

**Agencias Universales S.A.  
Internal Control Report  
For the Period January 1, 2005 to May 15, 2005**

**National Science Foundation  
Office of Inspector General**

**March 22, 2007  
NSF OIG 07-1-009**



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## **EXECUTIVE SUMMARY**

## **EXECUTIVE SUMMARY**

National Science Foundation  
Office of the Inspector General  
4201 Wilson Boulevard  
Arlington, Virginia 22230

### **Background**

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Raytheon Polar Services Company (RPSC) notified the National Science Foundation (NSF) of a potentially fraudulent act committed by employees of its subcontractor Agencias Universales S.A. (AGUNSA), who are responsible for performing NSF ship chandlery duties. Ship chandlery involves the dockside supply of food, fuel, and equipment to the Research Vessel (RV) Gould and RV Palmer at Punta Arenas, Chile. The fraudulent act was discovered in 2003 and involved two AGUNSA employees at the Punta Arenas office, who were later charged in a Chilean court for embezzling funds, using a vendor invoice lapping scheme through which payments intended for AGUNSA vendors were diverted for the embezzlers' private use.

AGUNSA is a Chilean company with annual sales of [REDACTED] million in the maritime port services sector in Latin America, including a total of 39 offices distributed in 10 countries: Perú, Ecuador, Colombia, Argentina, Paraguay, Venezuela, USA (Miami), Jamaica, Mexico and Chile. AGUNSA is considered to be a large company in Chile, and has begun to play an important role in the international transport sector, providing such services as cargo handling, bunkering, tug services, serving as a logistics and stevedoring agent, and airport concessions. Overall, the Company employs approximately [REDACTED] people.

Although it is a Chilean company, AGUNSA, as a subcontractor on a NSF contract, is required to follow all applicable contract requirements in the Federal Acquisition Regulation (FAR). The AGUNSA subcontract is approximately \$2 million annually and expected to continue through Fiscal Year 2009.

### **Objectives, Scope and Methodology**

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Our objectives were to determine whether AGUNSA's internal control systems in its accounting and billing processes subsequent to the embezzlement scheme are adequate to properly accumulate, track and monitor its costs and billings under the RPSC subcontract in compliance with NSF and Federal requirements. Our objectives were also to identify matters concerning instances of noncompliance with laws, regulations, and the provisions of the subcontract between AGUNSA and RPSC. To accomplish these objectives, we compared AGUNSA's internal control over the accumulation, tracking, monitoring, and billing of subcontract costs to RPSC against the internal control guidance published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the standard for internal control for the U.S. Federal Government and the U.S. based Public Company Accounting Oversight Board, and documented our findings. COSO provides a common definition of internal controls and guides in the

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creation, assessment, and improvement of an organization's internal control system.<sup>1</sup> We also reviewed the circumstances surrounding the embezzlement which we reported on in a separate report,<sup>2</sup> which also provides recommendations to prevent future recurrence.

This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and the standards applicable to attestation engagements contained in *Government Auditing Standards (2003 Revision)*, issued by the Comptroller General of the United States.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on AGUNSA's internal controls. Accordingly, we do not express such an opinion. If we had performed the additional procedures necessary for an examination level review, other matters might have come to our attention that would have been reported to you.

At AGUNSA's central office in Valparaiso, we concentrated our procedures on an analysis of the control environment, risk assessment, information and communication systems, and monitoring activities. At AGUNSA's Punta Arenas office, the site of the embezzlement, we concentrated our procedures on control activities.

To achieve the audit objectives, we inspected the Company's financial management, human resources, and financial accounting system procedures. We also inspected the internal management financial reports, financial audit reports, contract documentation, annual financial statements, job descriptions, and all other relevant background documentation made available to us, including the AGUNSA commissioned Guerra Raby CPA Audit Report on the extent of the embezzlement and the Chilean Police's Economic Crime Unit Report. We also interviewed relevant management officials and staff as part of the overall Internal Control Assessment. (See Attachment B - Internal Control Assessment and Attachment C - List of Interviewees)

In addition, we analyzed transactions and costs incurred by AGUNSA under its RPSC subcontract in 2005, for compliance with its corrective actions implemented to address the embezzlement. We also assessed AGUNSA's procedures to account for and bill RPSC for subcontractor costs, including compliance with NSF and Federal requirements. We conducted our audit work from January 1, 2005 to May 15, 2005 at the AGUNSA main office located in Valparaiso, Chile.

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<sup>1</sup> See [www.theiia.org](http://www.theiia.org) for more information concerning COSO.

<sup>2</sup> See NSF OIG Report titled *Agencias Universales S.A. Embezzlement Report for the period January 1, 2002 to June 30, 2003*, for further discussion of the embezzlement.

## Summary of Findings and Recommendations

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Our review of invoices for the period January 1, 2002 through June 30, 2003 disclosed that the embezzlement loss to AGUNSA totaled approximately \$157,000<sup>3</sup> of which approximately \$7,200 related to AGUNSA's subcontract with RPSC. AGUNSA, after discovery of the embezzlement, held itself accountable for the embezzlement and paid all affected vendors. Nevertheless, judgmental sampling conducted during the audit, but subsequent to the embezzlement, identified up to approximately \$616,000 of potentially lapped (delayed) payments to vendors servicing the RPSC contract. AGUNSA had no other U.S. government contracts. In general, AGUNSA's lack of management oversight, lack of internal control over the accounting and vendor payment process, failure to enforce its own policies and procedures, and noncompliance with the RPSC subcontract terms enabled the embezzlers to perpetrate the vendor invoice lapping scheme. Properly designed internal controls that are monitored and enforced could have prevented, or allowed, earlier detection of the embezzlement.

We also noted some continuing internal control deficiencies and compliance violations, despite corrective actions implemented after the embezzlement by AGUNSA management. AGUNSA lacks an overall internal control framework and methodology (COSO Framework) to oversee and manage its financial accounting and reporting operations with respect to its RPSC contract. Furthermore, AGUNSA has not fully implemented its corrective action plan to correct the internal control deficiencies surrounding the embezzlement. As such, these deficiencies could have an impact on AGUNSA's ability to effectively administer its ongoing financial activities under the RPSC subcontract.

The following is a brief description of the continuing internal control and compliance findings that could allow the embezzlement to reoccur and which continue to affect AGUNSA's internal controls over its RPSC contract.

- 1. Inadequate Internal Controls For a Large Corporation:** AGUNSA lacks a COSO methodology framework of internal control over its RPSC subcontract commensurate with AGUNSA's current operating capacity to manage and oversee its financial accounting, billing, invoicing, and reporting operations at its Puntas Arenas office. It appears that development and upgrades in business systems and controls did not keep pace with the extensive corporate growth AGUNSA has experienced and could have contributed to the lax monitoring of vendor payments on the RPSC subcontract associated with the embezzlement.
- 2. Federal Acquisition Regulation Inexperience Leads to Regulatory Violations:** AGUNSA did not comply with the Federal Acquisition Regulations (FAR). The terms and conditions of the RPSC subcontract requires AGUNSA to follow certain FAR provisions including those related to vendor invoice terms and payment to vendors before requesting payment from RPSC. AGUNSA did not pay the vendor's invoices within 30 days of receipt as required by the FAR. AGUNSA submitted invoices to RPSC for reimbursement prior to making payments to its own vendors which is prohibited by the FAR and the RPSC subcontract. As a result, AGUNSA could have received reimbursement for costs that it had not yet paid. AGUNSA must establish, implement

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<sup>3</sup> All monetary amounts identified in this report are stated in U.S. dollars unless otherwise indicated.

and enforce policies and procedures that will meet the minimum requirements contained in the FAR for a subcontractor performing for a U.S. Government contractor. In addition, periodic reviews by AGUNSA management of its policies and operating procedures will ensure AGUNSA's higher-level management, RPSC, and NSF that it has correctly recorded, paid, and billed subcontract costs. Management reviews should also ensure that AGUNSA's policies and procedures remain current and consistent with its accounting practices and its applicable FAR and RPSC contractual requirements.

3. **Inadequate Board of Directors Involvement in Internal Controls:** The AGUNSA Board of Directors agreed on July 30, 2003, to systematize and revitalize internal audit procedures but it does not appear that the Board has monitored this process; ensured that the AGUNSA Internal Control Unit performed a visit to the Punta Arenas Office as required in AGUNSA's procedures; or followed-up to ensure the adequacy and implementation of the AGUNSA General Manager's corrective action plan.
4. **Inadequate Segregation of Employee Duties:** AGUNSA lacks proper segregation of employee duties by continuing to concentrate a number of payment processing duties in the current [REDACTED] position that are not significantly different than the duties of the previous [REDACTED] (one of the embezzlers). Therefore, this continuing concentration of duties in a single individual could allow future embezzlements to occur. The [REDACTED]. The [REDACTED] was responsible for both the [REDACTED], creating an internal control weakness between the duties of accounting and the check [REDACTED] functions. After the embezzlement was discovered, several vendor invoice payment procedures changed including the implementation of a mandatory vacation policy. However, those changes did not address the continued concentration of duties and unrestricted accounting system access in the [REDACTED] position. Poor segregation of duties directly impacts AGUNSA's ability to accumulate, track, monitor, and bill subcontract costs to RPSC and limit future reoccurrences of an embezzlement.
5. **Inadequate Development and Implementation of Financial and Administrative Policies and Procedures Results in Inadequate Internal Controls:** There are policies and procedures for processing invoice payments and for other financial and administrative activities; however, they are either not complete, not well communicated, not complied with, or the employees are not trained in them. AGUNSA implemented corrective actions following the discovery of the embezzlement; however, it has not adequately documented those corrective actions (i.e. internal controls) in written policies and procedures; carried out any tests of their effectiveness; or analyzed the possibility of any additional financial risks associated with its RPSC subcontract, for which appropriate controls should be implemented.
6. **Employees Insufficiently Trained About Internal Controls:** Subsequent to the embezzlement, AGUNSA did not conduct sufficient employee training on financial and administrative procedures, internal controls, ethical matters or fraud prevention. In particular, AGUNSA's employee-training program does not cover identifying and monitoring restricted funds and unallowable costs. Inadequately trained employees directly impact AGUNSA's ability to accumulate, track, monitor, and bill subcontract

costs to RPSC in compliance with NSF and Federal requirements. AGUNSA's lack of a formal approach to anti-fraud and internal control related training directly increases the risk of a future embezzlement.

7. **Poorly Defined Employee Duties and Performance Evaluations:** AGUNSA lacks both written formal job descriptions for its accounting and billing staff, and a system of regular performance evaluations. In order for AGUNSA's policies and procedures to effectively safeguard company assets and maintain efficient operations, employee duties must be clearly defined and employee performance of those duties evaluated and documented to identify opportunities for improvement. Proper segregation of duties among employees cannot be achieved without first clearly delineating the employee's duties in, for example, the vendor invoice payment process. Unclear and poorly defined employee duties make it possible for employees to subvert the vendor invoice payment process for their own gain. The oversight provided by requiring managers to evaluate employee performance by clearly defined duties, is a further safeguard that promotes the effectiveness of internal controls incorporated in the design of the vendor invoice payment system.
8. **Need for Evaluation of Employee Assignments and/or Retraining:** The [REDACTED] at the Punta Arenas office remains in his current position despite not exercising adequate due diligence in co-signing checks associated with the embezzlement. Failure to adequately review the checks for compliance with AGUNSA's company policy, before co-signing checks, circumvented the internal control and indirectly benefited the embezzlers, allowing them to convert AGUNSA funds to their own private use.
9. **RPSC May Have Paid for Services Not Received:** AGUNSA allowed for purchasing goods and services without adequate RPSC Marine Project Coordinator documentation, authorization and approval. In addition, there was limited documentation evidencing delivery of goods or services to RPSC. Without adequate invoice documentation and proof of delivery there is a risk that payments could be made for goods or services that were not ordered and/or delivered.

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

1. Adopt a COSO methodology to internal control over the RPSC subcontract, which would serve as a guide for AGUNSA management in developing, implementing, and overseeing the important elements of internal control such as the control environment, risk assessment, control activities, information and communication system, and monitoring.
2. Obtain an understanding of the FAR provisions applicable to its RPSC subcontract and communicate these requirements both verbally and in writing to appropriate management and accounting personnel. AGUNSA should specifically design procedures to monitor AGUNSA's compliance with these provisions using the COSO framework as a guide.
3. Ensure that the AGUNSA Board of Directors make certain that the proposed corrective actions relating to compliance and control monitoring by AGUNSA's Internal Control Unit are implemented and followed. We also recommend that NSF ensure that RPSC directs AGUNSA to consider having the Internal Controls Unit report directly to an Audit

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Committee of the AGUNSA Board, or similar governing body. The Unit should follow standard internal audit practices such as those promulgated by the Institute of Internal Auditors (IIA), and perform semiannual internal audits of its various branches as stated in its corporate policies and procedures.

4. Revise Company policies as necessary to segregate the duties of the [REDACTED] such that processing, recording, and payment of vendor invoices are segregated among different staff to perform. AGUNSA should ensure that vendor checks are properly prepared, documentation properly supports each payment, accounting records are updated properly, and invoices are paid promptly in accordance with AGUNSA policies and procedures and the RPSC subcontract. All cash flow activity, including checks, invoices paid, and accounting records should be reconciled and posted daily. AGUNSA management should also monitor compliance with all Company policies and procedures, especially with regard to the vendor payment process and help mitigate fraud by collusion by monitoring compliance with its new vacation policy. The new vacation policy currently being communicated verbally should also be incorporated into the Human Resources manual. AGUNSA management should perform unannounced spot checks to ensure compliance with company policies and procedures.
5. Develop a comprehensive set of financial and administrative procedures with regard to the RPSC subcontract based on a control risk analysis, and communicate and implement these procedures in the Punta Arenas office. Additionally, AGUNSA should specifically design internal control procedures to monitor compliance with the FAR as well as financial and administrative procedures mentioned above, using the COSO framework as a guide. AGUNSA should also train all financial and administrative personnel on Company policies and procedures and periodically evaluate the effectiveness of its controls and analyze the risks associated with its operations, so that appropriate controls can be effectively designed (or modified) and monitored with regard to the RPSC subcontract.
6. Provide employee training on financial and administrative procedures with particular focus on risks and associated controls. We also recommend that AGUNSA provide adequate training on ethical behavior, resolution of conflict of interests, internal controls, and anti-fraud procedures. AGUNSA should establish more detailed ethical and anti-fraud procedures as well as periodic reviews of these procedures. Additionally, AGUNSA and RPSC should conduct joint working/training sessions with RPSC on subcontract management, both in administrative and financial matters.
7. Define personnel responsibilities and conduct formal employee performance evaluations for all staff involved in the RPSC subcontract. In addition, AGUNSA should provide training that supports and relates directly to employee job duties and responsibilities of staff working on and monitoring the RPSC subcontract.
8. Review the Punta Arenas [REDACTED] indirect involvement in the embezzlement in order to evaluate whether the [REDACTED] has had the retraining necessary to effectively discharge his control duties and continue in his current assignment. Obtain details of AGUNSA's assessment of other individual's direct or indirect involvement in the embezzlement. Ensure all Punta Arenas AGUNSA employees with check signature

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authority understand fully and properly execute their responsibilities in disbursing and safeguarding company funds.

9. Have internal control procedures in place to follow subcontract procedures to obtain proper documentation, authorization, and approval of invoices for submission to RPSC. These procedures should require that AGUNSA obtain authorization and supporting documentation from the RPSC Marine Project Coordinator in Punta Arenas before invoices are submitted to RPSC to ensure that the goods and services were delivered and benefited the RPSC subcontract activities.

AGUNSA's response to the audit report, dated March 15, 2007, indicated that in general, they agreed with the findings and recommendations in this report, except finding nos. 3 and 9. In recommendation no. 3, AGUNSA stated that there was no further need for the Board of Director's involvement because corrective actions were sufficient and in recommendation no. 9, AGUNSA stated that its invoices now have the RPSC Marine Project Coordinator approval on them. We considered these statements and indicated that 'monitoring' is a key component of internal control and that our testing performed indicated that RPSC Marine Project Coordinator approvals were missing.

For a complete discussion of the audit findings, refer to the "Independent Accountant's Report on Applying Agreed-Upon Procedures at Agencias Universales S.A. Internal Control Report." The findings in this report should not be closed until NSF has determined that all the recommendations have been adequately addressed and the proposed corrective actions have been satisfactorily implemented.

### Exit Conference

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We attended an onsite exit conference with AGUNSA in December 2005. Mr. Jorge Martinez (PKF Witt Mares) met with [REDACTED] for five hours, to present in detail, and obtain comment on, our preliminary findings. We were informed that they agreed with some of the findings and had various levels of disagreement with certain other findings and would like the opportunity to respond in writing.

We presented AGUNSA with a draft report on March 2<sup>nd</sup>, 2007 to which they responded in writing on March 15<sup>th</sup>, 2007. Certain specific comments can be seen throughout this report under the caption "Management's comments:" and AGUNSA's general response has been included in its entirety in Attachment D to this report.

**INDEPENDENT ACCOUNTANT'S REPORT ON  
APPLYING AGREED-UPON PROCEDURES AT  
AGENCIAS UNIVERSALES S.A.**

**INTERNAL CONTROL REPORT**

## **INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES**

National Science Foundation  
Office of the Inspector General  
4201 Wilson Boulevard  
Arlington, Virginia 22230

To the National Science Foundation Office of the Inspector General

We have performed the procedures identified below for the period January 1, 2005 to May 15, 2005, which were agreed to by the National Science Foundation (NSF) Office of Inspector General (OIG) for their purpose of assessing whether AGUNSA's internal control has the ability to accumulate, track, monitor, and bill subcontract costs to Raytheon Polar Services Company (RPSC) in compliance with NSF and Federal requirements. The sufficiency of these procedures is solely the responsibility of the NSF OIG. Consequently, we make no representation regarding questions of legal interpretation or the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose. Performance of the procedures by PKF Witt Mares should not supplant any additional inquiries or procedures NSF OIG would undertake in consideration of AGUNSA's internal control with regard to the RPSC subcontract. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and the standards applicable to attestation engagements contained in *Government Auditing Standards (June 2003 revision)*, issued by the Comptroller General of the United States.

At the request of the NSF OIG, we compared AGUNSA's internal control over the accumulation, tracking, monitoring, and billing of subcontract costs to RPSC against the internal control guidance published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the standard for internal control for the U.S. Federal Government, and documented our findings. Refer to Attachment A for the detailed Internal Control Assessment Scope and Methodology.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on AGUNSA's internal controls. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the NSF OIG, NSF, RPSC, and AGUNSA and is not intended to be and should not be used by anyone other than these specified parties.

*PKF WITT MARES PLLC*

PKF Witt Mares, PLC  
Fairfax, Virginia.  
May 27, 2005

## **FINDINGS AND RECOMMENDATIONS**

### ***Finding No. 1: Inadequate Internal Controls for a Large Corporation***

AGUNSA lacks an overall internal control framework and methodology to manage and oversee its financial accounting, billing, invoicing, and reporting operations at its Punta Arenas, Chile office commensurate with its size as a large corporation. AGUNSA was missing important elements of internal control in each of the COSO control categories of control environment, risk assessment, control activities, information and communication system, and monitoring to manage and oversee its financial accounting, billing, invoicing, and reporting operations in the Punta Arenas office. See Attachments A and B for a more detailed description of the auditors' assessment of AGUNSA's internal controls as they relate to the COSO Framework.

AGUNSA experienced rapid revenue growth in its business of 74 percent between 2001 and 2004. In 2003, (the year the embezzlement was discovered) revenue increased by 54 percent and net profits increased by 56 percent over the prior year. In 2004, revenue increased by 7 percent while net profits increased by 33 percent. In periods of rapid growth, a company should ensure that its control environment and infrastructure are able to support such an expansion. An internal control system based on a COSO methodology would ensure that an internal control infrastructure is in place to properly manage the new risks associated with AGUNSA's rapid growth. It is possible that this rapid expansion had a direct effect on AGUNSA's ability to monitor compliance with their policies and procedures in the Punta Arenas office. AGUNSA's lack of a formal structured approach to internal control created an environment that magnified the opportunity for fraud, such as the embezzlement by two long time AGUNSA employees in the Punta Arenas office illustrates.

### ***Recommendation No. 1:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Adopt a COSO methodology to internal control over the RPSC subcontract,
- b) Use the COSO methodology to serve as a guide to oversee, manage, and review the adequacy of its company's internal control infrastructure,
- c) Design the internal control system to accommodate AGUNSA's expanding business and monitor itself for necessary control changes in periods of company growth.

### ***Management's comments:***

"We agree on adopting the COSO methodology over the contract in our office in Punta Arenas if it is required by RPSC or NSF." Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

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***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 2: Federal Acquisition Regulation Inexperience Leads to Regulatory Violations***

AGUNSA's vendor payment procedures do not comply with the FAR requirements in its RPSC subcontract and AGUNSA's own cost reimbursement procedures are not followed. These noncompliances, coupled with the collusion in the embezzlement resulted in AGUNSA not paying its vendor invoices within 30 days of invoice receipt and resulted in AGUNSA claiming unpaid vendor costs to RPSC. The terms and conditions of the RPSC subcontract requires that AGUNSA follow certain FAR provisions including those related to adhering to vendor invoice payment terms and paying vendors before billing the U.S. Government through a contractor.

Specifically, the RPSC subcontract incorporates by reference the FAR that requires that vendors be paid within vendor invoice terms, within 30 days of invoice submission to AGUNSA. In addition, AGUNSA's policy requires that vendor invoices be paid within 32 days (2 days for entry into the system and 30 days for payment once entered); however, that policy fails to meet the 30-day vendor invoice payment requirement of the RPSC subcontract. AGUNSA did not pay the vendor's invoices within the number of days required by the RPSC subcontract or its own policy. AGUNSA officials state that the standard practice for payment of vendor invoices in Punta Arenas is 60 days or more. The embezzlers in the Punta Arenas office delayed vendor payments a further 83 days (average) or more as part of their embezzlement scheme. If AGUNSA management had enforced its own policy for vendor invoice payment of 32 days, the embezzlers' ability to successfully execute their embezzlement scheme would have been limited.

In addition, primarily due to the embezzlement, AGUNSA submitted claims to RPSC prior to making payments to its own vendors (in accordance with vendor terms) which is prohibited by the FAR. This could result in AGUNSA receiving reimbursements from RPSC for costs that it had not yet paid. Therefore, control deficiencies with the invoice payment process at the Punta Arenas Office was not only contrary to AGUNSA's own payment policy but also contributed to the embezzlement scheme.

Although the RPSC subcontract with AGUNSA incorporates by reference RPSC TC-002 Raytheon Company Standard Terms and Conditions, FAR Provisions, AGUNSA management was not aware that the subcontract incorporates certain provisions from the FAR, (by reference) and that AGUNSA, therefore, has to comply with the FAR as part of the subcontract. Therefore, the AGUNSA internal control system, as currently designed, is not adequate to ensure compliance with the terms and conditions of the subcontract with RPSC and the applicable FAR. This directly impacts AGUNSA's ability to accumulate, track, monitor, and bill subcontract costs to RPSC in compliance with NSF and Federal requirements.

AGUNSA must establish, implement and enforce policies and procedures that will meet the minimum requirements contained in the FAR. Also, periodic management reviews of its policies and operating procedures are needed to ensure AGUNSA's higher-level management, RPSC, and NSF that AGUNSA has correctly recorded, paid, and billed subcontract costs. The management reviews should also ensure that AGUNSA's policies

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and procedures remain current and consistent with its disclosed accounting practices and its FAR and RPSC contractual requirements.

***Recommendation No. 2:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Obtain an understanding of the applicable FAR provisions that AGUNSA is required to comply with under its RPSC subcontract, including the requirement to pay vendors within 30 days of invoice receipt and the prohibition of submitting claims to RPSC prior to making payments to its own vendors (in accordance with their terms).
- b) Revise written internal policies and procedures accordingly.
- c) Communicate the FAR requirements to appropriate management and accounting personnel.
- d) Design internal control procedures to monitor compliance with the procedures mentioned above using the COSO framework as a guide.

***Management's comments:***

“Our policy is a 30 days payment we have an automatic an centralize method of payment. Our bank allow us to pay 3 times in the month. When an invoice is recorded it takes 28 days for payment, but is has to wait the next bank payment date. The process would never take more than 40 days. The FAR was properly communicated to the personnel. We believe is not necessary in this point to use COSO for something so punctual.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 3: Inadequate Board of Directors Involvement in Internal Controls***

The AGUNSA Board of Directors agreed on July 30, 2003, to systematize and revitalize its internal audit procedures but has not monitored this process to ensure its implementation. To determine the extent to which the AGUNSA Board of Directors monitored the revitalization of internal audit procedures, we examined three areas discussed at a) through c) below.

- a) An extract from the AGUNSA Board of Directors' minutes, dated July 30, 2003, stated *"It is considered of vital importance that given the size, variety, and geographical dispersion of the company's activities, internal audit procedures must be systematized and revitalized, requesting as a consequence that management act in said direction."* This directive is consistent with the "monitoring" component of the COSO Internal Control Framework used in establishing or evaluating internal controls. Under this component, an organization is supposed to monitor its internal control system through ongoing monitoring and separate evaluations. However, we requested but were not provided with documentation indicating that this task has been accomplished.
- b) AGUNSA's administrative procedures manual states that "each decentralized agency (AGUNSA operates through 13 decentralized agencies in Chile) should be visited at least twice a year by the Internal Controls Unit." However, we requested but were not provided with documentation that these two visits occurred in 2004 at the Punta Arenas office or as of the date of our fieldwork in May, 2005. Also, the internal audit function, as it exists, does not comply with recognized internal audit practices as promulgated by the Institute of Internal Auditors<sup>4</sup> or a comparable professional audit organization. Specifically, AGUNSA's Internal Controls Unit lacks independence, as it reports directly to the Director of Administrative Operations. The Internal Controls Unit is very informal in terms of defining the scope, frequency, methodology, and execution of internal audit work. There is very little documentation on the review procedures that are performed during an internal audit. There are no formal written reports on the areas reviewed, the findings identified, or the corrective actions proposed, if any.
- c) In response to the embezzlement, the [REDACTED] of AGUNSA issued a list of corrective actions that were to be adopted to prevent future embezzlement opportunities and correct the associated internal control deficiencies. We requested but were not provided with a list of these corrective actions and, therefore, could not verify their existence or AGUNSA's compliance.

AGUNSA's monitoring of its internal control system, as currently designed, is not adequate to ensure compliance with the terms and conditions of its subcontract with RPSC and the FAR. This, coupled with the lack of monitoring by the AGUNSA Board, directly impacts the reliability of AGUNSA's system to accumulate, track, monitor, and bill subcontract costs to RPSC. AGUNSA's lack of a formal approach to internal control directly increases the risk of embezzlement recurrence.

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<sup>4</sup> Internet site is ([www.theiia.org](http://www.theiia.org))

***Recommendation No. 3:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Ensure that the AGUNSA Board of Directors make certain that the proposed corrective actions relating to compliance and control monitoring by AGUNSA's Internal Control Unit are implemented and followed.
- b) Consider having the Internal Controls Unit report directly to an Audit Committee of the AGUNSA Board, or similar governing body, and that the Unit follow standard internal audit practices, such as those promulgated by the Institute of Internal Auditors (I.I.A.)
- c) Perform semi-annual internal audits of its various branches as stated in its corporate policies and procedures.

***Management's comments:***

"The AGUNSA Board of directors instructs and monitoring through the CEO changes in the computer systems and the administrative, financial and internal control procedures to avoid this type of grafts. The actions were taken immediately, that why a follow up it was not needed. We agreed in that the audits should be made in periodic form are and especially in Punta Arenas in relation to RPSC will make the two audit minimum annually."

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

One of the key components described in the internal control guidance published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the standard for internal control for the U.S. Federal Government, is that of monitoring. Our recommendation refers to the monitoring of, and documentation of this monitoring, of Board of Directors decisions. The report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 4: Inadequate Segregation of Employee Duties***

AGUNSA lacks proper segregation of employee duties by continuing to concentrate a number of payment processing duties in the current Punta Arenas [REDACTED] position that are not significantly different than those of the previous Punta Arenas [REDACTED] who was removed from the position for embezzling funds. Therefore, this continuing concentration of duties in a single individual could allow future embezzlements to occur.

The [REDACTED]  
[REDACTED]. This condition enabled the [REDACTED] to manipulate the data entered into the central accounting system. The [REDACTED] was in collusion with his supervisor, the [REDACTED], who did not ensure payments were being made appropriately to vendors. Because the [REDACTED] colluded with the [REDACTED], the [REDACTED] signatory authority did not operate as an internal control safeguard on the proper recording and payment of invoices.

The Punta Arenas [REDACTED] did not exercise due diligence by co-signing checks that were not being written in accordance with Company policy, in particular the restrictions on the use of "open checks."

In October 2002, during the period of the embezzlement, AGUNSA changed its method of paying certain vendors by switching to "vale vistas"<sup>5</sup> instead of using individual checks. This process required the local Punta Arenas office to submit a list of the vendors to be paid by the AGUNSA central office in Valparaiso, accompanied with detailed information of which invoices were being paid. The Company's central office would then issue one check to the local Punta Arenas bank covering the amount of all the invoices, and the local AGUNSA office would submit to the local bank the list of specific vendors to be paid.

This process allowed the [REDACTED] and the [REDACTED] to continue alter the original vendor list (originally sent to the central office) and take an altered list to the local bank. This altered list allowed them to continue to perpetrate the embezzlement scheme, although the corporate records showed the payments had been made to the list of original vendors.

In addition to failing to follow Company policy relating to "vale vistas" by writing "open" checks to pay vendor invoices, the office in Punta Arenas also failed to comply with a Company policy that required all cash flow activity, including the use of the vale vista checks and invoices paid, and accounting records be reconciled and posted daily. In Punta Arenas, this policy was not enforced, and there were times when transactions were left "pending" or "not transmitted" until the month-end closing. This, too, was a factor in not detecting the embezzlement. A vendor check would be written on a certain date. The vendor would be notified of which invoices were being paid and would cash the check, but the [REDACTED] would wait until the end of the month to record the transaction, at which

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<sup>5</sup> Vale Vista is a process by which a company check is issued (or funds transferred) to a bank from which multiple vendors are paid.

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time he would show more recent invoices being paid than those detailed for the vendor. During the embezzlement period, as far as the central office was concerned, all vendor accounts were current and in compliance with the Company's 30-day payment policy.

In 2003, after the discovery of the embezzlement, AGUNSA properly made changes in the Company's invoice payment policy and procedures to require that most large vendors now be paid directly from the central office in Valparaiso by electronic payment transfers, thus avoiding potential modification of the list of invoices to be paid at the local office level. However, some payments are still made by check and cash at the Punta Arenas office, but these payments are treated as exceptions and must be approved by the finance department at Valparaiso. The checks are co-signed by the [REDACTED] who also reviews the bank reconciliations. To avoid collusion in the future, the Company also instituted a new procedure on vacation policies, which requires mandatory vacations. Whenever an employee takes a vacation, an employee from a different office is sent to assume the vacationing employee's job responsibilities. As of June 2005, this procedure governing vacations was being communicated verbally; however, it had not been incorporated into the Human Resources Manual.

However, these measures do not address the continued concentration of duties and unrestricted accounting system access in the [REDACTED] position. Poor segregation of duties directly impacts AGUNSA's ability to accumulate, track, monitor, and bill subcontract costs to RPSC and limit future reoccurrences of an embezzlement. The COSO methodology serves as a guide for an entity's control activities that relate to adequately designed policies and procedures that help ensure management directives are carried out. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties. Therefore, adequate segregation of duties, which are monitored and enforced, is a required element of control activities for an entity. Properly segregating the Punta Arenas staff duties will limit future opportunities for fraudulent acts by AGUNSA employees.

***Recommendation No. 4:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Revise Company policies as necessary to segregate the duties of the [REDACTED] such that processing, recording, and payment of vendor invoices are segregated among different staff to perform. Ensure that vendor checks are properly prepared, documentation properly supports each payment, accounting records are updated properly, and invoices are paid promptly in accordance with AGUNSA policies and procedures and the FAR. The amounts and payees of the invoices received should be reconciled to and agreed with the amounts and payees of the checks written for invoice payments, the amounts and payees of the checks cashed, and the amounts and payees recorded in the accounting records.
- b) Monitor compliance with all Company policies and procedures, especially with regard to the vendor payment process.

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- c) Mitigate fraud by collusion by monitoring compliance with its new vacation policy. The new vacation policy currently being communicated verbally should also be incorporated into the Human Resources manual.
  
- d) Perform unannounced spot checks to ensure compliance with company policies and procedures.

***Management's comments:***

“To assure the fulfillment of our administrative and financial policies, segregation of functions were made. Accompanied by the change of personal, vacation policy and the reinforcement of the internal control and the centralization of the payment of suppliers would allow to avoid a similar situation again.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 5: Inadequate Development and Implementation of Financial and Administrative Policies and Procedures Results in Inadequate Internal Controls***

AGUNSA has an informal process for communicating its procedures. AGUNSA does not have an updated, complete, or cohesive set of rules or manuals containing the operational, financial, and administrative procedures for its different functional areas and activities, including invoice processing. AGUNSA has developed various procedure manuals over a period of time, particularly in connection with operational activities and contract management, but the existing financial and administrative procedure manuals are general and incomplete. Also, while there is documentation with respect to internal controls, such documentation is either not well communicated, not complied with, or the employees are not trained in its use.

These deficiencies highlight an overall information and communications control weakness at AGUNSA. The COSO methodology for an entity's Information and Communication control component relates to pertinent information that must be identified, captured and communicated in a form and timeframe that enables people to carry out their responsibilities. Information systems produce reports containing operational, financial, and compliance-related information that make it possible to run and control the business. It includes such aspects as information systems, channels of communication and dissemination of information. However, AGUNSA's financial and administrative policies and procedures were incomplete and poorly communicated and monitored. As a result, AGUNSA cannot ensure compliance with the terms and conditions of its subcontract with RPSC and the applicable FAR. This directly impacts AGUNSA's ability to accumulate, track, monitor, and bill subcontract costs to RPSC in compliance with NSF and Federal requirements. AGUNSA's lack of a formal approach to internal control increases the risk of future embezzlements.

**Manuals and Procedures**

AGUNSA's procedure manuals are developed at the individual Unit Manager's initiative rather than as corporate policy. As a result, there is a lack of cohesiveness in the manuals. For example, in Punta Arenas there is an operations manual for the warehouse, which was developed by that Unit Manager; however, this operations manual is not necessarily used anywhere else in the Company. We also noted the following concerns with the written procedures and guidance:

- a) We were unable to establish which manuals were the most current as the various versions were not dated.
- b) There were no specific or detailed procedures for activities such as internal audit, disbursements, invoicing, cash register closing, etc.
- c) Employees carry out their tasks based on informal practices such as what has been done in the past, on e-mail messages that are sent by Company directors, or simply by following the steps provided by the financial information system.

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E-mail is the most popular form of communication at AGUNSA for circulating changes in financial/administrative procedures. These e-mails usually originate in the central units located at the central office. However, assimilating and implementing new procedures or change to existing policies and procedures is the sole responsibility of the employees. The Company relies on its employees to keep up, substitute with current versions, find, and use the most current updated versions of those e-mail communications.

AGUNSA implemented various corrective actions following the discovery of the embezzlement; however, it has not adequately documented those corrective actions (i.e. internal controls) in written policies and procedures; carried out any tests of the effectiveness of these new control policies and procedures or analyzed the risks associated with its operations relating to the RPSC subcontract, so that any additional controls could be effectively designed, communicated, implemented, and monitored.

***Recommendation No. 5:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Develop a comprehensive set of financial and administrative procedures (with regard to the RPSC subcontract) based on a control risk analysis;
- b) Specifically design internal control procedures to monitor compliance with the FAR and financial and administrative procedures mentioned above, using the COSO framework as a guide;
- c) Communicate and implement these procedures in the Punta Arenas office;
- d) Train all financial and administrative personnel on Company policies and procedures; and
- e) Periodically evaluate the effectiveness of its controls and analyze the risks associated with its operations, so that appropriate controls can be effectively designed (or modified) and monitored with regard to the RPSC subcontract.

***Management's comments:***

“We agree on this point and the policies and the financial and administrative procedures and the compliance with the FAR was communicated and implemented in Punta Arenas office and periodically monitored.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 6: Employees Insufficiently Trained About Internal Controls***

Subsequent to the discovery of the embezzlement scheme, AGUNSA did not provide sufficient formal training in Punta Arenas on financial and administrative procedures, ethical behavior, conflicts of interest, internal controls, or anti-fraud procedures. Therefore, the current internal control system is not adequate for AGUNSA to ensure compliance with the terms and conditions of its subcontract with RPSC and the applicable FAR. Inadequately trained employees directly impact AGUNSA's ability to accumulate, track, monitor, and bill subcontract costs to RPSC in compliance with NSF and Federal requirements. AGUNSA's lack of a formal approach to anti-fraud and internal control related training directly increases the risk of a future embezzlement.

Subsequent to the embezzlement, AGUNSA should have used the COSO methodology to train employees on financial and administrative procedures, the importance of internal controls, ethical matters and fraud prevention in the Punta Arenas office. In addition, under the COSO Framework, an organization should implement, measure and monitor the training necessary for its employees to perform their assigned responsibilities with competency and integrity.

However, our analysis of the educational programs presented at AGUNSA between 2003 and 2005 found that most of the educational programs were related to general matters, such as the use of the Internet, software applications (word processors, spreadsheets, etc.), English, etc. While there were some formal training sessions that were designed to review modifications in administrative or operational procedures, these programs were less frequent. Instead, AGUNSA trains its employees "on the job" with respect to administrative and operational procedures. In this regard, it is very common for key financial and administrative personnel to spend from six months to two years at the Finance and Administration Department in Valparaiso before they are sent to a branch elsewhere in Chile or abroad. However, it is not readily apparent that policies and procedures learned at AGUNSA headquarters in Valparaiso are translated into practical application in the branch offices.

***Recommendation No. 6:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC direct AGUNSA to:

- a) Provide employee training on financial and administrative procedures, with a particular focus on risks and associated controls;
- b) Provide adequate training on ethical behavior, resolution of conflict of interests, internal controls, and anti-fraud procedures;
- c) Establish more detailed ethical and anti-fraud procedures as well as periodic reviews of these procedures; and
- d) Conduct joint working/training sessions with RPSC on subcontract management as it relates to administrative and financial matters.

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***Management's comments:***

“We will trainee this year.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 7: Poorly Defined Employee Duties and Performance Evaluations***

AGUNSA lacks both written formal job descriptions for accounting and billing staff and a system of regular performance evaluations. Under the COSO Framework, an organization should implement, measure and monitor the existence of formal job descriptions. However, many employees do not have formal job descriptions. The [REDACTED] [REDACTED] told us, “formalizing job descriptions and functions in a document could limit what the employees do.” We found that some employees in the Punta Arenas accounting and warehouse offices have detailed written job descriptions that include general and specific job functions but many do not. Also, AGUNSA has not established a formal employee performance evaluation system for any of its Punta Arenas employees. Rather, employees are given performance evaluations through unscheduled ad hoc reviews or through assessments of departmental progress in relation to operational indicators.

In order for AGUNSA’s policies and procedures to effectively safeguard company assets and maintain efficient operations, employee duties must be clearly defined and employee performance of those duties evaluated and documented on a regular basis. Also, clearly defined employee duties help ensure proper segregation of responsibilities among employees by delineating the employees’ duties in, for example, reviewing, approving, and disbursing funds to pay vendor invoices. Segregating those duties is an important internal control. Management oversight, by evaluating employee performance against clearly defined duties is a safeguard that enhances the effectiveness of internal controls.

As a result of these weaknesses, the current internal control system is not adequate to ensure that accounting and billing staff know and are held accountable for meeting job performance expectations. This directly impacts AGUNSA’s ability to accumulate, track, monitor, and bill subcontract costs to RPSC in compliance with NSF and Federal requirements.

***Recommendation No. 7:***

We recommend NSF’s Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Define personnel responsibilities and conduct formal employee performance evaluations for all staff involved in the administration of the RPSC subcontract, and
- b) Provide training that supports and relates directly to employee job duties and responsibilities of staff working on and monitoring the RPSC subcontract.

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***Management's comments:***

“The personnel knows what their duties and responsibilities are, the company provide training.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 8: Need for Evaluation of Employee Assignments and/or Retraining.***

The [REDACTED] at the Punta Arenas office remains in his current position, despite not exercising adequate due diligence in co-signing checks associated with the embezzlement. Failure to adequately review the checks for compliance with AGUNSA's company policy before co-signing checks circumvented the internal control, and indirectly benefited the embezzlers, allowing them to convert AGUNSA funds to their own private use.

AGUNSA's policy requires that vendor payment checks be restricted for deposit in the payee's bank account. The two embezzlers modified the checks so that they could be transferred to the bearer of the check. Because one of the embezzlers also had authority to co-sign the checks, the [REDACTED] was AGUNSA's final safeguard to ensure that checks were prepared in accordance with company policy. Although the [REDACTED] was not implicated as a participant in the embezzlement, effectively performing his duties would have mitigated the loss of approximately \$157,000 to AGUNSA. The [REDACTED] did report the embezzlement scheme to AGUNSA management because a vendor complained to him and not because he detected any irregularities during his oversight or review of the checks presented to him for signature. The authority to sign and commit AGUNSA funds for payment carries with it significant responsibilities to safeguard the company's assets.

Other employees had various relationships with the embezzlers beyond that of a work colleague and remain in their current positions with the Company. These employees may either not have known, or had a responsibility to question, issues related to the ongoing embezzlement. These employees may have benefited indirectly (knowingly or unknowingly) from the embezzlement.

We understand AGUNSA has interviewed these individuals in this regard.

We have no knowledge that any of these individuals should, or did, have knowledge of the embezzlement, or whether they benefited either directly or indirectly from it. However, we believe that a prudent person may ask for additional information based on the facts presented to us.

***Recommendation No. 8:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure that RPSC directs AGUNSA to:

- a) Review the Punta Arenas [REDACTED] indirect involvement in the embezzlement in order to evaluate whether the [REDACTED] has had the retraining necessary to effectively discharge his control duties and continue in his current assignment.
- b) Ensure all Punta Arenas AGUNSA employees with check signature authority understand fully and properly execute their responsibilities in disbursing and safeguarding AGUNSA company funds.
- c) Obtain details of AGUNSA's assessment of other individual's direct or indirect involvement in the embezzlement.

***Management's comments:***

"The new organization in office included a new agent, who is responsible for processing and compliance the administrative and financial policies. attached current flowchart." (Attachment D) "There is not another person involved in the embezzlement."

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

After taking into consideration managements' response, our recommendation stands, however, the report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

***Finding No. 9: RPSC May Have Paid for Services Not Received***

AGUNSA was purchasing goods and services without RPSC [REDACTED] documentation, authorization and approval contrary to RPSC's subcontract which states that AGUNSA should require the "Review and payment of all local bills, properly rendered, receipted, and authorized by the RPSC [REDACTED], or [REDACTED], when practicable." In addition, there was limited documentation evidencing delivery of goods or services to RPSC. Without adequate invoice approval documentation and proof of delivery, there is a risk that payments could be made for goods or services that were not ordered and/or delivered.

When we discussed with AGUNSA personnel the possibility of invoicing RPSC for goods or services that might not have been provided, AGUNSA management said that RPSC would be able to detect if such an event had occurred. When we posed the same question to RPSC representatives, they responded that the ship's captain or the scientists would complain if requested goods or services were not provided. This is an external control that should not be relied upon by AGUNSA or RPSC.

According to AGUNSA officials, certain invoices cannot have authorization from RPSC because they are either not directly related to the vessel (laundry, garbage removal, etc.) or are general port-related services (mooring, pilotage, tug boat, health-sanitary inspection, etc.). Therefore, after removing these industry standard dockside service invoices from our tests, we nevertheless found that approximately half the invoices tested, during the embezzlement period, did not have proper RPSC [REDACTED] authorization. The absence of these controls pose significant risks of fraud and abuse to AGUNSA and RPSC.

***Recommendation No. 9:***

We recommend that NSF's Director of the Division of Acquisition and Cooperative Support ensure RPSC directs AGUNSA to:

- a) Establish internal control procedures to follow subcontract requirements to obtain proper documentation, authorization, and approval from the RPSC [REDACTED] [REDACTED] in Punta Arenas for all NSF ship specific invoices before submitting them to RPSC for payment.

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***Management's comments:***

“This point is not accepted, AGUNSA it never had acted against its represented, it is the agent's duty to look after the interests of its clients. However we want it clarifies what to related to is indicated:

- the vessel (laundry, garbage removal, etc.)

This service was request by the vessel and they had a copy of the certificate. (Attachment D)

- general port-related services (mooring, pilotage, tug boat, health-sanitary inspection, etc.).

These services have a support in arrival and sailing report and general declaration. The documents could allow estimate and check Port authority charges. If changes in these procedures are needed, please let us know.”

Also refer to Attachment D – Response from Agencias Universales S.A. (AGUNSA) for their general comments about the report findings and recommendations.

***PKF Witt Mares response:***

We did not find any evidence that AGUNSA paid for services that they did not receive, however, during our discussions with AGUNSA, we did observe that certain invoices and shipping documentation did not appear to contain appropriate authorization and/or approval. Therefore, our recommendation to establish internal control procedures to follow subcontract requirements to obtain proper documentation, authorization, and approval from the RPSC [REDACTED] in Punta Arenas for all NSF ship specific invoices before submitting them to RPSC for payment, stands. The report finding should not be closed until NSF determines that corrective actions have been satisfactorily implemented.

**SUPPLEMENTARY INFORMATION  
ATTACHMENTS**

## **ATTACHMENT A INTERNAL CONTROL ASSESSMENT SCOPE AND METHODOLOGY**

Our work has been carried out in accordance with Generally Accepted Government Auditing Standards (GAGAS). Specifically, we have referred to the internal control guidance published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

COSO provides a common definition of internal controls and guides in the creation, assessment and improvement of an organization's internal control systems.

The COSO report defines internal control as a process effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- **Effectiveness and efficiency of operations.** Addresses an entity's basic business objectives, including performance and profitability goals and safeguarding of resources;
- **Reliability of financial reporting.** Relates to the preparation of reliable financial statements, including interim financial statements, and selected data derived from such statements;
- **Compliance with applicable laws and regulations.** Deals with complying with those laws and regulations to which the entity is subject;
- A subset of these objectives is the **safeguarding of assets**. Internal control should be designed to provide reasonable assurance regarding prevention of or prompt detection of unauthorized acquisition, use, or disposition of an entity's assets.

Internal control consists of five interrelated components, **all of which must be present and functioning effectively** and connected to the entity's business objectives. Our internal control assessment of AGUNSA has included all five components, which are:

- **Control Environment.** Sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure. Control environment factors include the integrity, ethical values and competence of the entity's people, management philosophy and operating style, the way management assigns authority and responsibility, and organizes and develops its people, and the attention and direction provided by the Board of Directors;
- **Risk Assessment.** Identification and analysis of relevant risks to the achievement of the objectives, forming a basis for determining how the risks should be managed. A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent.

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- **Control Activities.** Policies and procedures that help ensure management directives are carried out. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties;
- **Information and Communication.** Pertinent information must be identified, captured and communicated in a form and timeframe that enable people to carry out their responsibilities. Information systems produce reports, containing operational, financial and compliance-related information, that make it possible to run and control the business. It includes such aspects as information systems, channels of communication and dissemination of information.
- **Monitoring.** Internal control systems need to be monitored – a process that assesses the quality of the system’s performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two.

Based on the *Internal Control Planning Document* agreed with NSF OIG, our fieldwork was carried out from May 9th to May 20<sup>th</sup>, 2005 at AGUNSA Headquarters in Valparaiso, Chile, and from May 26th to May 27<sup>th</sup>, 2005 at AGUNSA’s Office in Punta Arenas, Chile. The fieldwork included the following steps:

- **Gathering and Analysis of Key Information:** In order to understand and become familiar with AGUNSA’s internal controls documentation, we reviewed financial management, human resources and financial systems procedures, as well as internal management and financial reporting, financial audit reports, contract documentation, annual report, job descriptions, and all other relevant background documentation that was made available to us, such as the [REDACTED] and [REDACTED] Audit Report, the Chilean Police’s Economic Crime Unit Report.
- **Testing:** We tested controls on transactions for year 2005 including all relevant procedures involved on AGUNSA’s accounting and billing processes to Raytheon Polar Services Company (RPSC) in compliance with NSF and Federal requirements.
- **Interviews with Management and Staff:** We carried out interviews with relevant management officials and staff (Attachment C) as part of the internal control assessment.

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**INTERNAL CONTROL ASSESSMENT METHODOLOGY**

Components	Subcomponents
Control Environment	Integrity and ethical values Commitment to competence Management philosophy and operating style Board of directors/audit committee Organizational structure Human resources policies and procedures
Risk Assessment	Enterprise objectives Risk management
Control Activities	Policies and procedures Document and record management Payment process Bank reconciliations Segregation of duties Control over vulnerable assets
Information and Communication	Information Information systems Communication
Monitoring	Continuous supervision External audit Internal audit

Each of the subcomponents is tied to one or more of the evaluation criteria. Thus, for instance, the Subcomponent “Commitment to Competence,” which belongs to the Control Environment Component, is composed of the following four evaluation criteria:

- (1) Are there formal job descriptions or any other form of describing the tasks related to any particular function?
- (2) Are employees provided with the training necessary to perform their assigned responsibilities?
- (3) Is employee competence ensured through performance evaluation?
- (4) Are the key personnel in accordance with the job description profiles?

In our report, we have evaluated AGUNSA’s internal controls using 31 criteria associated with 20 subcomponents, which in turn are linked with the five COSO components. Our criteria was selected to focus mostly on AGUNSA’s accounting and billing processes. (See Attachment B - Internal Control Assessment)

**ATTACHMENT B**  
**INTERNAL CONTROL ASSESSMENT**  
**COMPONENTS/SUBCOMPONENTS/FACTORS**

***COMPONENT 1: CONTROL ENVIRONMENT***

**1.1 INTEGRITY AND ETHICAL VALUES**

- 1.1.1 Are there written communications or a Code of Conduct to document the entity's values, norms, and acceptable ethical behavior, conflicts of interest, etc.? If no such written document exists, does the organizational culture emphasize the importance of integrity and ethical behavior through management actions, verbal communications, group sessions or personal interviews?

*PKF Witt Mares' Comments:* AGUNSA does not have a Code of Conduct. It does have an Internal Regulation on Security, Hygiene, and Order which contains some provisions on ethical behavior. During our assessment, we observed the importance of ethical behavior and trust placed on the management and key employees in the Company. We also observed a lack of control activities in this regard. There are still several employees that were indirectly involved in the embezzlement at Punta Arenas that are still employed with the Company.

- 1.1.2 Are the written communications or Code of Conduct communicated adequately to the staff and are they in use?

*PKF Witt Mares' Comments:* The Internal Regulation on Security, Hygiene, and Order is given to each employee at the time they join the Company. However, no further training or ethical awareness programs are provided. No action in this regard was taken with the Punta Arenas employees after the embezzlement.

**1.2 COMMITMENT TO COMPETENCE**

- 1.2.1 Are there formal job descriptions or any other form of describing the task related to any particular function?

*PKF Witt Mares' Comments:* Few areas have formal job or task descriptions. There is no systematic approach to documenting procedures. The employees at the warehouse in Punta Arenas who deal with the Raytheon contract are among the few who do have a job description manual.

- 1.2.2 Are employees provided with the training necessary to perform their assigned responsibilities?

*PKF Witt Mares' Comments:* Improvements could be made through a systematic approach to training based on needs identification and career development. After the embezzlement, the Company should have implemented Company-wide training programs on ethical behavior and administrative and financial procedures, especially in the Punta Arenas office.

1.2.3 Is employee competence ensured through performance evaluation?

*PKF Witt Mares' Comments:* There is no formal performance evaluation system. From time to time, AGUNSA's employees are evaluated against operational indicators.

1.2.4 Are the key personnel in accordance with the job description profiles?

*PKF Witt Mares' Comments:* As mentioned in point 1.2.1 above, many areas or positions do not have formal job description profiles.

### **1.3 MANAGEMENT PHILOSOPHY AND OPERATING STYLE**

1.3.1 Is there personnel turnover in key functions, e.g., operating, accounting, data processing, internal audit?

*PKF Witt Mares' Comments:* AGUNSA is a company with low personnel turnover. Many of the people interviewed in key positions have been with AGUNSA for more than ten years.

1.3.2 Level of importance and use given by management to financial and operational information?

*PKF Witt Mares' Comments:* AGUNSA produces complete and detailed monthly and quarterly financial and management reports that allow for monitoring of key business indicators.

1.3.3 Frequency of interaction between senior management and operating management, particularly when operating from geographically removed locations. Delegation levels.

*PKF Witt Mares' Comments:* AGUNSA is highly decentralized. Each of the 13 agencies has its own management structure, where the General Manager for that Agency has the authority to make decisions on day-to-day operations. All agencies report to the Director of Agencies and Port Logistics.

1.3.4 How are strategic and operational plans formulated, communicated, and monitored?

*PKF Witt Mares' Comments:* Within the Administrative Operations Division, each area formulated its proposed activities and goals for the year, which are shared and adjusted by the Director of Administrative Operations. The Director monitors progress on each of the proposed activities by area using a spreadsheet containing: area, indicator, task, resources, responsibility, deadline, degree of completion, etc.

1.3.5 Do senior managers exercise adequate leadership?

*PKF Witt Mares' Comments:* The executive staff (or principal management team) is composed of seven individuals who have been with AGUNSA for several years. The

executive staff has failed to establish a formal control structure, has failed to implement an effective internal audit function, and has failed to provide formal ethical and fraud training.

#### **1.4 BOARD OF DIRECTORS/AUDIT COMMITTEE**

1.4.1 Is there a Board of Directors, independent from management, that provides oversight on the Company's results and the internal controls? Is there an audit committee supervising key financial activities or results?

*PKF Witt Mares' Comments:* The Board of Directors is composed of seven directors, none of whom are on the executive staff. A Director's Committee was set up in 2002, in accordance with Chilean law. This Committee is responsible for the supervision of financial activities, external auditing, compensation, etc. Following the embezzlement at the Punta Arenas office, the Board met on July 30, 2003, and agreed to strengthen and systematize AGUNSA's internal controls. However, we were not provided with any evidence that the Board is monitoring internal controls.

#### **1.5 ORGANIZATIONAL STRUCTURE**

1.5.1 Appropriateness of the entity's organizational structure, and its ability to provide the necessary information flow to manage its activities. Adequacy of definition of key managers' responsibilities, and their understanding of these responsibilities.

*PKF Witt Mares' Comments:* AGUNSA operates a financial administration computerized system which connects the operations of all agencies to headquarters. This facilitates the supervision of administrative and financial operations carried out from the central units (finance, internal controls, accounts receivable, accounting). Each agency is managed by a general manager (agent) who has operations and administrative/finance staff under his authority. Each general manager (or agent) reports to the Director of Agencies and Port Logistics, who is based in Santiago. We found that responsibilities and tasks are not always clearly defined.

#### **1.6 HUMAN RESOURCES POLICES AND PROCEDURES**

1.6.1 Extent to which policies and procedures for hiring, training, promoting, and compensating employees are in place.

*PKF Witt Mares' Comments:* AGUNSA's Human Resources Policies and Procedures Manual refers in a general manner to how to hire, train, promote, and compensate the employees.

## **COMPONENT 2: RISK ASSESSMENT**

### **2.1 ENTERPRISE OBJECTIVES**

2.1.1 How are strategic and operation plans formulated, communicated, and monitored?

*PKF Witt Mares' Comments:* AGUNSA does not have a formal enterprise risk management methodology.

### **2.2 RISK MANAGEMENT**

2.2.1 Thoroughness and relevance of the risk analysis process, including risk identification and estimating the significance of risks, assessing the likelihood of their occurring and determining needed actions.

*PKF Witt Mares' Comments:* AGUNSA has not established a systematic manner of analyzing risks, including the identification and evaluation of the significance or likelihood of their occurrence. This means that AGUNSA does not have a risk management system in place that would increase the possibilities of achieving the activity- level and company-level objectives.

### **COMPONENT 3: CONTROL ACTIVITIES**

#### **3.1 POLICIES AND PROCEDURES**

3.1.1 Existence of appropriate policies and procedures necessary with respect to each of the entity's activities.

*PKF Witt Mares' Comments:* AGUNSA lacks a systematic approach toward documenting its procedures. There are many operational procedures manuals, but most of them have been developed at a Unit Manager's own initiative. There is no clear Company policy for development, maintenance, or dissemination of overall procedures. The financial/administrative related procedures manuals are too general and incomplete. Many of the new procedures or updates related to payments, invoicing, accounting, etc., are sent only by email. There are no procedures related to internal auditing.

#### **3.2 DOCUMENTATION AND RECORD MANAGEMENT**

*PKF Witt Mares' Comments:* We observed adequate archive and documentation management systems at both AGUNSA's headquarters and the Punta Arenas office.

#### **3.3 PAYMENT PROCESS**

3.3.1 Verify whether vendor payments were done in accordance with RPSC subcontract terms and conditions.

*PKF Witt Mares' Comments:* Vendor payments are not done in accordance with subcontract terms and conditions.

3.3.2 Verify invoice documentation, authorization, and approval.

*PKF Witt Mares' Comments:* Vendor invoices are not always appropriately documented, authorized, and approved.

3.3.3 Verify the accuracy and timeliness recording of transactions.

*PKF Witt Mares' Comments:* Transactions are accurately but not timely recorded.

#### **3.4 BANK RECONCILIATION**

3.4.1 Verify all monthly bank reconciliations for 2005 and that they are prepared and authorized adequately.

*PKF Witt Mares' Comments:* At Punta Arenas, bank reconciliations are prepared by the [REDACTED], and reviewed and approved by the [REDACTED]. They are sent monthly to the central office in Valparaiso.

### **3.5 SEGREGATION OF DUTIES**

3.5.1 Verify that there is an adequate segregation of duties.

*PKF Witt Mares' Comments:* For a company the size of AGUNSA, the segregation of duties at Punta Arenas is inadequate. The [REDACTED] continues to have access to the accounting system's accounts payable module and cash disbursements.

### **3.6 CONTROL OVER VULNERABLE ASSETS**

3.6.1 Verify controls implemented to safeguard its assets.

*PKF Witt Mares' Comments:* The controls to safeguard assets in Punta Arenas continues to be inadequate. For example, cash payments (i.e. currency) continue to be made by the [REDACTED] with minimal management oversight.

## **COMPONENT 4: INFORMATION AND COMMUNICATION**

### **4.1 INFORMATION**

4.1.1 Verify that accounting records are updated and duly authorized.

*PKF Witt Mares' Comments:* Accounting records are not always duly authorized.

4.1.2 Adequacy of obtaining external and internal information, and provide management with necessary reports on the entity's performance relative to establish objectives.

*PKF Witt Mares Comments:* The [REDACTED] did not have knowledge of FARs. Following applicable FAR regulations was an established objective of the contract with RPSC.

### **4.2 INFORMATION SYSTEMS**

4.2.1 Adequacy of the accounting system to provide updated, secure, accurate, and complete financial information.

*PKF Witt Mares' Comments:* Not adequate

### **4.3 COMMUNICATION**

4.3.1 Adequacy of communication across the organization and the completeness and timeliness of information and its sufficiency to enable people to discharge their responsibilities effectively.

*PKF Witt Mares' Comments:* The [REDACTED] did not know about the FAR, and therefore could not communicate FAR requirements to the staff.

## **COMPONENT 5: MONITORING**

### **5.1 CONTINUOUS SUPERVISION**

5.1.1 Are management and process indicators adequately monitored by key personnel?

*PKF Witt Mares' Comments:* The Board of Directors has not monitored the internal control measures it promulgated after the embezzlement at Punta Arenas.

### **5.2 EXTERNAL AUDITING**

5.2.1 External Audits

*PKF Witt Mares' Comments:* AGUNSA's financial statements have been audited quarterly and annually by Ernst & Young since 2004, after many years with PriceWaterhouseCoopers. The reasons given for the change was cost and for a change.

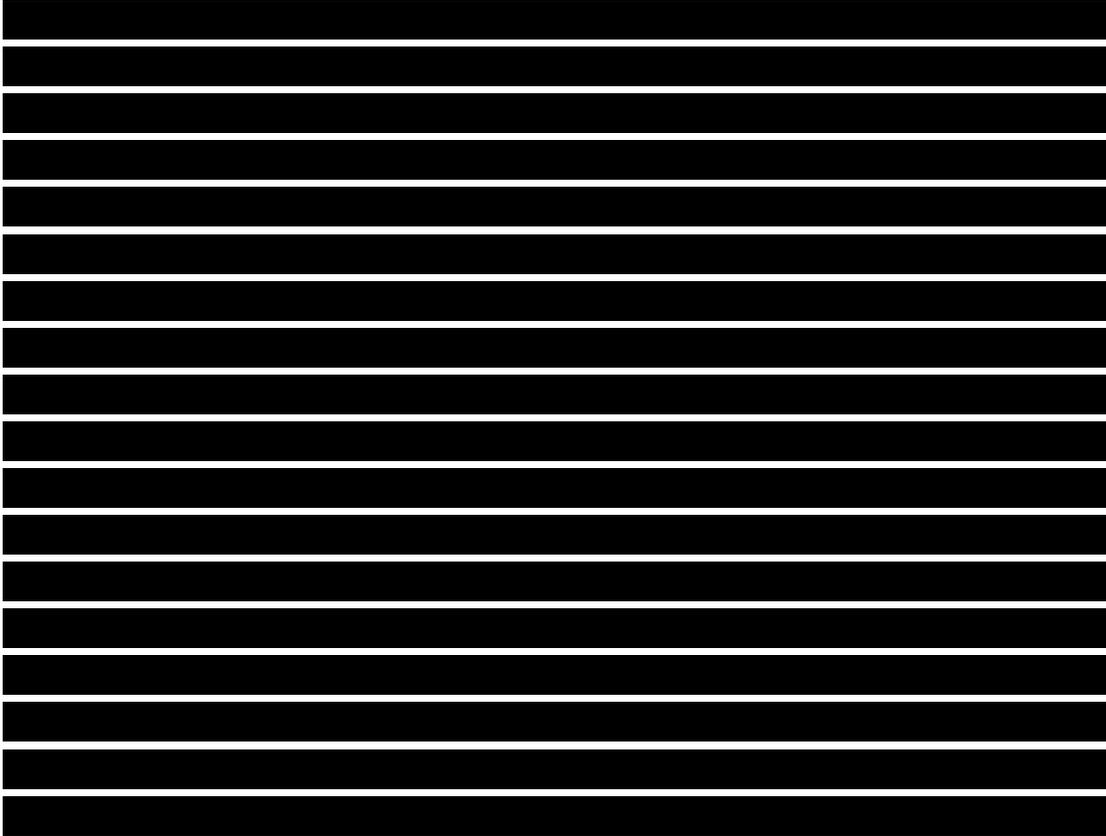
### **5.3 INTERNAL AUDITING**

5.3.1 Internal Auditing

*PKF Witt Mares Comments:* AGUNSA has a specific mandate from its Board of Directors to improve and systematize its internal controls. This mandate has been effectively ignored. At the time of our analysis, AGUNSA's internal audit procedures had not been systematized nor revitalized. AGUNSA lacks a formal approach to internal control, which impacts directly on the risk of embezzlement recurrence. AGUNSA's Internal Controls Unit is very informal in terms of defining the scope, frequency, methodology, and execution of the internal audit work. There is very little documentation of the review activity since there are no formal written reports of what has been reviewed, what the findings were, and what actions will be taken, by whom, and when. No specific testing is conducted in order to verify compliance with specific controls or key procedures. AGUNSA does not have a monitoring system in place to check the status of implementation of corrective actions identified during previous reviews.

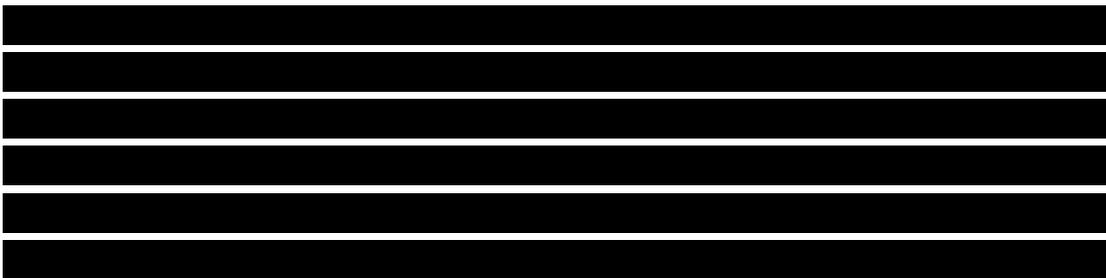
**ATTACHMENT C**  
**LIST OF INTERVIEWEES**

We conducted interviews with the following AGUNSA personnel:



A table with 18 rows, all of which are completely redacted with black bars, obscuring the names and details of the AGUNSA personnel interviewed.

We also interviewed the following non-AGUNSA personnel:



A table with 6 rows, all of which are completely redacted with black bars, obscuring the names and details of the non-AGUNSA personnel interviewed.

**ATTACHMENT D**  
**RESPONSE FROM AGENCIAS UNIVERSALES S.A. (AGUNSA)**

**From:** [REDACTED] [mailto:[REDACTED]]  
**Sent:** Thursday, March 15, 2007 6:30 PM  
**To:** [REDACTED]  
**Cc:** dcureton@nsf.gov; [REDACTED]  
**Subject:** RE: Internal control and Embezzlement report

[REDACTED]

Please find enclosed our comments about yours reports

Regards

[REDACTED]

PKF Witt Mares, PLC  
FAIRFAX, Virginia  
Att: [REDACTED], ACA, CGFM, CPA, CFE  
[REDACTED]

On Monday March 5, 2007, we received by email two reports prepared by PKF UIT Mares for NSF: Internal Control Report and Embezzlement Report. Both reports respectively cover the fraud happened in our signature in Punta Arenas during the period of 2002 and first six months of 2003, just like the state of our internal controls to the date of the investigation made by PKF Witt Mares between March and May 2005. PKF Witt Mares has giving us until March 16<sup>th</sup>, 2007 to make commentaries about both reports, if we want those commentaries added to the reports.

Do to the short time given to answer, the long period passed between the fraud and the investigation, and the fact that in our opinion the most relevant observations made in the reports had already surpassed, we now proceed to make a General Statement about the case covered by the reports:

1. Agunsa is committed on providing outstanding quality services to NSF throughout its contract with Raytheon. That is how is been done uninterruptedly from the beginning of the contract in the year XXXX until today. Throughout the period of the contract, it had done the necessary adjustments to the operative and administrative procedures with the intention of giving a better service, always-previous agreement with Raytheon.
2. Agunsa is proud of promoting transparency as one of its fundamental values. From the moment the fraud was discovered by us, we immediately informed Raytheon about the facts, taking the necessary measures: to restitute the funds to all the defrauded parts, to dismiss and to process the people responsible for the fraud, and to correct the possible operative and administrative faults. To this date we can confirm that :

Agencias Universales S.A. Internal Control Report  
For the Period January 1, 2005 to May 15, 2005

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- Just as it is indicate in the report, Independent accountants review report in the actual revision indeed of the amounts only involved \$7.200 were related to the RPSC and they were not affected
- Additionally this is effective it was never incurred in a lost one economic neither NSF stops neither RPSC stops
- All the defrauded parts indeed were restituting from the funds owed respectively.
- The responsible employees were fired and Agunsa filed a legal complain against them. These employees have done provisional jail time, failed against them recently, being in an appeal process. Our lawyers keep working in the case until they obtain the maximum possible pains for the responsible.
- Since the discovery of the fraud, we have implemented numerous measures to fortify our internal controls and to try to prevent that an incident of this type happens in our firm again.

The main measures taken include:

- i. Complete reorganization of the Punta Arenas Agency. Flowchart attached.
  - ii. The different activities properly separate operative and administrative functions.
  - iii. Greater supervision and pursuit on behalf of the central office by the internal audit unit, finances department and accounting department. This includes the centralized control of payments, revision of the registration of the invoices and their cost and their payment.
  - iv. Clear definition of procedures and employee duties.
3. Although we did not share some precise conclusions of the reports, in general we agree with them.

We agree in the way you describe how of the fraud was made, describing in detail how it was operated to commit the fraud and the amount of it (embezzlement report).

In the other report (internal control report), a series of weaknesses of internal controls are indicated, so are their respective recommendations for the improvement of them. We appreciate those recommendations, most of which have already been implemented.

However, we cannot accept the points 3 and 9 indicated in the internal controls report.

The points 3 indicate that the directors did not make the supervision of the changes in the systems and procedures. That is not correct; the instruction was given and completed immediately, that why it was not needed another action by the board.

Agencias Universales S.A. Internal Control Report  
For the Period January 1, 2005 to May 15, 2005

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The point 9 neither are acceptable since Agunsa as Agent has a primordial duty we should be diligent, look after the interests of all our represented. AGUNSA has never charged a non-received service, the point it should not been put in the report and it is not acceptable.

4. To finish, we want to declare that this fraud was a very isolated event, unique in the history of our company. Collusion of two key employees and with many years working for Agunsa was one of the main causes by which we didn't identify the problem previously, managing to elude the internal controls of the company. This case improves our internal control, and allows us to improve our procedures.

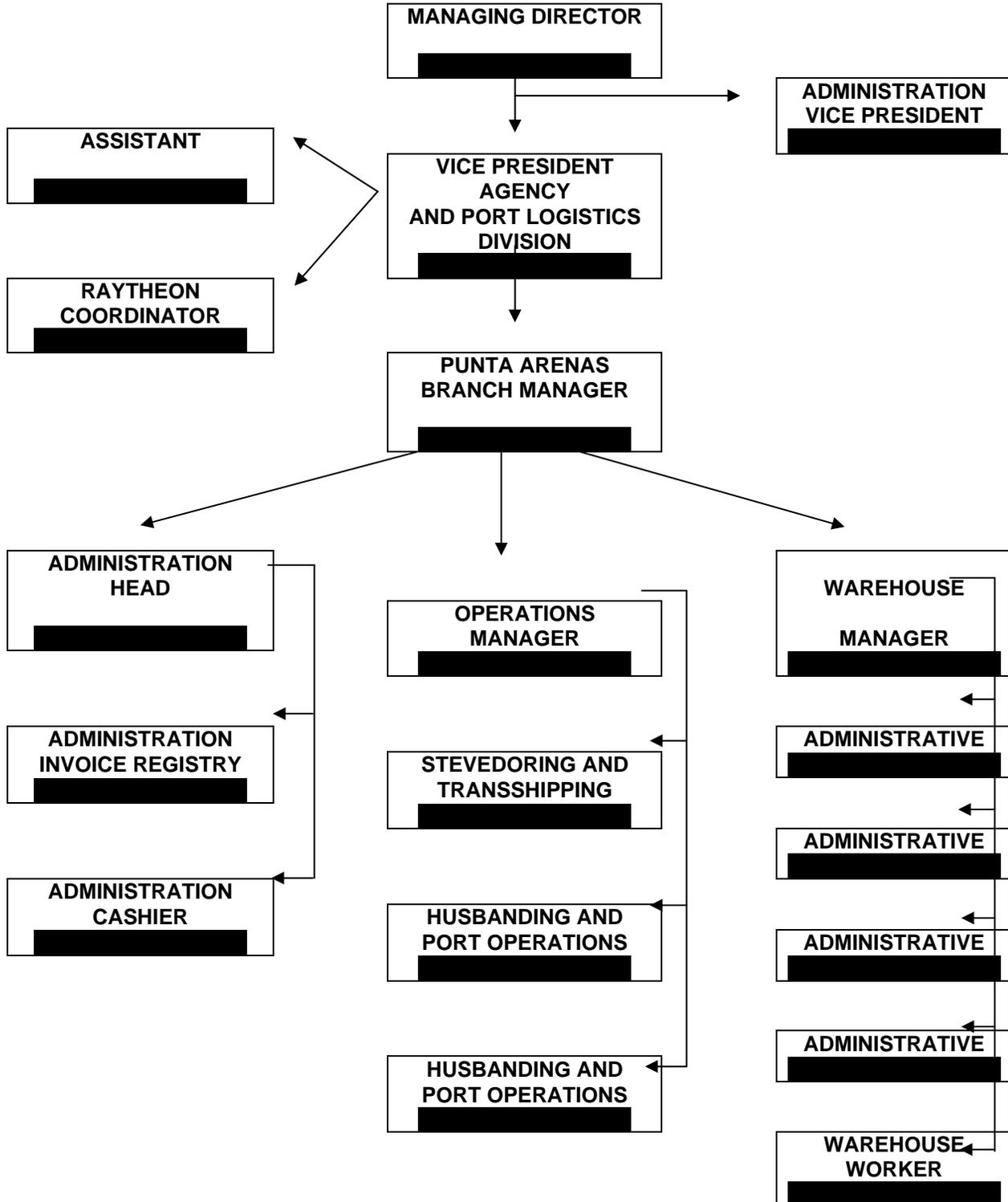
We hope that this incident had clarified, and reiterate to NSF our commitment with the quality and the transparency, and we are open to continue collaborating with the intention of providing the best possible service.

Our best regards,

, AGUNSA



### General organization for Raytheon Contract



Agencias Universales S.A. Internal Control Report  
For the Period January 1, 2005 to May 15, 2005

At Punta Arenas, Chile, JANUARY 1th . 2007

CERTIFICATE

We certify that regarding following trash picked up from ARSV R/V [REDACTED] was disposed at [REDACTED] spill are authorized by Chilean Government in order to comply Chilean law:

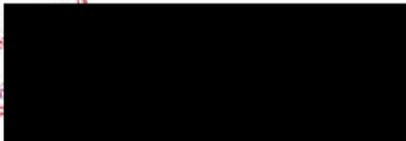
DATE	TRASH TYPE
DECEMBER 27th TO JANUARY 1th	INORGANIC TRASH FROM LMG06-14
	26 M3



Areas Verdes Ltda.  
Punta Arenas, Chile



AREAS VERDES  
Fono (061) 211956 F.  
Mardones 220 - Caleta 1227  
Punta Arenas - CHILE



Areas Verdes Ltda. - Enrique Abello N° 03170 - Fonos (61)211956 (61) 238278 - Fax (61) 210021 - Punta Arenas - Chile  
e-mail averdes@pntelchile.net

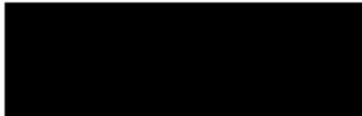
Agencias Universales S.A. Internal Control Report  
For the Period January 1, 2005 to May 15, 2005

At Punta Arenas, Chile, FEB. 16, 2007

**CERTIFICATE**

We certify that regarding following trash picked up from ARSV R/V [REDACTED] was disposed at [REDACTED] spill are authorized by Chilean Government in order to comply Chilean law:

DATE	TRASH TYPE
FEB. 11 TO FEB. 16 / 2007	INORGANIC TRASH FROM L.M.G. 19,5 M3



Areas Verdes Ltda.  
Punta Arenas, Chile

  
AREAS VERDES  
Fono (061) 211956 F.  
Mardones 220 - Casilla 1227  
Punta Arenas - CHILE



Agencias Universales S.A. Internal Control Report  
For the Period January 1, 2005 to May 15, 2005

At Punta Arenas, Chile, 08 MARCH

2007

**CERTIFICATE**

We certify that regarding following trash picked up from ARSV R/V [REDACTED] was disposed at [REDACTED] spill are authorized by Chilean Government in order to comply Chilean law.

DATE	TRASH TYPE
FROM MAR. 01 TO MAR.08/2007	INORGANIC TRASH FROM LMG.
	19,5 M3



Areas Verdes Ltda.  
Punta Arenas, Chile

AGENCIAS UNIVERSALES S.A.  
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