

The framework of this report is presented below case study example

[Business](#), [Company](#)



Executive Summary

One Tel Communications was the fourth largest telecommunications company in Australia. It touches on matters regarding poor management, fraudulent misstatements, the use of remuneration packages for self-interest and lack of regard of accounting policies and legal regulations. These, together with other factors, have led the company to liquidation in 2001. This report summarizes the key facts from the start of the company business, its capital structure, the people involved in the accounting scandal, the auditing scenario, factors that contributed to the business failure, the audit risks existing at that time, to the conclusion and possible audit procedures that should have uncovered the internal problems and saved the company from its eventual collapse.

Brief Introduction of the Organisation

Key People of One Tel

Share Capital Structure

Business History and Remarkable Achievements

The Final Auditor

Factors of the Business Failure

People Responsible to the Demise of One Tel

Audit Risks

Conclusion

What I Could Have Done

Brief Introduction of the Organisation

One Tel was a telecommunications company in Australia which was started

by John Rich and Brad Keeling on May 1995. The company sought to provide services to the public in such a way that ordinary people could understand. It mainly operated in three business lines: Internet subscription, wired long distance telephone, and cellular services. It was at one time the fourth largest Australian company in the telecommunication industry (Monem, "The One-Tel Collapse: Lessons for Corporate Governance").

Aside from Australia, One Tel also established businesses in other countries including Netherlands, United Kingdom, Switzerland, France, Hong Kong and Germany. It was funded by the Murdoch and Packer families and in its early years, was linked to Optus - one of the biggest telecommunications company in Australia (Carnegie et. al., "Accounting scandals in Australia since the late 1980s").

With success from the young generation, One Tel grew quickly over Europe. By the end of 1998, the founders Rich and Keeling, together with Alicia Crisp and Stephen More, had already developed Project GSM which would later on become the groundwork for the Mobile Virtual Network Operator (MVNO). Through that, One Tel would be able to provide their services for customers outside Australia without having to own the telecommunications infrastructure from which the services will be provided (Avison, "Information Systems Failure Explained Through the Lens of the Cultural Web").

In March 2000, One Tel officially released its Next Generation Network which was considered a state-of-the-art offering for any Australian telecommunications company at that time. The period from 1998 to 2001 marked a great success for the company with their revenues doubled and the number of One Tel subscribers tripled (One Tel, "Annual Report 2000").

Key People of One Tel

- John Rich

- Co-founder of One Tel, Joint Managing Director (CEO), Board of Directors-member

John Rich was responsible for regularly briefing the board members before their meetings and was a major influence in altering the views of the board members about the performance of One Tel (Monem, “ The One-Tel Collapse: Lessons for Corporate Governance”). He was the founder of one of Australia’s biggest information technology firm, Imagineering Telecommunications, in 1980. He has extensive knowledge in molecular biochemistry and nanotechnology. He is a graduate of The Wharton School under a Senior Executive Program. (One Tel, “ Annual Report 2000”).

- Brad Keeling

- Co-founder of One Tel, Joint Managing Director (CEO), Board of Directors – member

One of Brad Keeling’s responsibilities was to preside over the board meetings (Monem, “ The One-Tel Collapse: Lessons for Corporate Governance”). He was also the co-owner of Kalara Investments, together with John Rich, which held 50% ownership of One Tel.

He had practical training in business management and marketing. He served as the National Marketing Manager and later on, the General Manager of Imagineering Telecommunications until 1991. (One Tel, “ Annual Report 2000”).

- Kevin Beck

- Executive Director

Kevin Beck joined One Tel in 1995 as the Operations Director. Prior to working for the company, he served as the company secretary for Imagineering Telecommunications.

He has numerous experiences in the finance industry and a member of the Institute of Chartered Accountants of both South Africa and Australia. (One Tel, “ Annual Report 2000”).

- Rodney Adler

- Non-executive director, and CEO of FAI (holds 18% ownership of One Tel)

Rodney Adler made the connection for the One Tel founders to seek the investments of the Packer and Murdoch families. He was the director of HIH, which was the 2nd biggest Australian insurance provider that collapsed shortly after the demise of One Tel in 2001 (Cook, “ Collapse of Australia’s Fourth Largest Telco Adds To Growing List of Corporate Failures”).

He is a graduate of the University of New South Wales and holds a Masters degree in Economics. He is also a member of the Institute of Chartered Accountants in Australia. (One Tel, “ Annual Report 2000”).

- John Greaves

- Chairman of the Board of Directors, Chief Financial Officer of Optus

John Greaves has a close relationship with both founders and presided the majority of One Tel’s board meetings (Monem, “ The One-Tel Collapse: Lessons for Corporate Governance”).

- Mark Silbermann

- Financial Director, Secretary of the Company

Mark Silbermann has had experiences in the areas of Operations and Finance having worked for Cluttons London Residential Agency as a Finance Director.

He is also a member of the Institute of Chartered Accountants of South Africa (One Tel, “ Annual Report 2000”).

Since being employed with One Tel in February 1996, he has expressed only occasional viewing of the company’s accounting records and as a result, discrepancies were not detected (Monem, “ The One-Tel Collapse: Lessons for Corporate Governance”).

Share Capital Structure

In its 2000 annual report, One Tel published their consolidated balance sheet that reflected a heavy reliance on internally generated funds with equity instruments. The issuance of One Tel stocks proved crucial and played a major role as a source of capital than debt instruments. The following information indicates the significant transactions related to their capital structure through the years (One Tel, “ Annual Report 2000”):

- Debt Instruments

In October 1998, the company issued notes amounting to A\$10, 000, 000. The notes carried a conversion feature for the ordinary shares of the company with a conversion factor of 3. 125. By December 2000, the notes worth A\$4, 900, 000 were converted to One Tel’s stocks. The remaining notes were supposed to mature on October 2001.

The company also issued foreign currency notes on December 24, 1998. The notes amounting to US\$30, 000, 000 were completely converted to One Tel’s ordinary shares in 2000. Otherwise, these notes were set to mature four years from the date of issue .

- Equity Instruments

The company has issued shares worth AUD\$84, 000 to John Rich on July 7,

1999. This was issued in in relation to the exercise of stock options previously received by the founder on July 15, 1996.

On August 1996, the company also issued 33, 333, 330 One Tel shares worth AUD\$500, 000 to Lifecell, a company associated with John Rich. This was in connection with previously issued stock option on January 1997.

The conversion of the US\$30, 000, 000 was issued to Gilbert Global Equity Partners on December 1999. The following month, 166, 666, 667 shares were issued to Leteno, a company under News Limited which is controlled by the Murdoch family. Employees also exercised their share options and others stocks were issued to comply with institutional placements. As of June 2000, Publishing and Broadcasting Limited also made direct investments in the ordinary stocks of One Tel amounting to AUD\$710, 000, 000.

- Sale of Assets

The company has entered into numerous sale and leaseback transactions worth AUD\$19, 200, 000 of their property, plant and equipment. One Tel also sold investments for AUD\$1, 600, 000. There were no sale of assets in 2000 and both transactions were made in the previous year.

Business History and Remarkable Achievements

- Before the collapse of the company, One Tel was actually the fourth largest telecommunication services provider in Australia. It started out as a GSM reseller of Optus and after gaining a considerable amount of customer base, expanded its operations to several countries in Europe (Cook, " Collapse of Australia's Fourth Largest Telco Adds To Growing List of Corporate Failures").

- In the United Kingdom alone, it was the second leading long distance

telephone company for the residential market. The first being the local British Telecom (One Tel, “ Annual Report 2000”).

- One Tel was the first in Australia to provide its customers with new mobile features such as Voicemail with Reply Now, and Cool Services which provides content on demand related to sport, finance, news, TV guides, and movie screenings. In addition, they also revolutionized the cellular industry by being one of the first few to provide the Wireless Application Protocol, Smart SIM, Mobile Data, 3G, EDGE, GPRS in the Australian Market (One Tel, “ Annual Report 2000”).

- On November 1999, One Tel made the list to the Top 30 largest companies in Australia shortly after the announcement of a major investment of to their European mobile market (Monem, “ The One-Tel Collapse: Lessons for Corporate Governance”).

The Final Auditor

The last auditor of One Tel before it the company collapsed in 2001 was BDO Nelson Parkhill. BDO is the largest auditing firm in Australia and the fifth biggest in the world. The company audited the financial statements of One Tel from 1997 to 2000. BDO Partner, Stephen La Greca, signed the last annual report on September 11, 2000 (Barry, “ One. Tel's Cash SOS, Then It All Fell Apart”). By 2001, the One Tel changed their auditor to Ernst & Young, the auditor of companies controlled by the Packer family.

Factors of the Business Failure

The accounting issues of One Tel that led to its failure were largely related to the company’s overcapitalization, overtrading, and marketing. One Tel is guilty of inadequate credit inspections for new subscriptions and had very

low provision for doubtful accounts. In addition, the company has overstated its spectrum licenses by \$500, 000 which was overpriced ten times than that from other competitors. They also understated their expenses by capitalizing an advertising cost worth \$90, 000, 000 (Carnegie et. al., “ Accounting scandals in Australia since the late 1980s”).

Financial reporting of the company was not free from errors. Mark Silbermann and John Rich expressed that they rarely see the trial balances, monthly report, spreadsheets, journals, ledgers and other accounting records related to the operations of One Tel. They also did not have real-time, updated information for the assessment of ageing, and debtors for the collection of customer accounts. They also had excessive accrual of revenues from 1998 – 1999 resulting to positive earnings when their counterparts Optus and Hutchinson reported negative accruals.

The chairman of the Board of Directors was not always present to preside over the board meetings. Out of ten meetings in the past two years before its collapse in 2000, John Greaves presided only four of them. John Rich, Mark Silbermann, and Brad Keeling handled the rest of the meetings. As such, the conflicting responsibilities of the CEOs and the chairman were not clearly delineated and were in violation of the good governance guidelines by the Australian Securities Exchange (ASX). Moreover, the discussions during the board meetings intentionally excluded amounts unavailable for One Tel’s general operations and cheques that were not handed over. Also, the non-executive directors of the company should not have been qualified as an independent director from the ASX recommendations since they had significant ownership interests in One Tel. The board members had little

independence in decision-making because the company's founder, John Rich, would conduct briefings regarding their performance and influence their votes.

There are also evidences related to excessive compensation and remuneration of the company executives particularly those given to the Brad Keeling and John Rich. From 1998 to 1999 alone, the founders received a combined AUD\$2, 300, 000. The directors also received a total of AUD\$15, 500, 000 from 1999 to 2000 with the large sum of AUD\$13, 800, 000 allocated to the CEOs (Monem, " The One-Tel Collapse: Lessons for Corporate Governance").

Thus, weak internal controls, conflict of interest and responsibilities, selective financial reporting, poor governance and excessive compensations all contributed to the failure of the company in May 29, 2001. (Jones, " Creative Accounting, Fraud, and International Accounting Standards")

People Responsible to the Demise of One Tel

John Rich and Brad Keeling, as the co-founders of the company, were negligent in the conduct of their operations. They prioritized their respective self-interest at the expense of the business by granting themselves compensation at unreasonable levels. They were dishonest in reporting the true state of the company's standing to the stockholders by overstating earnings which should have been reduced by unnecessary accruals and recognition of significant expenses.

John Greaves is also to blame for his failure to effectively preside over meetings that were crucial to the future management of the company. His failure to question the missing financial information being reported

prevented the early acknowledgement of erroneous accounting practices. In the same way, the finance director, Mark Silbermann, was also irresponsible in handling the company finances by his intentional infrequent analysis of the financial records which could have suggested immediate attention to save One Tel from bankruptcy.

Audit Risks

The inherent risks associated with One Tel include the marketing approach they chose in encouraging new subscriber to their services. The company initially gives incentives and charges their customers at prices that were significantly lower when compared to its Australian competitors. Moreover, One Tel's operations were dependent on Optus and Telstra which were also large participants to the telecommunications industry and provided services for the same market. So while they can guarantee cheaper rates, its competitors had lower operating costs. In addition, One Tel cannot guarantee subscription revenues in the long run since they had no fixed term contracts and access fees from customers. Equity instruments also largely funded business expansion.

The control risks of the company include having a bonus incentive to both CEOs based on the increasing company goodwill instead of its positive earnings or any other indication of financial growth that were quantifiable. The company also had limited guarantee as to the actual use of the SIM cards being given to customers thereby by substantially decreasing the sign up bonus from Optus. Credit checks were very poor since One Tel would easy grant subscription in the early stages and when customer are later found to have not been credit worthy, dealers had already thought of ways to

override the payments. This resulted to as much as 60% of revenues on receivables to be uncollectible.

The detection risk of One Tel should been low and the Chairman of Ernst & Young, Brian Long, actually withheld substantial facts to the Board of Directors the day before the company collapsed because they would be in conflict with the interest of the Packer-controlled companies as they were a major shareholder of the telecommunications company. A quick inquiry as to the infrequent viewing of the accounting records by its auditors could have suggested clues that the financial statements possibly not free from errors. Given that BDO Nelson Parkhill expressed an unqualified opinion regarding the correctness of the One Tel's financial statements when another auditing firm had information that should have rendered it erroneous, it just goes to show that their auditor failed to perform substantive tests to account for more detailed financial analysis that could have uncovered these anomalies.

Conclusion

In my understanding, the collapse of One Tel was largely attributed to overly positive forecasts of future earnings and a disregard of operating costs. The key people within the company prioritized their self-interest by gaining from excessive remuneration packages. They were very dependent on the proceeds from the equity instruments to fund their expansion across Europe. They had little consideration in the effective management of their financial information which had led to fraudulent misstatements and biased financial reports during board meetings and in their annual reports. The separation of duties with regard to their key executives were not properly carried out and

this has led to judgments which were predisposed to influence by other board members. Ultimately, these circumstances along with other factors has led to eventually bring the company to liquidation.

What I Could Have Done

Just like any the other accounting fraud case, One Tel was also guilty of overstating their income earnings, buying shares to increase their market prices, and understating debts and expenses to present a better picture of the company's financial performance.

As such, if I was to be the external auditor at that time, I would taken these steps to save the company from liquidation:

- Recognize the ethical considerations of the Board members' actions and stated my opinion on this matter
- Although advisory and consulting services do not involve the scope of my work, I should have at least mentioned the possible effects of not clearly separating the conflicting duties of their executives
- Be strict regarding the accounting practices that they follow, take note of the violations they had with the Australian Securities Exchange (ASX) recommendations and issued my qualified report

The three control procedures that could have saved the company includes:

- a clear organizational structure that determined their specific responsibilities
- a consistent check-and-balance procedure for all company transactions
- strengthening internal controls regarding the manipulation of financial data

Works Cited

- Attard, M. (2009). Jodee Rich. Retrieved from <http://www.abc.net.au/sundayprofile/stories/2762328.htm>
- Avison, D. (2004). Information Systems Failure Explained Through the Lens of the Cultural Web. Retrieved from <http://epsress.lib.uts.edu.au/research/bitstream/handle/10453/2710/2004001411.pdf>
- Barry, P. (2002). One Tel's Cash SOS, Then It All Fell Apart. Retrieved from <http://www.smh.com.au/articles/2002/07/31/1027926916297.html>
- Bartholomeusz, S. (2009). One. Tel's wealth of Rich's. Retrieved from <http://www.businessspectator.com.au/article/2009/11/18/financial-markets/onetels-wealth-richs>
- Carnegie, G., & O'Connel, B.(2009). Accounting scandals in Australia since the late 1980s. Retrieved from <http://www.edwards.usask.ca/special/5ahic/papers/Accounting%20scandals%20in%20Australia%20since%20the%20late%201980s.pdf>
- Cook, T. (2011). Collapse of Australia's Fourth Largest Telco Adds To Growing List of Corporate Failures. Retrieved from <http://www.wsws.org/en/articles/2001/06/onte-j08.html>
- Jones, M. (2011). Creative Accounting, Fraud, and International Accounting Standards. Retrieved from http://books.google.com.ph/books?id=P35zA_RsN9MC
- Low, H. (2012). Court hangs up on One Tel. Retrieved from http://www.afr.com/p/national/court_hangs_up_on_one_tel_c4JQR7ObLw4fj1YpSE6RBP
- Monem, R. (2011). The One-Tel Collapse: Lessons for Corporate Governance. Retrieved from <http://www98.griffith.edu>

au/dspace/bitstream/handle/10072/42673/74746_1. pdf

- Moran, S. (2009). May Days for One Tel. Retrieved from <http://www.theaustralian.com.au/business/may-days-for-onetel/story-e6frg8zx-1225800815387>

- One Tel. (2000). Annual Report 2000. Retrieved from <http://acc3510theateam.wikispaces.com/file/view/Report.pdf>

- Schneider, J. (2010). James Packer and Jodee Rich Agree to Settle Dispute Over One Tel Collapse. Retrieved from <http://www.bloomberg.com/news/2010-09-14/james-packer-and-jodee-rich-agree-to-settle-dispute-over-one-tel-collapse.html>