once US WEST processed a call at its St. Paul Market Street facility, the call was routed with all other calls on the State's Centron system. The categories of outgoing calls were local metro calls through US WEST, in-state long distance calls over private lines purchased from AT&T, in-state long distance calls over service purchased from Teleconnect, or out-of-state long distance calls through Teleconnect.

Long Distance Billing And Payment

As noted above, the Department of Administration buys telephone services for all of State government and each month pays the phone companies for the actual charges for calls. Administration gets the money to pay the bills from the State agencies. However, as an internal accounting matter, Administration does not require the agencies to pay the actual costs of service. Instead, all agencies pay the same predetermined, flat, per-minute rate. Administration sets a rate which it calculates will recover the cost of service over the whole system--in effect an apportioned average cost of all State calling rather than the actual cost. This flat rate facilitates billing, agency verification, and also avoids imposing

disproportionately large bills on users outstate where the actual cost of service is often much greater than in the Metro area.

During 1991 the charge to State agencies was \$.20 per minute for domestic long distance calls, and \$1.15 for international calls. The actual rates--what Administration paid under the US WEST and Teleconnect contracts--were \$.12/minute for a call into the remote access unit, \$.0214 for the call to be switched in the RAU, plus \$.0986/minute for an intrastate call out of the switch or \$.0975/minute for an interstate call. Thus, for example, a State agency might pay \$1.00 each for two five-minute, INWATS calls, but the actual cost of a call from Mankato to Chicago would be somewhat less than a call from Mankato to Willmar. Since all calls at one point or another were processed through US WEST's switching system, US WEST kept track of all calls for billing purposes. Using magnetic tapes of account data provided by Administration, US WEST sorted the call records and generated bills at its office in Omaha every month. US WEST acted as the billing agent for the State, and billed all State agencies directly, at the Administration-calculated, apportioned rate.

The Department of Administration received microfiche copies of the bills for all telephone service provided to State agencies except the Legislature. In 1989, a law was passed which stated, in pertinent part, "that [n]otwithstanding any law to the contrary, legislators' telephone records are private data." Minn. Laws 1989, ch. 335, art. 1, sec. 15. At the Legislature's request, no copies of telephone bills were sent to Administration.

The House of Representatives' telephone bill was itemized by sub-accounts: the Clerk of the House and the House members. The calls for the members of the House were sorted by telephone number and by type of call. Each member's call detail would show all Minnesota calls, all calls using the authorization code, and all interstate calls and individual totals. Each call would be shown by date, time, length of call and total cost of the call, and there would be a summary of all calls for each person at the end of that person's bill. House Administrative Services did not provide House members with their individual call detail.

Although the Department of Administration paid its long distance bill each month, the House did not. There is some dispute about whether US WEST sent regular monthly bills to the House. House Director of Staff Larry Bothwell complained about receiving irregular billings. Part of his job is to review the various bills submitted to the House, as assembled into a monthly "abstract." The abstract, which is typically prepared by staff in the name of the Speaker, is like an invoice of a month's authorized expenses. (See Appendix 9) A summary of total House phone bills from September 1990 through February 1993 does not show when bills were received, but does show that the House did not pay phone bills during a number of months, including July, September and November, 1991. (Appendix 14)

It appears from further investigation, however, that US WEST did generate monthly bills which the State received on or around the 20th of each month. Network Services Manager Bonnie Plummer received regular monthly billings from the State's phone companies, except during a system changeover several years before the incidents in question. While Plummer and her department did not receive the itemized call detail provided to the House, they did get the bottom line totals, which they posted monthly throughout 1991. (See Appendix 15) Moreover, House Administrative Services Aide Murphy-Grusin recalls receiving the bills monthly.

What appeared to Bothwell, at his level, to be irregular billing by the phone company, seems to have been irregular processing of the bills by House Administrative Services. The irregular processing made it less likely that anyone in the House would detect irregularities in monthly billings. However, the House's total monthly bills--as opposed to Welle's individual bills--did not markedly exceed historical levels until October 1991. See Appendices 16, 17, and 18: US WEST did not generate the October billing until November 14, the same day the State discovered the unauthorized use by other means. See Appendix 19.

HOUSE POLICY REGARDING AUTHORIZED USE OF STATE PHONES

The House Had No Written Policies

The House has no formal rules governing the use of State phones, including the incoming WATS line. As head of House Administration, David Kienitz briefed new members on the phone system, telling them that State phones were for legislative business only. (Appendix 5) There were no other systematic efforts to communicate policy to House members on staff. House Administration issued each new member a wallet-size, laminated card with the INWATS system numbers and dialing directions. Partly because members' spouses often stay home in the districts, and often receive local calls about legislative matters, spouses have been authorized to use the system to talk to the members in St. Paul. Children who needed to talk to parent-members were also authorized to use the system to call St. Paul. Purely personal calls, however, were not officially authorized. Appendix 5)

House Administration Was Repeatedly Warned That Some Members And Their Families Were Making Unauthorized Calls

House Administrative Services appears to have unofficially sanctioned much broader usage than the official new member briefings and memoranda indicate, or than the House has heretofore acknowledged. Network Services' telephone operators had repeatedly warned House managers that the system was being abused, but the operators were told not to question people who appeared to be authorized users.

The friction between State operators and House managers helped prompt a changeover to fully automated calling in the spring of 1991. Before May 1, 1991, daytime INWATS calls were connected through State operators under the supervision of Laura Hoffman. Because the operators customarily stayed on the lines long enough to ensure a good connection, they often heard enough of the conversations to determine their essential nature. Hoffman and her operators believe that historically 30 to 40 percent of legislators' long distance calls have been unauthorized. The operators kept log sheets categorizing calls. Few log such sheets survive,

but examples (Appendix 20) show that of 1,251 INWATS calls during March and April, 1981, only three were connected to 296 or 297 State government exchanges (the "STN" column on Appendix 20). The minimal number long distance calls made to State numbers corroborates the operators' belief that many calls were not for State business.

Hoffman and other staff met with Kienitz, and sometimes House fiscal manager Mark Rogosheske, every 12 to 18 months to talk about phone usage. Hoffman says she and others repeatedly told Kienitz and Rogosheske that the House phone lines were being used by former members, by college-age children calling each other, for calls to out-of-state relatives, and for obvious non-business purposes. Hoffman says that Kienitz and Rogosheske instructed the operators to connect the calls, not to question people who had the right access codes and identified themselves as legislators or their family members. Kienitz eventually told the operators they should only let members' families call 296 and 297 exchanges, a restriction which limited daytime calls before May 1, 1991. Hoffman and her colleagues had similar conversations with Sandy Burill of Senate Administration, although the Senate was less of a problem.

The House shifted the cost of daytime, operator-assisted INWATS to Network Services, and as the House phone bills continued to grow, Network Services could no longer afford to pay the monthly bills out of the telecommunications fund. (See Appendix 21) The May 1, 1991 changeover from daytime operator-assisted to fully automated calling was prompted in part by Network Services complaints about the growing cost of service to the House.

MONITORING MEMBER PHONE USAGE

There was virtually no monitoring or auditing of House member phone usage during 1991. The Department of Administration kept track of total billings but could not monitor individual usage because it did not have the records. House Administrative Services had the records, but for all practical purposes did nothing with them. Members did not get their individual bills, or even see the total billings. The only monitoring House Administrative

Services did do was a vestige of an older House rule limiting members to \$600 of calls per year, and requiring them to pay any excess billings out of their own pockets. To enforce the \$600 limit a clerk posted monthly member total billings and notified members accordingly.

Since 1989 House rules have not limited members' calls, but, according to Kienitz, House Administration continued to keep some track of member totals even after the rule changed. This was done more out of habit than for any other purpose. It was not done rigorously, and no permanent records were made. Through 1991 the \$600 figure remained as an informal and non-binding benchmark, and Kienitz assigned Murphy-Grusin to pore through the monthly hard copy bills and alert members when they approached \$600 in phone billings for the year. Despite earlier inconsistent statements, however, Murphy-Grusin has admitted that she did not look at the records. There appears to have been no other scrutiny of member phone use.

According to a spread sheet generated by the House and showing all House members' phone bills for 1991, 17 people exceeded \$600 for the year. (Appendix 21) This spread sheet does not include all long distance phone usage, however. Some member calls made from remote locations to House staff phones, then transferred back out to long distance numbers are not included, and many legislators make such calls. In addition, some calls are simply not billed correctly, and a number of legislators have noted that they made long distance calls when the spread sheet shows they did not.

Welle Was Warned Of High Phone Use

Sometime in 1991 Welle was warned that his long distance bills had exceeded \$600--but it is not clear when he was warned, or who issued the warning. Murphy-Grusin, who was supposed to review the records and notify members, first told us that she remembered sending Welle a warning note in March or April. Later, however, she disclaimed any memory of sending a warning, or even of reviewing the records, saying that she originally told us March or April because she wanted to appear that she knew what she was doing. She now says that it

was Kienitz who told her, in early 1992, that Welle had mentioned after the abuse was discovered that Welle had received such a note in March 1991.

Kienitz, when interviewed in March 1993, thought the warning was given in mid-summer, 1991, but admits not knowing about any note when it was sent. Croonquist was not sure, but thought the warning arrived in November. Mary Ellen Langenberger, Welle's secretary, thought the warning came in a phone call, rather than a note, and that she took the call in the summer. Welle says he does not now recall whether he received a written notice or a phone call, but remembers getting something, and believes it was in October or November. No one suggested that there may have been more than one notification, and Kienitz says that the informal policy only called for one warning.

Two facts are consistent with the possibility that Welle received a warning in March or April, 1991. First, Welle's WATS bill was \$223.26 in January, and \$495.41 in February, for a cumulative total of \$718.67. (See Appendix 8) If anyone had been sending out timely notices, Welle's should have been sent soon after the February bill arrived in the third or fourth week of March.

Second, when Plummer asked for Welle's records in connection with her investigation in November 1991, she asked for the months of March and September. (See Appendix 3) She based that request on the collective best guess at that time that the unauthorized phone calls went back as far as March. No one remembers now how they arrived at March, and the only now-apparent possibility is that Welle or someone associated the month of March with the warning.

In any event, there is no dispute that Welle ignored what warning he received. Having never exceeded \$600 in his then eight years in the House, he considered the warning as simply a clerical mistake and disregarded it.

THE HOUSE CHANGES THE PHONE SYSTEM

In early 1992, Long, Bothwell and the House DFL caucus quickly overhauled the House system to prevent future toll fraud and increase member accountability. By February 18, 1992, Bothwell recommended changeover to a system of individual, personal credit cards, which members would check monthly and submit for reimbursement. That system was adopted effective July 1, 1992, and remains in effect. (Appendix 22)

The House now requires each of its members to review individual call detail and verify that all calls placed on their telephones were business-related calls. For remote access, House members are required to use a personal calling card when they are on the road, and an AT&T corporate account from their home or business. Members must submit reimbursement requests after paying their telephone bills themselves. For those 30 or so members in non-equal access areas, a 1-800 number is available. Each person still has an individual code, but is required to verify on a monthly basis that all calls on the 1-800 system were business related. The 1-800 number will gradually be eliminated as non-equal access areas are converted into equal access areas.

The new House phone system greatly increases member accountability, though it still does not result in consolidated phone bills reflecting all a member's calls, nor does it address abuses of office phones by staff members and third persons allowed access to the phones.

The Senate has yet to adopt any reforms to increase member accountability for phone use. The Senate's change to an individual credit card or similar system is long overdue.

SELECTED MINNESOTA AND FEDERAL STATUTES

Statutes Applicable to Telephone Fraud

Minnesota has a number of criminal statutes dealing with the subject of telephone fraud, and the possible involvement of a public official or employee in telephone fraud. It must be left to the appropriate prosecutors to apply the law to specific situations; it is not the purpose of this report to analyze the statutes in detail, or to speculate how they could be applied to individuals. A brief discussion, however, is in order.

Minn. Stat. § 609.893 Telecommunications and Informations Services Fraud

The telecommunications fraud statute makes it a crime to steal telephone services and to facilitate fraud. Under subdivision 1, it is unlawful for a person to 1) obtain telephone service for the person's own use, 2) by any fraudulent means, and 3) with intent to evade a lawful charge. The severity of the crime depends on the value of the services taken, with \$500 being the dividing line between a misdemeanor and a felony.

Subdivision 2 covers two common ways of facilitating phone fraud: 1) offering, advertising or making available a "telecommunications device or information"--which could include either a piece of electronic equipment, a credit card or access codes, in order to "facilitate" the unlawful taking of phone service; and 2) making or possessing a device for unlawfully obtaining phone service (such as a "black box"). Facilitating fraud is a felony without regard to the amount of any actual loss.

Minn. Stat. §§ 609.52, subd. 2 (13), Theft of Services, and 609.52, subd. 2 (14), Theft of Telecommunications Service

The State's general theft statute contains two provisions which can be applied to telecommunications fraud. The first is subdivision 2 (13), which makes it a crime to "[obtain] the services of another with the intention of receiving those services without making the agreed or reasonably expected payment of money or other consideration...." This provision can cover the theft of all kinds of services--everything from running out of the barber shop to avoid

paying for a haircut, to getting illegal access to a computer service. It requires proof of an intent not to pay for the service.

Subdivision 2 (14) prohibits "intentionally depriv[ing] another of a lawful charge for telecommunications service..." by means of black boxes, or other kinds of unauthorized physical or electronic connections.

As with other theft crimes, the punishment depends on the value of the services or property taken. Theft of up to \$200 is a misdemeanor, theft between \$200 and \$500 is a gross misdemeanor, and theft over \$500 is a felony (with several levels of punishment within the felony category, again depending on the amount taken).

18 U.S.C.A. § 1029, Fraud and Related Activity in Connection with Access Device

Federal law--which State prosecutors have no standing to enforce--provides that one who 1) knowingly and with intent to defraud, produces, uses, or traffics in...counterfeit access devices; or 2) knowingly and with intent to defraud traffics in or uses...unauthorized access devices..." is guilty of a felony. 18 U.S.C.A. § 1029. A "counterfeit" device may include a counterfeit credit card, or even a legitimate access device fabricated by a computer "hacker" systematically generating code numbers until finding one that worked. See United States v. Brewer, 835 F.2d 550, 553 (5th Cir. 1987).

Selected Statutes Governing the Conduct of Public Officials and Public Business

Minn. Stat. § 609.43, Misconduct of Public Officer or Employee

It is a gross misdemeanor for a public officer or employee to 1) intentionally fail or refuse to perform a mandatory duty as prescribed by law; 2) in an official capacity, do some act knowing it to be in excess of lawful authority; 3) intentionally and unlawfully injure another under pretense or color of official authority; or 4) in an official capacity, make a return, certificate, official report or similar document, knowing it to be false in any material respect. This statute further requires that the violation be one "for which no other sentence is specifically provided by law."

Gross misdemeanors are punishable by not more than one year's imprisonment and a fine of not more than \$3,000.

Minn. Stat. § 609.455, Permitting False Claims Against the Government

"A public officer or employee who audits, allows, or pays and claim or demand made upon the state...[and] which the [person] knows is false or fraudulent..." is guilty of a felony.

Minn. Stat. § 609.456, Mandatory Reporting to State Auditor

"[A] public employee or public officer of a political subdivision" who discovers the "theft, embezzlement, or unlawful use of public funds or property" is required to report the matter to the state auditor, unless doing so would interfere with a criminal investigation. No punishment is specified.

This statute requires local government officers and employees to report incidents such as known toll fraud to an investigating authority. It does not apply to state officials, such as Alan Welle or David Kienitz.

**LIST OF PERSONS PROVIDING
INFORMATION INCLUDED IN THIS REPORT**

Dana Badgerow, Commissioner, Department of Administration

Lawrence Bothwell, Director of Staff, House of Representatives

Bernard Conlin, Assistant Commissioner, InterTechnologies Group, Department of Administration, which includes the Telecommunications Division

Scott Croonquist, Legislative Aide to House Majority Leader Alan Welle

TD, a friend of MH (and a minor at the time of the relevant events)

Christie Eller, Assistant Attorney General, manager of the Administration and Finance Division which represents the Department of Administration

Laura Hoffman, Communications Center manager, Department of Administration

MH, Rep. Welle's nephew, a minor at the time of the relevant events

Todd Johnson, Legislative Aide to Speaker Long

David Kienitz, head of Administrative Services for the House

Mary Ellen Langenberger, Rep. Welle's secretary

Dee Long, Speaker of the House

Kathi Lynch, former Director, Business Technologies Division (Telecommunications), Department of Administration

Joel Michael, House Counsel

Aliceann Murphy-Grusin, Administrative Aide, House Administrative Services

Mary Jo Murray, Special Assistant Attorney General, Administration and Finance Division, designated counsel for the Department of Administration on telecommunications issues

Bonnie Plummer, Manager, Network Services Management, Department of Administration

Patsy Randell, Governor Carlson's former Deputy Chief of Staff

Tom Shutz, MCI fraud investigator

Robert Vanasek, former Speaker of the House.

Alan Welle, State Representative

BW, Rep. Welle's son, a minor