High Cost & Low Income

Audit Briefing Book

Monday, April 26, 2021

Virtual Meeting

Universal Service Administrative Company

700 12th Street NW, Suite 900

Washington, D.C. 20005

Summary of High Cost Support Mechanism Beneficiary Audit Reports Released: January 15, 2021

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
3 Rivers Tel Cooperative, Inc. **Attachment A**	3	• Improper Allocation Methodology: For the building allocation factor, the Beneficiary did not sufficiently allocate labor costs associated with Customer Service and General and Administrative employees to non-regulated accounts; thus, an improper factor was used to allocate costs. • Improper Inclusion of Non-regulated Amounts: The Beneficiary did not allocate joint costs related to a specific vendor to non-regulated accounts.	$25,356,983	$131,136	$131,136	N
Central Montana Communications, Inc. **Attachment B**	2	• No significant findings	$10,438,100	($3,440)	$0	N

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
Farmers Telephone Cooperative, Inc. **Attachment C**	2	• Use of Group Asset Depreciation for General Support Assets: The Beneficiary calculated depreciation expense on an individual asset basis for general support assets rather than under the group plan of accounting for depreciation.	$9,045,423	($84,470)	$0	N
Lumos Telephone Company **Attachment D**	3	• Lack of Supporting Documentation for Reported Access Lines: The Beneficiary did not maintain supporting documentation for its actual 2016 access line counts.	$12,303,156	$14,860	$14,860	N
Poka Lambro Telephone Cooperative, Inc. **Attachment E**	2	• Inaccurate Allocations/Factors: The Beneficiary used outdated cost studies to allocate costs for general support facilities to regulated and non-regulated accounts.	$2,681,979	$26,014	$26,014	N

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
Ragland Telephone Company **Attachment F**	3	• Improper Inclusion of Nonregulated Assets: The Beneficiary did not remove nonregulated assets and the corresponding accumulated depreciation from its High Cost program filings.	$758,222	$2,722	$2,722	N
Total	**15**		**$60,583,863**	**$86,822**	**$174,732**	

ATTACHMENT A

HC2019BE014

3 Rivers Telephone Cooperative, Inc.
Audit ID: HC2019BE014
(SAC No.: 482255)

Performance audit for the Universal Service High Cost Program Disbursements made during the twelve-month period ended December 31, 2018

Prepared for: Universal Service Administrative Company

As of Date: January 5, 2021

KPMG LLP
1021 East Cary Street
Richmond, VA 23219

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EXECUTIVE SUMMARY

January 5, 2021

Ms. Teleshia Delmar, Vice President – Audit and Assurance Division
Universal Service Administrative Company
700 12th Street, NW, Suite 900
Washington, DC 20005

Dear Ms. Delmar:

This report presents the results of our work conducted to address the performance audit objectives relative to 3 Rivers Telephone Cooperative, Inc. ("Beneficiary"), Study Area Code ("SAC") No. 482255, ("3 Rivers" or "Beneficiary") for disbursements, of $25,356,983, made from the Universal Service High Cost Program ("HCP") during the twelve-month period ended December 31, 2018. Our work was performed during the period from November 6, 2019 to January 5, 2021, and our results are as of January 5, 2021.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards issued by the Comptroller General of the United States (2018 Revision, as amended) and *American Institute of Certified Public Accountants Consulting Standards*. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the Federal Communications Commission's ("FCC") Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP (collectively, the "Rules") relative to disbursements, of $25,356,983, made from the HCP during the twelve-month period ended December 31, 2018. Compliance with the Rules is the responsibility of the Beneficiary's management. Our responsibility is to evaluate the Beneficiary's compliance with the Rules based on our audit.

As our report further describes, KPMG identified three findings as discussed in the Audit Results and Recovery Action section. Based on these results, we estimate that disbursements made to the Beneficiary from the HCP for the twelve-month period ended December 31, 2018 were $131,136 higher than they would have been had the amounts been reported properly.

KPMG cautions that projecting the results of our evaluation to future periods is subject to the risks that controls may become inadequate because of changes in conditions or because compliance with controls may deteriorate.

In addition, we also noted other matters that we have reported to the management of the Beneficiary in a separate letter dated January 5, 2021.

This report is intended solely for the use of the Universal Service Administrative Company, the Beneficiary, and the FCC and is not intended to be and should not be relied upon by anyone other than these specified parties. This report is not confidential and may be released by USAC to a requesting third party.

Sincerely,

KPMG LLP

List of Acronyms

Acronym	Definition
3 Rivers	3 Rivers Telephone Cooperative, Inc.
ACAM	Alternative Connect America Cost Model
ARC	Access Recovery Charge
BLS	Broadband Loop Support
C.F.R.	Code of Federal Regulations
C&WF	Cable and Wire Facilities
CAF ICC	Connect America Fund Intercarrier Compensation
COE	Central Office Equipment
CLEC	Competitive Local Exchange Carrier
CPRs	Continuing Property Records
ETC	Eligible Telecommunications Carrier
FCC	Federal Communications Commission
Form 509	CAF BLS Annual Common Line Actual Cost Data Collection Form
G/L	General Ledger
HCL	High Cost Loop
HCL Form	National Exchange Carrier Association Universal Service Fund Data Collection Form
HCM	High Cost Model
HCP	High Cost Program
ICLS	Interstate Common Line Support
ILEC	Incumbent Local Exchange Carrier
LEC	Local Exchange Carrier
NECA	National Exchange Carrier Association
SAC	Study Area Code
SLC	Subscriber Line Charge
SNA	Safety Net Additive
SVS	Safety Valve Support
TPIS	Telecommunications Plant In Service
USAC	Universal Service Administrative Company
USF	Universal Service Fund

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect	Recommended Recovery[1]
<u>HC2019BE014-F01: Improper Allocation Methodology</u> – For the building allocation factor, the Beneficiary did not sufficiently allocate labor costs associated with Customer Service and General & Administrative employees to non-regulated accounts and thus an improper factor was utilized to allocate costs.	$ 75,806	$ 75,806
<u>HC2019BE014-F02: Improper Inclusion of Non-regulated Amounts</u>– The Beneficiary did not allocate joint costs related to specific vendor to non-regulated affiliates.	$ 54,680	$ 54,680
<u>HC2016BE014-F03: Inaccurate Loop Counts</u> – The Beneficiary under reported the Total Loops and Category 1.3 Loops submitted on the HCP Forms.	$ 650	$ 650
Total Net Monetary Effect	**$ 131,136**	**$ 131,136**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery of the High Cost Program support from the Beneficiary for SAC 482255 in the amount noted in the table below.

Regarding Finding #1, USAC Management requires the Beneficiary to be placed on a corrective action plan (C.A.P.) to address the Improper Allocation Methodology. As part of the C.A.P., the Beneficiary must report to High Cost Management, within 60 days of the date of the Recovery Letter to be issued by High Cost Program, how it plans to improve its documentation processes.

The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	HCL (A)	ICLS (B)	USAC Recovery Action (A) + (B) + (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	($7,441)	$83,247	$75,806	
Finding #2	$40,864	$13,816	$54,680	
Finding #3	$650	$	$650	
Mechanism Total	**$34,073**	**$97,063**	**$131,136**	

As a result of the audit, USAC management will recover $131,136 of High Cost Program support from the Beneficiary for SAC 482255.

BACKGROUND, OBJECTIVES, SCOPE AND PROCEDURES

BACKGROUND

Program Overview

USAC is an independent not-for-profit corporation that operates under the direction of the FCC pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the USF through four support mechanisms: High Cost; Lifeline; Rural Health Care; and Schools and Libraries. These four support mechanisms ensure that all people regardless of location or income level have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations or advocate regarding any matter of universal service policy.

The High Cost Support Mechanism, also known as the HCP, ensures that consumers in all regions of the nation have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas, regardless of location or economic strata. Thus, the HCP provides support for telecommunications companies (Beneficiaries) that offer services to consumers in less-populated areas. Several legacy HCP support mechanisms are noted below:

1. HCL: HCL support is available for rural companies operating in service areas where the cost to provide service exceeds 115% of the national average cost per line. HCL support includes the following two sub-components:
    a. SNA: SNA support is available for carriers that make significant investment in rural infrastructure in years when HCL support is capped and is intended to provide carriers with additional incentives to invest in their networks.
    b. SVS: SVS support is available to rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.
2. HCM: HCM support is available to carriers serving wire centers in certain states where the forward-looking costs to provide service exceed the national benchmark.
3. CAF ICC: CAF ICC support is available to ILECs to recover revenue that is not covered by Access Recovery Charges (ARC) to the end user.
4. ICLS: ICLS is available to rate-of-return incumbent carriers and competitive carriers, and is designed to help carriers offset interstate access charges and to permit each rate-of-return carrier to recover its common line revenue requirement, while ensuring that its SLCs remain affordable to its customers.
5. CAF BLS: CAF BLS provides support for voice and broadband service, including stand-alone broadband. CAF BLS provides support for rate-of-return carriers to the extent that SLC caps do not permit them to recover their common line revenue requirements. CAF BLS replaced ICLS effective July 1, 2016.
6. ACAM: ACAM provides funding to rate-of-return carriers that voluntarily elected to transition to a new cost model for calculating High Cost support in exchange for meeting defined broadband build-out obligations.

USAC engaged KPMG to conduct a performance audit relating to the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $25,356,983, made from the HCP during the twelve-month period ended December 31, 2018.

Beneficiary Overview

3 Rivers Telephone Cooperative, Inc. (SAC No.482255), the subject of this performance audit is a rural ILEC located in Fairfield, MT that serves around 15,000 customers over a 16,500 square-mile service area in portions of west central, north central and southwestern Montana providing voice, broadband internet and video services. 3 Rivers also offers CLEC wireline and access services, and has a RadioShack store located in Browning, MT.

3 Rivers Telephone Cooperative owns 100% of 3 Rivers Telecommunications, Inc., which is a holding company for investments in telecommunications related enterprises.

The following table illustrates the High Cost support disbursed by USAC to the Beneficiary during the twelve-month period ended December 31, 2018 by fund type:

High Cost Support	Disbursement Amount
Connect America Fund (CAF) Broadband Loop Support (BLS)	$16,011,444
High Cost Loop (HCL)	$ 7,582,511
Connect America Fund (CAF) Intercarrier Compensation (ICC)	$ 1,602,186
Interstate Common Line Support (ICLS)	$ 160,842
Total	**$25,356,983**

Source: USAC

The High Cost support received by the Beneficiary during the twelve-month period ended December 31, 2018, was based on the following annual financial and operational data submitted by the Beneficiary to NECA and USAC:

- 2017-1 and 2017-2 HCL Forms, based on the twelve-month periods ended December 31, 2016 and March 31, 2017, respectively,
- 2016 FCC Form 509, based on the twelve-month periods ended December 31, 2016 data, and
- 2016 CAF ICC Tariff Review Plan (TRP), based on program year 2016 data

The above Forms capture line count data and the totals of certain pre-designated G/L Accounts including all asset accounts that roll into the TPIS account as well as certain deferred liabilities and operating expenses, subject to the allocation between regulated and non-regulated activities (Part 64 Cost Allocations), the separation between interstate and intrastate operations (Part 36 Separations) and the separation between access and non-access elements (Part 69 Separations). In addition, the Beneficiary is required to submit certain annual investment data, including the categorization of COE and C&WF on the HCP Forms.

OBJECTIVES

The audit objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $25,356,983, made from the HCP during the twelve-month period ended December 31, 2018.

SCOPE

The scope of this performance audit includes, but is not limited to, reviewing HCP Forms or other correspondence and supporting documentation provided by the Beneficiary, assessing the Beneficiary's methodology used to prepare or support the HCP Forms or other correspondence, and evaluating disbursement amounts made by the Beneficiary or potentially due to the Beneficiary. The scope of our work is focused on the HCP Forms or other correspondence filed by the Beneficiary that relate to disbursements made from the HCP during the twelve-month period ended December 31, 2018, as well as performing other procedures we considered necessary to form a conclusion relative to disbursements made from the HCP during the twelve-month period ended December 31, 2018.

KPMG identified the following areas of focus for this performance audit:[2]

1. General Procedures
2. Materiality Analysis
3. Reconciliation
4. Assets
5. Expenses
6. HCP Eligibility Forms
7. COE Categorization
8. C&WF Categorization
9. Overheads
10. Taxes
11. Part 64 Cost Allocations
12. Affiliate Transactions
13. Revenues, Subscriber Listings and Billing Records
14. Revenue Requirement

PROCEDURES

1. General Procedures

KPMG obtained and examined the ETC designation order to determine whether the Beneficiary was designated as an ETC in the study area prior to receiving HCP support. We obtained and examined the Beneficiary's state and/or self-certification letters for timeliness and the notation that all federal HCP support provided was used in the preceding calendar year and will be used in the coming calendar year only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. We also obtained the Form 481 filed by the Beneficiary to determine whether the Beneficiary made the required certifications and whether the Beneficiary's supporting documentation agrees to the data reported for the certifications made.

2. Materiality Analysis

[2] If exceptions were noted in areas other than the aforementioned in-scope areas as a result of our testing procedures and the execution of our performance audit, we identified those findings in the 'Results' section of the report.

For applicable HCP Forms, we obtained the forms submitted for the periods ended December 31, 2016 and March 31, 2017, input the information into KPMG's HCP models, and ran a materiality analysis that increased and decreased the account balances by +/- 50%. If the impact generated a +/- 5% or $100,000 change to overall disbursements, the individual line item/account was considered material for purposes of our performance audit.

3. **Reconciliation**

KPMG obtained the audited 2016 and 2017 financial statements and reconciled to the G/L, from the G/L we reconciled to the Part 64 cost allocation inputs and then to the applicable HCP Forms. We also reconciled the trial balance for the twelve-month period ended March 31, 2017 to the respective Part 64 cost allocation study inputs and then to the 2017-2 HCL Form. We obtained explanations for any reconciling differences.

4. **Assets**

KPMG utilized a monetary unit sampling methodology to select asset samples from material accounts identified in the relevant HCP Forms. Asset selections were made from CPR details, and material accounts included COE, C&WF and certain general support asset accounts. We assessed whether asset balances were properly supported by reviewing underlying documentation such as work orders, third-party vendor invoices, and time and payroll documentation for labor-related costs; agreed dollar amounts charged to the work orders and verified proper Part 32 categorization; and validated the physical existence of selected assets. The Beneficiary was unable to provide any supporting documentation for four of the 31 assets selected for testing. In order to determine the original four asset amounts selected for testing were reasonable, KPMG performed the alternative procedures which included obtaining documentation for a comparable asset (of the same or similar type and vintage year) and explanations from the Beneficiary and cost consultant.

5. **Expenses**

KPMG utilized a monetary unit sampling methodology to select expense samples including payroll from material operating expense accounts identified in the relevant HCP Forms. Expense amounts were compared to the supporting documentation such as invoices and were reviewed for proper Part 32 account coding and categorization by expense type and nature of the costs incurred (regulated versus non-regulated activities). We also obtained and examined monthly depreciation expense and accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation.

6. **HCP Eligibility Forms**

For the relevant HCP Forms (HCL, ICLS/CAF BLS, and CAF ICC) completeness of reported accounts was assessed via reconciliations to the audited financial statements via the 'Reconciliation' process described above. Reconciling items were discussed with the Beneficiary.

7. **COE Categorization**

KPMG reviewed the methodology established by the Beneficiary for COE categorization including the process for updating the network map and COE cost studies as well as performing a physical inspection. We assessed whether COE amounts reconciled to studies including reviewing power and common allocations, Part 36 inputs and whether amounts agreed to the HCL form data.

8. **C&WF Categorization**

KPMG reviewed the methodology established by the Beneficiary for C&WF categorization including the process for updating the network map and C&WF cost studies. We assessed whether C&WF amounts reconciled to studies and whether amounts agreed to the HCL form data and also performed a route distance inspection.

9. Overhead

KPMG performed a walkthrough of the overhead allocation and clearing process related to work orders and payroll for 2016 and 2017. Additionally, we reviewed overhead clearing reports for a selected month and reviewed the overhead clearance process for compliance with Part 32 requirements.

10. Taxes

KPMG noted that the Beneficiary is a tax-exempt cooperative. We obtained and reviewed the 2016 and 2017 Form 990s, and noted the Beneficiary is not required to pay federal or state income taxes on patronage activities.

11. Part 64 Cost Allocations

KPMG reviewed the Beneficiary's cost apportionment methodology and performed procedures to evaluate the apportionment factors which included performing a walkthrough with the Beneficiary and evaluating the reasonableness of the cost pool and regulated/non-regulated apportionment factors as compared to regulated and non-regulated activities performed by the Beneficiary, assessing the reasonableness of the allocation methods and corresponding data inputs used to calculate the material factors and recalculating each of the material factors.

12. Affiliate Transactions

KPMG performed procedures to assess the reasonableness of affiliate transactions via a joint management and operation agreement among other things that occurred during January 1, 2016 to March 31, 2017. These procedures included determining the population of affiliate transactions by reviewing the audited financial statements, trial balance, and intercompany accounts, and through inquiry, and utilizing attribute sampling to select a sample of the different types of affiliate transactions for testing. For the sample selected, we reviewed the business purpose of each transaction and determined if the transactions were recorded in accordance with 47 C.F.R. Section 32.27 and 47 C.F.R. Section 36.2 and categorized in the appropriate Part 32 accounts.

13. Revenues, Subscriber Listings and Billing Records

KPMG examined revenue G/L accounts, invoices and other related documentation to verify the accuracy and existence of revenue account balances. KPMG analyzed subscriber listings and billing records to determine that the number and type of lines reported in the HCP filings agreed to underlying support documentation that subscriber listings did not include duplicate lines, invalid data, or non-revenue producing or non-working loops, and that lines were properly classified as residential/single-line business or multi-line business.

14. Revenue Requirement

KPMG reviewed the calculation of the Beneficiary's revenue requirement, including assessing the reasonableness and application of Part 64 cost allocation, Part 36 and Part 69 separations and other cost study adjustments utilized in the calculation of the common line revenue requirement. KPMG obtained the projected data reported on FCC Forms 508 and compared against associated FCC Form 509 representing actual data, as applicable. KPMG inquired of the Beneficiary regarding the process related to determination of projections related to ICLS and BLS funding mechanisms.

RESULTS

KPMG's performance audit results include a listing of findings, recommendations and Beneficiary responses, with respect to the Beneficiary's compliance with FCC requirements, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69, applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018. USAC management is responsible for any decisions and actions resulting from the findings or recommendations noted.

FINDINGS, RECOMMENDATIONS AND BENEFICIARY RESPONSES

KPMG's performance audit procedures identified three findings. The findings, including the condition, cause, effect, recommendation and Beneficiary response are as follows:

Finding # HC2019BE014-F01: 47 C.F.R. Section 64.901(a) (2016) – Improper Allocation Methodology

CONDITION

While reviewing the Part 64 cost allocation study and associated support, it was noted that the Building allocation factor was based on labor hours reported on time sheets which allocated an understated amount of cost to non-regulated. The Beneficiary did not perform further Part 64 cost allocations to allocate Customer Service and General & Administrative employee time between regulated and non-regulated accounts and thus did not use an appropriate factor to allocate costs. See detail below regarding updated cost allocations for accounts utilizing the Building allocation factor:

Account	Dollar Amount Overstated to Regulated Accounts for the year ended December 31, 2016	Dollar Amount Overstated to Regulated Accounts for the year ended March 31, 2017
2121: Buildings	$ 1,621,832	$ 1,621,832
2122: Office Furniture	$ 162,382	$ 162,382
2123: Office Equipment	$ 78,283	$ 77,686
2124: General Purpose Computers	$ 136,036	$ 139,303
3100: Accumulated Depreciation – Support Assets	$ 1,610,153	$ 1,633,110
6121: Land and Building Expense	$ 17,857	$ 16,510
6123: Office Equipment Expense	$ 8,234	$ 8,129
6124: General Purpose Computers Expense	$ 51,656	$ 44,120
6560: Depreciation & Amortization Expense – Support Assets	$ 93,325	$ 94,219
6610: Customer Service	$ 199,223	$ 142,337
6620: Customer Service	$ 436,255	$ 422,332
6710: General Support Expense	$ 47,317	$ 54,921
6720: General Administrative Expenses	$ 204,125	$ 216,162

CAUSE

The Beneficiary did not have adequate procedures and controls over the review and approval of Part 64 cost allocations of common or joint costs between regulated and non-regulated activities to ensure that all costs related to non-regulated activities were properly allocated.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-payment of $75,806. See below for the summarization of the support mechanisms impacted by this finding:

Support Type	Monetary Effect	Recommended Recovery
HCL	($ 7,441)	($ 7,441)
ICLS	$ 83,247	$ 83,247
CAFF BLS	N/A	N/A
CAF ICC	N/A	N/A
Total	**$ 75,806**	**$ 75,806**

RECOMMENDATION

KPMG recommends that USAC management seek recovery of the amounts identified in the Effect section above.

The Beneficiary should establish, document and implement procedures to address the preparation, review and approval processes related to the Part 64 cost allocation of common or joint costs to ensure compliance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

3 Rivers Telephone Cooperative's management acknowledges the error as set forth in the "Condition" section above. While 3 Rivers' management was unable to recalculate the monetary effect, the above effect is in line with management's expectations based on discussions and calculations which transpired during the KPMG audit. This specific "condition" has already been corrected for 3 Rivers Telephone Cooperative's most recent cost study and 3 Rivers has also implemented new review procedures to help to ensure that joint expenses are adequately allocated between regulated and nonregulated operations.

Finding # HC2019BE014-F02: 47 C.F.R. Section 64.901(a) (2016) – Improper Inclusion of Non-regulated Amounts

CONDITION

Through review of affiliate transactions and shared costs, we noted the Beneficiary did not perform Part 64 cost allocations to allocate joint software expenses, billing expenses and other miscellaneous costs related to a specific vendor to non-regulated accounts during the audit period. See detail below:

For the year ended December 31, 2016	
Account	**Over-Stated Amounts**
6120: General Support Expense	$ 7,859
6510: Other Property Plant Expense	$ 295
6530: Network Operations Expense	$ 54,257
6610: Marketing Expense	$ 4,971
6620: Customer Services Expense	$ 113,566
6720: General Administrative Expenses	$ 6,851
Total	**$ 187,799**

For the year ended March 31, 2017	
Account	**Over-Stated Amounts**
6120: General Support Expense	$ 19,773
6510: Other Property Plant Expense	$ 296
6530: Network Operations Expense	$ 53,783
6610: Marketing Expense	$ 4,971
6620: Customer Services Expense	$ 117,504
6720: General Administrative Expenses	$ 11,333
Total	**$ 207,660**

CAUSE

The preparation, review and approval processes of the Beneficiary related to Part 64 common cost allocations did not completely review joint expense transactions in order to allocate amounts between regulated and non-regulated accounts.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-payment of $54,680. See below for the summarization of the support mechanisms impacted by this finding:

Support Type	Monetary Effect	Recommended Recovery
HCL	$ 40,864	$ 40,864
ICLS	$ 13,816	$ 13,816
CAFF BLS	N/A	N/A
CAF ICC	N/A	N/A
Total	**$ 54,680**	**$ 54,680**

RECOMMENDATION

KPMG recommends that USAC management seek recovery of the amounts identified in the Effect section above.

The Beneficiary should establish controls governing the preparation, review and approval processes related to Part 64 common cost allocations. The Beneficiary should also perform an appropriate study to allocate plant assets between regulated and non-regulated accounts. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

3 Rivers Telephone Cooperative's management acknowledges the error as set forth in the "Condition" section above. While 3 Rivers' management was unable to recalculate the monetary effect, the effect is in line with management's expectations based on information provided to KPMG during its audit. This specific "condition" has already been corrected for 3 Rivers Telephone Cooperative's most recent cost study and 3 Rivers has also implemented new review procedures to help to ensure that joint expenses are adequately allocated between regulated and nonregulated operations.

Finding # HC2019BE014-F03: 47 C.F.R. Section 54.903(a)(4)(2016) – Inaccurate Loop Counts

CONDITION

The Beneficiary filed line count data on the 2017-1 HCL form using subscriber counts from December 26, 2016 versus December 31, 2016. After obtaining and inspecting support for new lines and disconnects between the dates, it was noted the Total Loops and Category 1.3 Loops submitted on the 2017-1 HCP Form did not reconcile to the source documentation and were under-reported by one loop as follows:

	Amount per 2017-1 HCL Form	Amount per Supporting Documentation	Variance
Totals Loops	17,230	17,231	1
Category 1.3 Loops	17,179	17,180	1

CAUSE

The Beneficiary filed the 2017-1 HCL form utilizing the last billing cycle of the year, December 26, 2016 versus actual December 31, 2016 data.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $650 and is summarized as follows:

Support Type	Monetary Effect	Recommended Recovery
HCL	$ 650	$ 650
ICLS	N/A	N/A
CAF BLS	N/A	N/A
CAF ICC	N/A	N/A
Total	**$ 650**	**$ 650**

RECOMMENDATION

KPMG recommends that USAC management seek recovery of the amounts identified in the Effect section above.

The Beneficiary should implement processes to review and report the appropriate line counts, including the performance of a reconciliation of all line count data to underlying support documentation. Moreover, the Beneficiary should enhance its preparation, review and approval processes over HCP filing to ensure compliance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

3 Rivers Telephone Cooperative's management acknowledges the error as set forth in the "Condition" section above. 3 Rivers' management did not attempt to recalculate the monetary effect of this finding and finds KPMG's calculated effect to be adequate. In line with common industry practice, 3 Rivers has historically utilized its billing register loop (or line) counts for its loop count reporting. The billing register reflects actual billed line counts and is the best source of evidence for supporting line counts. Additionally, the activity between billing "transmit" and the end of the month/year are typically negligible as is evidenced by the variance above. That being said, 3 Rivers acknowledges that to ensure compliance with FCC Rules and orders, its line counts should reflect month/year end counts. Therefore, management will implement a process to ensure that the billing register is reconciled for additions and deletions from the "transmit" date to the end of the month/year to ensure proper loop count reporting.

CRITERIA

Finding	Criteria	Description
#1, #2	47 C.F.R. Section 32.14(c)(2016)	"In the application of detailed accounting requirements contained in this part, when a regulated activity involves the common or joint use of assets and resources in the provision of regulated and nonregulated products and services, companies shall account for these activities within the accounts prescribed in this system for telephone company operations. Assets and expenses shall be subdivided in subsidiary records among amounts solely assignable to nonregulated activities, amounts solely assignable to regulated activities, and amounts related to assets used and expenses incurred jointly or in common, which will be allocated between regulated and nonregulated activities."
#1, #2	47 C.F.R. 64.901(a) and (b)(2)-(3) (2016)	"Carriers required to separate their regulated costs from nonregulated costs should use the attributable cost method of cost allocation for such purposes. In assigning or allocating costs to regulated and nonregulated activities, carrier shall follow the principles described herein. Costs shall be directly assigned to either regulated or nonregulated activities whenever possible. Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and non-regulated activities in accordance with the following hierarchy: (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves. (ii) When direct analysis is not possible, common cost categories shall be allocated based upon indirect, cost-causative linkage to another cost category (or group of categories) for which a direct assignment or allocation is available. (iii) When neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated based upon a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities."
#3	47 C.F.R. Section 54.903(a)(4) (2016)	"Each rate-of-return carrier shall submit to the Administrator on December 31st of each year the data necessary to calculate a carrier's Interstate Common Line Support, including common line cost and revenue data, for the prior calendar year. Such data shall be used by the Administrator to make adjustments to monthly per-line Interstate Common Line Support amounts in the final two quarters of the following calendar year to the extent of any differences between the

Finding	Criteria	Description
		carrier's ICLS received based on projected common line cost and revenue data and the ICLS for which the carrier is ultimately eligible based on its actual common line cost and revenue data during the relevant period."

CONCLUSION

KPMG's evaluation of the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018 identified improper allocation methodology, improper inclusion of non-regulated amounts and inaccurate loop count findings. Detailed information relative to the findings is described in the Findings, Recommendations and Beneficiary Responses section above.

The combined estimated monetary impact of these findings is as follows:

Fund Type	**Monetary Impact Overpayment (Underpayment)**
HCL	$ 34,073
ICLS	$ 97,063
Total Impact	**$ 131,136**

KPMG recommends that the Beneficiary enhance the preparation, review and approval processes related to Part 64 cost allocations and reporting of loop counts, in accordance with FCC Rules and Orders.

ATTACHMENT B

HC2019BE016

Available For Public Use

Central Montana Communications, Inc.
Audit ID: HC2019BE016
(SAC No.: 483310)

Performance audit for the Universal Service High Cost Program Disbursements made during the twelve-month period ended December 31, 2018

Prepared for: Universal Service Administrative Company

As of Date: January 7, 2021

KPMG LLP
Suite 900
8350 Board Street
McLean, VA 22102

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KPMG LLP
Suite 900
8350 Broad Street
McLean, VA 22102

EXECUTIVE SUMMARY

January 7, 2021

Ms. Teleshia Delmar, Vice President – Audit and Assurance Division
Universal Service Administrative Company
700 12th Street, NW, Suite 900
Washington, DC 20005

Dear Ms. Delmar:

This report presents the results of our work conducted to address the performance audit objectives relative to Central Montana Communications, Inc.'s, Study Area Code ("SAC") No. 483310, ("CMC" or "Beneficiary") for disbursements, of $10,438,100, made from the Universal Service High Cost Program ("HCP") during the twelve-month period ended December 31, 2018. Our work was performed during the period from October 30, 2019 to January 7, 2021, and our results are as of January 7, 2021.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards issued by the Comptroller General of the United States (2018 Revision, as amended) and *American Institute of Certified Public Accountants Consulting Standards*. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the Federal Communications Commission's ("FCC") Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP (collectively, the "Rules") relative to disbursements, of $10,438,100, made from the HCP during the twelve-month period ended December 31, 2018. Compliance with the Rules is the responsibility of the Beneficiary's management. Our responsibility is to evaluate the Beneficiary's compliance with the Rules based on our audit.

As our report further describes, KPMG identified two findings as discussed in the Audit Results and Recovery Action section as a result of the work performed. Based on these results, we estimate that disbursements made to the Beneficiary from the HCP for the twelve-month period ended December 31, 2018 were $3,440 lower than they would have been had the amounts been reported properly.

KPMG cautions that projecting the results of our evaluation to future periods is subject to the risks that controls may become inadequate because of changes in conditions or because compliance with controls may deteriorate.

In addition, we also noted other matters that we have reported to the management of the Beneficiary in a separate letter dated January 7, 2021.

This report is intended solely for the use of the Universal Service Administrative Company, the Beneficiary, and the FCC and is not intended to be and should not be relied upon by anyone other than these specified parties. This report is not confidential and may be released by USAC to a requesting third party.

Sincerely,

KPMG LLP

List of Acronyms

Acronym	Definition
ACAM	Alternative Connect America Cost Model
ARC	Access Recovery Charge
BLS	Broadband Loop Support
C.F.R.	Code of Federal Regulations
C&WF	Cable and Wire Facilities
CAF ICC	Connect America Fund Intercarrier Compensation
COE	Central Office Equipment
CMC	Central Montana Communications, Inc.
CPRs	Continuing Property Records
ETC	Eligible Telecommunications Carrier
FCC	Federal Communications Commission
Form 509	CAF BLS Annual Common Line Actual Cost Data Collection Form
G/L	General Ledger
HCL	High Cost Loop
HCL Form	National Exchange Carrier Association Universal Service Fund Data Collection Form
HCM	High Cost Model
HCP	High Cost Program
ICLS	Interstate Common Line Support
ILEC	Incumbent Local Exchange Carrier
LEC	Local Exchange Carrier
NECA	National Exchange Carrier Association
PRI	Primary Rate Interface
SAC	Study Area Code
SLC	Subscriber Line Charge
SNA	Safety Net Additive
SVS	Safety Valve Support
TB	Trial Balance
TPIS	Telecommunications Plant In Service
TTC	Triangle Telephone Cooperative Association, Inc.
USAC	Universal Service Administrative Company
USF	Universal Service Fund

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect	Recommended Recovery[1]
HC2019BE016-F01: Improper Inclusion of Non-Regulated Amounts – The Beneficiary did not accurately and appropriately allocate certain expenses between regulated and non-regulated activities, and between affiliates.	$ 1,480	$ 1,480
HC2019BE016-F02: Inaccurate Revenues – The Beneficiary overstated ARC revenues on their Program Year 2018 CAF ICC Form.	($4,920)	($4,920)
Total Net Monetary Effect	**($3,440)**	**($3,440)**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary for the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	HCL (A)	ICLS (B)	CAF ICC (C)	USAC Recovery Action (A) + (B) + (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$1,125	$355		$1,480	
Finding #2			($4,920)	($4,920)	
Mechanism Total	**$1,125**	**$355**	**($4,920)**	**($3,440)**	

As the above findings represent a net underpayment, the total recommended recovery (and thus, the recommended recovery for each individual finding) is zero as USAC policy is not to issue support in the case of a net underpayment. Thus, USAC recovery action is $0.

BACKGROUND, OBJECTIVES, SCOPE AND PROCEDURES

BACKGROUND

Program Overview

USAC is an independent not-for-profit corporation that operates under the direction of the FCC pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the USF through four support mechanisms: High Cost; Lifeline; Rural Health Care; and Schools and Libraries. These four support mechanisms ensure that all people regardless of location or income level have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations or advocate regarding any matter of universal service policy.

The High Cost Support Mechanism, also known as the HCP, ensures that consumers in all regions of the nation have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas, regardless of location or economic strata. Thus, the HCP provides support for telecommunications companies (Beneficiaries) that offer services to consumers in less-populated areas. Several legacy HCP support mechanisms are noted below:

1. HCL: HCL support is available for rural companies operating in service areas where the cost to provide service exceeds 115% of the national average cost per line. HCL support includes the following two sub-components:
    a. SNA: SNA support is available for carriers that make significant investment in rural infrastructure in years when HCL support is capped and is intended to provide carriers with additional incentives to invest in their networks.
    b. SVS: SVS support is available to rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.
2. HCM: HCM support is available to carriers serving wire centers in certain states where the forward-looking costs to provide service exceed the national benchmark.
3. CAF ICC: CAF ICC support is available to ILECs to recover revenue that is not covered by Access Recovery Charges (ARC) to the end user.
4. ICLS: ICLS is available to rate-of-return incumbent carriers and competitive carriers, and is designed to help carriers offset interstate access charges and to permit each rate-of-return carrier to recover its common line revenue requirement, while ensuring that its SLCs remain affordable to its customers.
5. CAF BLS: CAF BLS provides support for voice and broadband service, including stand-alone broadband. CAF BLS provides support for rate-of-return carriers to the extent that SLC caps do not permit them to recover their common line revenue requirements. CAF BLS replaced ICLS effective July 1, 2016.
6. ACAM: ACAM provides funding to rate-of-return carriers that voluntarily elected to transition to a new cost model for calculating High Cost support in exchange for meeting defined broadband build-out obligations.

USAC engaged KPMG to conduct a performance audit relating to the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $10,438,100, made from the HCP during the twelve-month period ended December 31, 2018.

Beneficiary Overview

Central Montana Communications, Inc. (SAC No. 483310), the subject of this performance audit, is a rural ILEC located in Havre, Montana. CMC is part of Triangle Telephone Cooperative Association, Inc., which is also another ILEC (SAC No. 482257) located in rural Montana. CMC and TTC provide traditional ILEC services including local telephone, long distance, and internet services, to their customers.

Triangle Telephone Cooperative Association, Inc. also has one non-regulated subsidiary, Triangle Communication, System Inc., that provides long distance service, cellular telephone service and wireless internet.

Triangle Telephone Cooperative Association, Inc., including CMC, and its subsidiary, Triangle Communication, System Inc. have a joint operation and maintenance agreement with Hill County Electric Cooperative, Inc. Costs incurred in the performance of regulated services under the agreement that relate to joint operations are to be apportioned between the companies and Hill County Electric Cooperative, Inc.

The following table illustrates the High Cost support disbursed by USAC to the Beneficiary during the twelve-month period ended December 31, 2018 by fund type:

High Cost Support	Disbursement Amount
Connect America Fund (CAF) Broadband Loop Support (BLS)	$ 3,995,442
Connect America Fund (CAF) Intercarrier Compensation (ICC)	$ 681,150
High Cost Loop (HCL)	$ 5,699,270
Interstate Common Line Support (ICLS)	$ 62,238
Total	**$10,438,100**

Source: USAC

The High Cost support received by the Beneficiary during the twelve-month period ended December 31, 2018, was based on the following annual financial and operational data submitted by the Beneficiary to NECA and USAC:

- 2017-1 and 2017-3 HCL Forms, based on the twelve-month periods ended December 31, 2016 and June 30, 2017, respectively,
- 2016 FCC Form 509, based on the twelve-month periods ended December 31, 2016, and
- 2016 CAF ICC Tariff Review Plan (TRP), based on twelve-month period ended June 30, 2017

The above Forms capture line count data and the totals of certain pre-designated G/L Accounts including all asset accounts that roll into the TPIS account as well as certain deferred liabilities and operating expenses, subject to the allocation between regulated and non-regulated activities (Part 64 Cost Allocations), the separation between interstate and intrastate operations (Part 36 Separations) and the separation between access and non-access elements (Part 69 Separations). In addition, the

Beneficiary is required to submit certain annual investment data, including the categorization of COE and C&WF on the HCP Forms.

OBJECTIVES

The audit objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $10,438,100, made from the HCP during the twelve-month period ended December 31, 2018.

SCOPE

The scope of this performance audit includes, but is not limited to, reviewing HCP Forms or other correspondence and supporting documentation provided by the Beneficiary, assessing the Beneficiary's methodology used to prepare or support the HCP Forms or other correspondence, and evaluating disbursement amounts made by the Beneficiary or potentially due to the Beneficiary. The scope of our work is focused on the HCP Forms or other correspondence filed by the Beneficiary that relate to disbursements made from the HCP during the twelve-month period ended December 31, 2018, as well as performing other procedures we considered necessary to form a conclusion relative to disbursements made from the HCP during the twelve-month period ended December 31, 2018.

KPMG identified the following areas of focus for this performance audit:[2]

1. General Procedures
2. Materiality Analysis
3. Reconciliation
4. Assets
5. Expenses
6. HCP Eligibility Forms
7. COE Categorization
8. C&WF Categorization
9. Overheads
10. Taxes
11. Part 64 Cost Allocations
12. Affiliate Transactions
13. Revenues, Subscriber Listings and Billing Records
14. Revenue Requirement

[2] If exceptions were noted in areas other than the aforementioned in-scope areas as a result of our testing procedures and the execution of our performance audit, we identified those findings in the 'Results' section of the report.

PROCEDURES

1. General Procedures

KPMG obtained and examined the ETC designation order to determine whether the Beneficiary was designated as an ETC in the study area prior to receiving HCP support. We obtained and examined the Beneficiary's state and/or self-certification letters for timeliness and the notation that all federal HCP support provided was used in the preceding calendar year and will be used in the coming calendar year only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. We also obtained the Form 481 filed by the Beneficiary to determine whether the Beneficiary made the required certifications and whether the Beneficiary's supporting documentation agrees to the data reported for the certifications made.

2. Materiality Analysis

For applicable HCP Forms, we obtained the forms submitted for the periods ended December 31, 2016 and June 30, 2017, input the information into KPMG's HCP models, and ran a materiality analysis that increased and decreased the account balances by +/- 50%. If the impact generated a +/- 5% or $100,000 change to overall disbursements, the individual line item/account was considered material for purposes of our performance audit.

3. Reconciliation

KPMG obtained the audited 2016 and 2017 financial statements and reconciled to the G/L, from the G/L we reconciled to the Part 64 cost allocation inputs and then to the applicable HCP Forms. We also reconciled the trial balance for the twelve-month period ended June 30, 2017 to the respective Part 64 cost allocation study inputs and then to the 2017-3 HCL Form. We obtained explanations for any reconciling differences.

4. Assets

KPMG utilized a monetary unit sampling methodology to select asset samples from material accounts identified in the relevant HCP Forms. Asset selections were made from CPR details, and material accounts included COE, C&WF and certain general support asset accounts. We assessed whether asset balances were properly supported by reviewing underlying documentation such as work orders, third-party vendor invoices, and time and payroll documentation for labor-related costs; agreed dollar amounts charged to the work orders and verified proper Part 32 categorization; and validated the physical existence of selected assets.

5. Expenses

KPMG utilized a monetary unit sampling methodology to select expense samples including payroll from material operating expense accounts identified in the relevant HCP Forms. Expense amounts were compared to the supporting documentation such as invoices and were reviewed for proper Part 32 account coding and categorization by expense type and nature of the costs incurred (regulated versus non-regulated activities). We also obtained and examined monthly depreciation expense and accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation.

6. HCP Eligibility Forms

For the relevant HCP Forms (HCL, ICLS/CAF BLS, and CAF ICC) completeness of reported accounts was assessed via reconciliations to the audited financial statements via the 'Reconciliation' process described above. Reconciling items were discussed with the Beneficiary.

7. **COE Categorization**

KPMG reviewed the methodology established by the Beneficiary for COE categorization including the process for updating the network map and COE cost studies as well as performing a physical inspection. We assessed whether COE amounts reconciled to studies including reviewing power and common allocations, Part 36 inputs and whether amounts agreed to the HCL form data.

8. **C&WF Categorization**

KPMG reviewed the methodology established by the Beneficiary for C&WF categorization including the process for updating the network map and C&WF cost studies. We assessed whether C&WF amounts reconciled to studies and whether amounts agreed to the HCL form data and also performed a route distance inspection.

9. **Overhead**

KPMG performed a walkthrough of the overhead allocation and clearing process related to work orders and payroll for 2016 and 2017. Additionally, we reviewed overhead clearing reports for a selected month and reviewed the overhead clearance process for compliance with Part 32 requirements.

10. **Taxes**

KPMG noted that the Beneficiary is one of two SACs in a tax-exempt cooperative, Triangle Telephone Cooperative. Triangle Telephone Cooperative files a consolidated Federal Income Tax Form 1120, U.S. Corporation Income Tax Return with its subsidiary, Triangle Communications Systems Inc. We obtained and reviewed the form, and noted the Beneficiary is not required to pay federal or state income taxes on patronage activities.

11. **Part 64 Cost Allocations**

KPMG reviewed the Beneficiary's cost apportionment methodology and performed procedures to evaluate the apportionment factors which included performing a walkthrough with the Beneficiary and evaluating the reasonableness of the cost pool and regulated/non-regulated apportionment factors as compared to regulated and non-regulated activities performed by the Beneficiary, assessing the reasonableness of the allocation methods and corresponding data inputs used to calculate the material factors and recalculating each of the material factors.

12. **Affiliate Transactions**

KPMG performed procedures to assess the reasonableness of affiliate transactions via a joint management and operation agreement among other things that occurred during January 1, 2016 to June 30, 2017. These procedures included determining the population of affiliate transactions by reviewing the audited financial statements, trial balance, and intercompany accounts, and through inquiry, and utilizing attribute sampling to select a sample of the different types of affiliate transactions for testing. For the sample selected, we reviewed the business purpose of each transaction and determined if the transactions were recorded in accordance with 47 C.F.R. Section 32.27 and 47 C.F.R. Section 36.2 and categorized in the appropriate Part 32 accounts.

13. **Revenues, Subscriber Listings and Billing Records**

KPMG examined revenue G/L accounts, invoices and other related documentation to verify the accuracy and existence of revenue account balances. KPMG analyzed subscriber listings and billing records to determine that the number and type of lines reported in the HCP filings agreed to underlying support documentation that subscriber listings did not include duplicate lines, invalid data, or non-revenue producing or non-working loops, and that lines were properly classified as residential/single-line business or multi-line business.

14. Revenue Requirement

KPMG reviewed the calculation of the Beneficiary's revenue requirement, including assessing the reasonableness and application of Part 64 cost allocation, Part 36 and Part 69 separations and other cost study adjustments utilized in the calculation of the common line revenue requirement. KPMG obtained the projected data reported on FCC Forms 508 and compared against associated FCC Form 509 representing actual data, as applicable. KPMG inquired of the Beneficiary regarding the process related to determination of projections related to ICLS and BLS funding mechanisms.

RESULTS

KPMG's performance audit results include a listing of findings, recommendations and Beneficiary responses, with respect to the Beneficiary's compliance with FCC requirements, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69, applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018. USAC management is responsible for any decisions and actions resulting from the findings or recommendations noted.

FINDINGS, RECOMMENDATIONS AND BENEFICIARY RESPONSES

KPMG's performance audit procedures identified two findings. The findings, including the condition, cause, effect, recommendation and Beneficiary response are as follows:

Finding # HC2019BE016-F01: 47 C.F.R. Section 64.901(a) – Improper Inclusion of Non-Regulated Amounts

CONDITION

KPMG obtained and examined a random sample, utilizing monetary unit sampling, of 32 expenses totaling $276,922 to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. For three of the 32 expenses sampled during the period of January 1, 2016 through June 30, 2017, the Beneficiary did not calculate and allocate non-regulated portion of the expense accurately. Specifically:

- For expense account 6230: Central Office Transmission Equipment Expense, KPMG noted that an IPV4 address expense from December 2016 was not accurately calculated based on the actual usage. KPMG recalculated the amount using actual usage and found the expense was overstated by $3,879.
- For expense account 6710: Executive and Planning Expense, KPMG noted that an employee's severance payment from December 2016 was miscalculated due to a percentage error in the calculation. KPMG recalculated the amount and found the expense was understated by $173.
- For expense account 6720: General and Administrative Expense, KPMG noted that CMC used a balance forward amount from December 2015 instead of the year to date balance to perform the expense calculation in October 2016. KPMG recalculated the amount using the YTD balance and found CMC understated the expense by $260.

CAUSE

The preparation, review and approval processes governing the expense allocations between regulated and non-regulated accounts did not detect the miscalculations made by the Beneficiary, thus the expenses were not in accordance with FCC Rules.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $1,480 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	$1,125
ICLS	$ 355
CAF BLS	N/A
CAF ICC	N/A
Total	**$ 1,480**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

The Beneficiary should enhance controls and procedures related to preparation, review and approvals related to the calculation, recording and reporting of regulated expenses. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Central Montana Communications, Inc. agrees with the listed condition. We will take steps to make sure allocations of IP address expense, severance payments and General Administration expense allocations are updated annually and reviewed before being posted.

Finding # HC2019BE016-F02: 47 C.F.R. Section 51.917(d)(1)(vii) – Inaccurate Revenues

CONDITION

KPMG obtained and examined the Beneficiary's general ledger to determine whether the Beneficiary reported its ARC revenues accurately for High Cost Program purposes. The Beneficiary overstated its 2016 ARC true-up revenues by $4,920 as reported on their Program Year 2018 CAF ICC Form compared to the ARC revenue recorded in the G/L.

CAUSE

The Beneficiary's processes and procedures governing the preparation and review of the CAF ICC Form did not identify the submission of erroneous ARC revenue information that included ARC's for Lifeline lines and PRI's that were not charged to customers.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an under-disbursement of $4,920 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	N/A
ICLS	N/A
CAF BLS	N/A
CAF ICC	($ 4,920)
Total	**($ 4,920)**

RECOMMENDATION

The Beneficiary should enhance controls and procedures related to preparation, review and approvals related to the calculation, recording and reporting of revenues. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Central Montana Communications, Inc. agrees with the listed condition. In Jan. 2019 we updated our procedures to exclude ARC revenues not billed to PRI and Lifeline customers.

CRITERIA

Finding	Criteria	Description
#1	47 C.F.R. Section 32.12(b) (2016)	"The company's financial records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission."
#1	47 C.F.R. Section 64.901(a) (2016)	"Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose."
#2	47 C.F.R. Section 51.917(d)(1)(vii) (2016)	"If a Rate-of-Return Carrier recovers any costs or revenues that are already being recovered as Eligible Recovery through Access Recovery Charges or the Connect America Fund from another source, that carrier's ability to recover reduced switched access revenue from Access Recovery Charges or the Connect America Fund shall be reduced to the extent it receives duplicative recovery. Any duplicative recovery shall be reflected as a reduction to a carrier's Eligible Recovery calculated pursuant to §51.917(d). A Rate-of-Return Carrier seeking revenue recovery must annually certify as part of its tariff filings to the Commission and to the relevant state commission that the carrier is not seeking duplicative recovery in the state jurisdiction for any Eligible Recovery subject to the recovery mechanism."

CONCLUSION

KPMG's evaluation of the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018 identified improper inclusion of non-regulated amounts and inaccurate revenues findings. Detailed information relative to the findings is described in the Findings, Recommendations and Beneficiary Responses section above.

The combined estimated monetary impact of these findings is as follows:

Fund Type	Monetary Impact Overpayment (Underpayment)
HCL	$ 1,125
ICLS	$ 355
CAF BLS	$ 0
CAF ICC	($ 4,920)
Total Impact	**($ 3,440)**

KPMG recommends that the Beneficiary enhance the preparation, review and approval processes related to calculating and allocating expenses, and reporting revenues, in accordance with FCC Rules and Orders.

ATTACHMENT C

HC2019BE024

Available For Public Use

Farmers Telephone Cooperative, Inc.

Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC2019BE024

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MOSSADAMS

EXECUTIVE SUMMARY

January 11, 2021

Teleshia Delmar, Audit and Assurance Division
Universal Service Administrative Company
700 12th St NW, Suite 900
Washington, DC 20005

Dear Teleshia Delmar:

This report represents the results of Moss Adams LLP's (we, us, our, and Moss Adams) work conducted to address the performance audit obligations relative to Farmers Telephone Cooperative, Inc. (Beneficiary), study area code 240520 for disbursements of $9,045,423 made from the federal Universal Service High Cost Program (HCP) (Disbursements) during the year ended December 31, 2017.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2018 Revision). Those standards require that we plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form our conclusions. We believe the evidence we have obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. However, our performance audit does not provide a legal determination of the Beneficiary's compliance with specified requirements.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support for the HCP relative to the disbursements (collectively, the Rules).

Based on the test work performed, our audit disclosed two detailed audit findings (Finding or Findings) discussed in the Audit Results section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations. This report is intended solely for the use of USAC, the Beneficiary, and the FCC and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

Moss Adams LLP

Spokane, Washington
January 11, 2021

AUDIT RESULTS

Audit Results	Monetary Effect & Recommended Recovery
Finding #1: 47 C.F.R. § 32.4300(a) – Incorrect Study Adjustment to Other Postretirement Employment Benefit (OPEB) Liability: The 2015 cost study adjustment related to account 4310 for the accumulated benefit obligation liability removed amounts calculated by the actuary that incorrectly increased the Beneficiary's rate base.	$5,380
Finding #2: 47 C.F.R. § 32.2000(g) – Use of Group Asset Depreciation for General Support Assets: The Beneficiary calculated depreciation expense on an individual asset basis for general support assets rather than under the group plan of accounting for depreciation.	($89,850)
Total	**($84,470)**

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary of the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	Support Type ICLS (A)	USAC Recovery Action (A) + (B) = (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$5,380	$5,380	
Finding #2	($89,850)	($89,850)	
Mechanism Total	($84,470)	($84,470)	

As indicated in the table above, the findings represent a net underpayment, thus, the total recommended recovery is zero. USAC does not issue support in instances where the total recommended recovery is a net underpayment. Thus, USAC's recovery action is $0.

BACKGROUND AND PROGRAM OVERVIEW

BACKGROUND

The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that provides telecommunications services, including local service and Internet to residential and business customers residing in areas of eastern South Carolina. The Beneficiary also provides non-regulated services such as cable television.

PROGRAM

USAC is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (FCC) pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the federal Universal Service Fund (USF), which is designed to ensure that all people, regardless of location or income have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations, or advocate regarding any matter of universal service policy.

The High Cost Program (HCP), a component of the USF, ensures that consumers in rural areas of the country have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas. The HCP consists of the following support mechanisms that are available to cost-based telecommunications carriers:

- High cost loop support (HCL): HCL is available for rural companies operating in services areas where the cost to provide service exceeds 115% of the national average cost per loop.

- Connect America Fund Intercarrier Compensation support (CAF ICC): CAF ICC support replaced Local Switching Support is available to ILECs to assist them in recovering a portion of the revenue requirement related to switching investment that is not covered by the access recovery charge (ARC) billed to the end user or certain other changes billed to other carriers. This revenue requirement was frozen based on forecasted switching investment filed by eligible carriers in 2011 and is being reduced by 5% per year. CAF ICC disbursements began July 1, 2012.

- Interstate Common Line Support (ICLS): ICLS is available to ILECs and is designed to help its recipients cover common line revenue requirement while ensuring the subscriber line charge (SLC) remains affordable to customers. The common line revenue requirement is related to facilities that connect end users to the carrier’s switching equipment.

OBJECTIVE, SCOPE, AND PROCEDURES

OBJECTIVE

The objective of our performance audit was to evaluate the Beneficiary's compliance with 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's Orders governing federal Universal Service Support for the HCP relative to the disbursements for the 12-month period ended December 31, 2017.

This performance audit did not constitute an audit of financial statements in accordance with *Government Auditing Standards*. We were not engaged to, and do not render an opinion on the Beneficiary's internal control over financial reporting or internal control over compliance. We caution that projecting the results of our evaluation on future periods is subject to the risks that controls may become inadequate because of changes in conditions that affect compliance.

SCOPE

The following chart summarizes the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	12/31/2015	12/31/2017	$3,542,382
High Cost Loop (HCL)	12/31/2015	12/31/2017	$5,637,939
Interstate Common Line Support (ICLS)	12/31/2015	12/31/2017	$(134,898)
Total			**$9,045,423**

AUDIT METHODOLOGY

To accomplish our audit objective, we performed the following procedures:

Reconciliation

We reconciled the December 31, 2015 and December 31, 2014, trial balances to the separations and Part 64 study inputs and then to the applicable HCP Forms, obtained explanations for any variances, and evaluated the explanations for reasonableness.

Rate Base and Investment High Cost Program Support Amount

We utilized an attribute sampling methodology[1] to select asset samples from central office equipment (COE) and cable and wire facilities (CWF) accounts. We made asset selections utilizing a random number generator from continuing property record (CPR) detail. We determined that the balances for the selected assets were properly supported by underlying documentation such as work order detail, third-party vendor invoices, materials used sheets, and time and payroll documentation for labor and related costs.

We agreed the amounts charged to work order detail and verified the proper general ledger coding under Part 32. In addition, we verified the physical existence of select assets.

Tax Filing Status

We verified the tax filing status for the Beneficiary as a cooperative and noted that income taxes were properly excluded from HCP filings.

Expenses

We utilized an attribute sampling methodology to select expense samples from operating expense accounts that impact ICLS and HCL. We made payroll sample selections from a listing of employees. We agreed the amounts from the employee paystubs to supporting documentation such as time sheets, labor distribution reports, and approved pay rates, and verified the costs were coded to the proper Part 32 account. We reviewed benefits and clearings to ensure the Beneficiary's compliance with Part 32. We made other disbursement selections from accounts payable transactions and agreed amounts to supporting documentation, reviewing for proper coding under Part 32. We selected a sample of manual journal entries to ensure reclassifications between expense accounts were appropriate and reasonable. We utilized MindBridge, a software program that uses data science and machine learning techniques to uncover outliers and anomalous transactions for 100% of the transactions within general ledger data, to identify keywords within the transaction descriptions to identify transaction for potential disallowed expenses and reviewed supporting documentation for a selection of transactions to determine if expenses were properly included or properly excluded from the cost study.

Affiliate Transactions

We performed procedures to assess the reasonableness of affiliate transactions that occurred during the period under audit. The affiliate transactions involved the transfer of assets or the provision of service between the Beneficiary and its wholly owned subsidiaries. We noted the Beneficiary is the parent of a wholly-owned controlled group of entities consisting of FTC Communications, LLC, FTC Management Group, Inc., and FTC Diversified Services, LLC. We

[1] Attribute sampling is a methodology where the selections made from a representative population are tested to determine if they contain predefined qualified characteristics (attributes).

judgmentally selected a sample of various transactions between the Beneficiary and its affiliates to determine whether the Beneficiary had recorded the transactions in accordance with 47 C.F.R. Section 32.27 and if they were categorized in the appropriate Part 32 accounts. The Beneficiary entered into the following transactions with its affiliates during the period under audit:

- Accounting services priced at fully distributed cost
- Special access charges priced at tariff rates
- Call processing and completion charges priced at prevailing price
- Internet services priced at prevailing price
- Office lease priced at fair value
- General management services priced at fully distributed cost

Revenues and Subscriber Listings

We tested general ledger accounts, subscriber bills, and other documentation to verify the accuracy and existence of revenues. We utilized an attribute sampling methodology to select revenue samples utilizing a random number generator from subscriber listings. We tested subscriber bills with procedures to ensure the lines were properly classified as residential, single-line business, or multi-line business. In addition, we reconciled the ICLS related revenues reported to the National Exchange Carrier Association (NECA) to the general ledger and billing support, and we reconciled switched related revenues reported to USAC as part of the CAF ICC filing to general ledger and billing support. We obtained subscriber listings and billing records to determine the lines or loops reported in the HCP filings agreed to supporting documentation. We reviewed the subscriber listings for duplicate lines, invalid data, and nonrevenue producing lines.

Part 64 Allocations

We (1) reviewed the Beneficiary's cost apportionment methodology to assess the reasonableness of the allocation methods and corresponding data inputs used to calculate the factors, (2) recalculated the material factors, and (3) recalculated the material amounts allocated. We also evaluated the reasonableness of the assignment between regulated, nonregulated, and common costs and the apportionment factors as compared to the regulated and nonregulated activities performed by the Beneficiary.

Central Office Equipment (COE) and Cable and Wire Facilities (CWF) Categorization

We reviewed the Beneficiary's methodology for categorizing assets including a comparison to network diagrams. We reconciled the COE and CWF amounts to the cost studies and agreed them to the applicable HCP Forms. In addition, we reviewed power and common allocations and remotely viewed via video call a judgmentally selected sample of COE assets and tested route distances of CWF for reasonableness.

Revenue Requirement

We recalculated the Beneficiary's revenue requirement using our cost allocation software program and reviewed the calculation of revenue requirement including the applications of Part 64, 36, and 69 for reasonableness. In addition, we traced cost adjustments that were not recorded in the general ledger to supporting documentation and reviewed them for reasonableness.

DETAILED AUDIT FINDINGS

Our performance audit resulted in the following detailed audit findings and recommendations with respect to the Beneficiary's compliance with the Rules, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Part 54, Subparts C, D, K, and M, Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B, as well as the FCC's orders governing federal Universal Service Support applicable to the disbursements made from the HCP during the year ended December 31, 2017.

Finding #1: 47 C.F.R. § 32.4300(a) – Incorrect Study Adjustment to Other Postretirement Employment Benefit (OPEB) liability

CONDITION

Moss Adams obtained and reviewed the Beneficiary's 2015 computation of its postretirement benefit liability, the corresponding cost study adjustments, and related supporting schedules to determine whether the Beneficiary reported amounts accurately for HCP purposes. We noted the Beneficiary provided postretirement and group health benefits to its employees, both of which were included in the calculation of the OPEB liability calculated by its third-party actuary. For its cost study, the Beneficiary removed the portion of its OPEB liability that it had not yet recorded in expenses (amounts included in the equity section of the balance sheet termed "accumulated other comprehensive loss"). We noted that the actuary had calculated a $513,306 adjustment to increase the OPEB liability, however the beneficiary excluded this amount from the cost study. As a result, the Beneficiary overstated its rate base by $513,306.

CAUSE

The process to review, approve, and prepare the 2015 cost study did not identify and adjust for the impact of group health postretirement benefits on accumulated other comprehensive loss as calculated by the actuary.

EFFECT

The exception[2] identified above resulted in overstatement of rate base of $513,306, which impacted ICLS disbursements. We increased account 4310 by $513,306 in the HCP filings to calculate the impact on ICLS. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2017, to be an overpayment of $5,380:

Support Type	Monetary Effect & Recommended Recovery
ICLS	$5,380
Total	**$5,380**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary review its policies and procedures to review adjustments provided by third parties for accuracy and to reconcile the accounts related to the post-retirement benefit plan to the valuation report prepared by the independent actuary when the report becomes available to ensure amounts reported in its HCP filings are accurate. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

Beneficiary Response

We acknowledge the results of the findings and we have implemented appropriate procedures to correct this going forward.

It is company's understanding that while this finding has a negative impact on total settlements, due to finding #2 below having positive impact to company the two findings will be netted and no additional funds are due company or USAC.

[2] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.

Finding #2: 47 C.F.R. § 32.2000(g) – Use of Group Asset Depreciation for General Support Assets

CONDITION

We obtained and reviewed the Beneficiary's depreciation calculations. The Beneficiary calculated depreciation expense on general support assets on an individual asset basis rather than using the group asset method of accounting for depreciation.

CAUSE

The Beneficiary understood that this method was a departure from the Rules. The Beneficiary elected to use specific asset depreciation to manage, or more specifically, to slow down the depreciation expense on newly acquired assets.

EFFECT

The exception identified above resulted in an understatement of depreciation expense of $495,353 which impacted ICLS disbursements. To calculate the impact on ICLS, we increased accounts 6560 and 3100 by $495,353 in the HCP filings. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2017, to be an underpayment of $89,850 and is summarized by support mechanism as follows:

Support Type	Monetary Effect & Recommended Recovery
ICLS	($89,850)
Total	**($89,850)**

RECOMMENDATION

We recommend that the Beneficiary review its policies and procedures to correct its use of specific asset depreciation for general support assets and compute depreciation expense using the group plan of accounting for depreciation. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

Beneficiary Response

We acknowledge the results of the finding and are in process to implement appropriate procedures to correct going forward. After receipt of the draft report and further review of process, company implemented the change beginning October 2020 on a going forward basis. This change required company to modify the deprecation calculation for general support assets per finding and remove the individual asset calculation to convert to mass asset or group plan process. Company will use monthly average of total asset account and calculate depreciation expense based on the monthly average asset balance.

CRITERIA

Finding	Criteria	Description
Finding #1	47 C.F.R. § 32.4300(a) (2015)	This account shall include amounts accrued to provide for such items as unfunded pensions (if actuarially determined), death benefits, deferred compensation costs and other long-term liabilities not provided for elsewhere. Subsidiary records shall be maintained to identify the nature of these items.

Finding #2	47 C.F.R. § 32.2000(g)(2) (2015)	**(2)** Depreciation charges. (i) A separate annual percentage rate for each depreciation category of telecommunications plant shall be used in computing depreciation charges. (ii) Companies, upon receiving prior approval from this Commission, or, upon prescription by this Commission, shall apply such depreciation rate, except where provisions of paragraph (g)(2)(iv) of this section apply, as will ratably distribute on a straight line basis the difference between the net book cost of a class or subclass of plant and its estimated net salvage during the known or estimated remaining service life of the plant. (iii) Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one-twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The average monthly balance shall be computed using the balance as of the first and last days of the current month. (iv) In certain circumstances and upon prior approval of this Commission, monthly charges may be determined in total or in part through the use of other methods whereby selected plant balances or portions thereof are ratably distributed over periods prescribed by this Commission. Such circumstances could include but not be limited to factors such as the existence of reserve deficiencies or surpluses, types of plant that will be completely retired in the near future, and changes in the accounting for plant. Where alternative methods have been used in accordance with this subparagraph, such amounts shall be applied separately or in combination with rates determined in accordance with paragraph (g)(2)(ii) of this section.

ATTACHMENT D

HC2019BE017

Lumos Telephone Company

Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC 2019BE017

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MOSSADAMS

EXECUTIVE SUMMARY

October 30, 2020

Teleshia Delmar, Audit and Assurance Division
Universal Service Administrative Company
700 12th St NW, Suite 900
Washington, DC 20005

Dear Teleshia Delmar:

This report represents the results of Moss Adams LLP's (we, us, our, and Moss Adams) work conducted to address the performance audit obligations relative to Lumos Telephone Company (Beneficiary), study area code 190226 for disbursements of $12,303,156 made from the federal Universal Service High Cost Program (HCP) (Disbursements) during the year ended December 31, 2018.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2018 Revision). Those standards require that we plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form our conclusions. We believe the evidence we have obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. However, our performance audit does not provide a legal determination of the Beneficiary's compliance with specified requirements.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R Part 54, Subparts C, D, K, and M; Part 51, Part 32, Subpart B as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support for the HCP relative to the disbursements (collectively, the Rules).

Based on the test work performed, our audit disclosed three detailed audit findings discussed in the Audit Results section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations.

This report is intended solely for the use of USAC, the Beneficiary, and the FCC and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

Moss Adams LLP

Overland Park, Kansas
January 4, 2021

AUDIT RESULTS

Audit Results	Monetary Effect & Recommended Recovery
Finding #1: 47 C.F.R § 54.320(b) & 47 C.F.R § 54.903(a)(1) – Lack of Supporting Documentation for Reported Access Lines: The Beneficiary did not maintain supporting documentation for its actual 2016 access line counts.	$9,396
Finding #2: 47 C.F.R § 51.917(b)(6) – Inaccurate Revenue Reported: The Beneficiary reported incorrect revenue amounts in its final 2017-18 Connect America Fund Intercarrier Compensation filings.	3,611
Finding #3: 47 C.F.R § 51.917(b)(4) & 47 C.F.R § 51.917(d)(1)(iii) – Improper inclusion of costs in Eligible Recovery: The Beneficiary improperly included the cost increments of its Tele-Relay Service fees, FCC fees, and NANPA fees in its Eligible Recovery calculations for its 2017-18 CAF-ICC filings.	1,853
Total	**$14,860**

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary for SAC 190226 for the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	CAF ICC (A)	ICLS (B)	USAC Recovery Action (A) + (B) = (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$0	$9,396	$9,396	
Finding #2	$3,611	$0	$3,611	
Finding #3	$1,853	$0	$1,853	
Mechanism **Total**	$5,464	$9,396	**$14,860**	

BACKGROUND AND PROGRAM OVERVIEW

BACKGROUND

The Beneficiary is a rate of return eligible telecommunications carrier (ETC) that provides telecommunications services, including local service and Internet to residential and business customers residing in areas of West Virginia. The Beneficiary is an average schedule company and participated in the National Exchange Carrier Association (NECA) average schedule company Common Line tariff pool. During the period under audit, the Beneficiary received High Cost Program (HCP) support based on settlement formulas and associated procedures derived from representative samples of network facilities and demand quantities rather than its own costs.

PROGRAM

USAC is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (FCC) pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the federal Universal Service Fund (USF), which is designed to ensure that all people, regardless of location or income have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations, or advocate regarding any matter of universal service policy.

The HCP, a component of the USF, ensures that consumers in rural areas of the country have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas. During the relevant audit period, the following support mechanisms were available to rate of return telecommunications carriers:

- High Cost Loop support (HCL): HCL is available for rural companies operating in services areas where the cost to provide service exceeds 115% of the national average cost per loop.

- Connect America Fund Intercarrier Compensation support (CAF ICC): CAF ICC support replaced Local Switching Support is available to incumbent local exchange carriers (ILECs) to assist them in recovering a portion of the revenue requirement related to switching investment that is not covered by the access recovery charge (ARC) billed to the end user or certain other charges billed to other carriers. This revenue requirement was frozen based on forecasted switching investment filed by eligible carriers in 2011 and is being reduced by 5% per year. CAF ICC disbursements began July 1, 2012.

- Interstate Common Line Support (ICLS): ICLS is available to ILECs and is designed to help its recipients recover common line revenue requirement while ensuring the subscriber line charge (SLC) remains affordable to customers. The common line revenue requirement is related to facilities that connect end users to the carrier's switching equipment. With the transition to Connect America Fund Broadband Loop Support (CAF BLS), 2018 was the last year for ICLS true up disbursements.

OBJECTIVE, SCOPE, AND PROCEDURES

OBJECTIVE

The objective of our performance audit was to evaluate the Beneficiary's compliance with 47 C.F.R. Part 54 Subparts C, D, K, and M; Part 51, Part 32 Subpart B (where applicable to average schedule companies), as well as FCC Orders governing federal Universal Service Support for the HCP relative to the disbursements for the 12-month period ended December 31, 2018.

This performance audit did not constitute an audit of financial statements in accordance with *Government Auditing Standards*. We were not engaged to, and do not render an opinion on the Beneficiary's internal control over financial reporting or internal control over compliance. We caution that projecting the results of our evaluation on future periods is subject to the risks that controls may become inadequate because of changes in conditions that affect compliance.

SCOPE

In the following chart, we summarize the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	7/1/2015 – 6/30/2017	12/31/2018	$12,295,734
Interstate Common Line Support (ICLS)	12/31/2016	12/31/2018	$7,422
Total			**$12,303,156**

AUDIT METHODOLOGY

To accomplish our audit objective, we performed the following procedures:

Eligibility Requirements

We obtained and reviewed the required filings and certifications made by or on behalf of the Beneficiary to ensure it was in compliance with the eligibility requirements to receive HCP support.

Revenues and Subscriber Listings

We tested general ledger accounts, subscriber bills, and other documentation to verify the accuracy and existence of revenues. We utilized an attribute sampling methodology[1] to select revenue samples from subscriber listings. We tested subscriber bills with procedures to ensure the lines were properly classified as residential, single-line business, or multi-line business. In addition, we reconciled the ICLS related revenues reported to NECA to the general ledger and billing support, and we reconciled access recovery charge revenue and switched related revenues reported to USAC as part of the CAF ICC filing to general ledger and billing support.

Access Lines & Exchanges

We obtained subscriber listings and billing records to determine the access lines used in the calculation of Common Line Revenue Requirement and reported in the HCP filings agreed to supporting documentation. We reviewed the subscriber listings for duplicate lines, invalid data, and company official lines. We confirmed affiliate access lines were not company official lines, which are specifically excluded from average schedule settlement formulas. We also verified the number of telephone serving wire center exchanges reported in NECA Tariff 4[2].

Exogenous Costs

We obtained cost support for the exogenous cost increments used in the determination of Eligible Recovery amounts for 2018 CAF-ICC disbursements. Exogenous costs included Tele-Relay Surcharges (TRS), FCC Regulatory fees, and North America Numbering Plan Administration (NANPA).

[1] Attribute sampling is a methodology where the selections made from a representative population are tested to determine if they contain predefined qualified characteristics (attributes).

[2] NECA Tariff 4 contains information related to wire centers/rating point locations providing access service in local access and transport areas (LATAs) and market areas, subtending information identifying the relationship between wire centers for the ordering and provisioning of access services and interconnection information when two or more exchange carriers are jointly providing access service within or between LATAs or market areas under separate access service tariffs.

Revenue Requirement and Eligible Recovery

We recalculated the Beneficiary's revenue requirement using NECA average schedule pool procedures published for the tariff periods January 1, 2016 and July 1, 2016 and traced the revenue requirement to the Beneficiary's ICLS Form 509. We also recalculated Eligible Recovery amounts for CAF-ICC TRP filings for the periods July 1, 2015 through June 30, 2017.

DETAILED AUDIT FINDINGS

Our performance audit resulted in the following detailed audit findings and recommendations with respect to the Beneficiary's compliance with the Rules, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Part 54, Subparts C, D, K, and M, Part 51, Part 32, Subpart B (where applicable to average schedule companies), as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support applicable to the disbursements made from the HCP during the year ended December 31, 2018.

Finding #1: 47 C.F.R. § 54.320(b) & 47 C.F.R. § 54.903(a)(1) – Lack of Supporting Documentation for Reported Access Lines

CONDITION

The Beneficiary did not maintain documentation to support its 2016 access lines used in the determination of its final Common Line Revenue Requirement reported on ICLS Form 509.[3] Specifically, the Beneficiary utilized line count reports from its field operations system for lines provisioned to customers for its monthly access line reporting to NECA. The line count reports were not retained and could not be recreated by the Beneficiary.

We obtained monthly billing system access line count reports and reconciled these reports to the Beneficiary's 2016 monthly billed revenues for 2016. We also validated the access lines included in the access line reports via attribute sampling of customer bills associated with customers listed in the access line reports. We noted the following differences between access lines supported by the Beneficiary's billing information and access lines reported to NECA for the determination of the Beneficiary's 2016 common line revenue requirement:

[3] *See* 47 C.F.R. 54.903(a)(1) (2016).

Month Reported in 2016	Access Lines Per CL Revenue Req. Development	Access Lines Per Lumos Billing support	Difference – Over (Under) Reported
January	17,003	16,991	12
February	16,930	16,924	6
March	16,847	16,796	51
April	16,761	16,721	40
May	16,669	16,609	60
June	16,604	16,554	50
July	16,389	16,442	(53)
August	16,323	16,273	50
September	16,170	16,134	36
October	16,114	16,048	66
November	16,001	15,956	45
December	16,196	15,857	339

CAUSE

The Beneficiary did not have adequate internal control procedures to ensure it retained supporting documentation for reported access lines in accordance with the HCP rules.

EFFECT

The exception[4] identified above resulted in an overstatement of reported access lines for eleven months during 2016 and an understatement of reported access lines for one month during 2016, which impacted ICLS disbursements. We recalculated the common line revenue requirement using

[4] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.

access lines supported by the Beneficiary's billing system as noted in the Condition section to calculate the impact on ICLS disbursements. We estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of ICLS support in the amount of $9,396. There was no impact to CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$9,396
CAF ICC	$0
Total	**$9,396**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish controls to ensure it maintains documentation to support information reported in its HCP filings. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Lumos Networks agrees with this finding. Until the end of 2016, Lumos Networks used a summary report of line counts to submit our monthly line counts, pulled from the service address management system side of our billing system. These reports were ran at certain points in time (snapshots) and cannot/could not be recreated subsequently to produce the same results submitted to USAC, due to customers disconnecting or changing services since 2016. However, Lumos Networks had already been in the process of redoing their data reporting system during 2016, as we recognized this lack of data integrity and ability to reconcile in the future. Therefore, as of January 1, 2017, Lumos Networks switched to using all billing system/revenue based files at the customer detail level and built by the billing period.

Finding #2: 47 C.F.R. § 51.917(b)(6) –Inaccurate Revenue Reported

CONDITION

We obtained general ledger and billing support information for actual billed interstate switched access revenue, intrastate terminating switched access, reciprocal compensation revenue and access recovery charge revenue from the Beneficiary to validate actual revenues reported and used in the Beneficiary's Eligible Recovery true-up presented in its 2017 and 2018 CAF ICC filings[5]. In our comparisons of the supporting documentation to amounts presented in the CAF ICC filings, we noted the final intrastate terminating switched access revenue in the 2017 CAF ICC filing was $2,176 lower than the billing support and general ledger information. We also noted the final intrastate terminating switched access revenue in the 2018 CAF ICC filing was $9,405 higher than the billing support and general ledger information.

CAUSE

The process to prepare, review, and approve the CAF ICC filings for the 2018 disbursement period did not detect the revenue reporting errors in the true-up calculations.

EFFECT

The exception identified above resulted in the Company reporting (1) $2,176 less Eligible Recovery than it should have in the 2017 CAF ICC filing which affected six months of 2018 HC program disbursements and (2) $9,405 more Eligible Recovery than it should have in the 2018 CAF ICC filing which affected six months of 2018 HC program disbursements. We estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of $3,611 in CAF ICC support. There was no impact to ICLS disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$0
CAF ICC	$3,611
Total	**$3,611**

[5] The 2017 CAF ICC filing is based on actual data reported for the period July 1, 2015 through June 30, 2016. The 2018 CAF ICC filing is based on actual data reported for the period July 1, 2016 through June 30, 2017.

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish additional controls to ensure final revenues reported in its CAF ICC filings reconcile to general ledger/billing support. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Lumos Networks agrees that there was a small difference in part of the final 2017 and 2018 true-up amounts filed in the CAF ICC filing compared to the general ledger and billing support information. Lumos Networks has implemented an additional step in the CAF ICC preparation and review to include comparison to a CAF True-Up Calculation worksheet that Accounting produces on a monthly basis. This worksheet uses general ledger and billing support data to track actual billed switched access revenue, reciprocal compensation revenue, and access recovery charge revenue compared to our CAF ICC estimates. Utilizing this worksheet will ensure that the CAF ICC prepared inputs for actuals will tie to both the general ledger and the billing support data.

Finding #3: 47 C.F.R § 51.917(b)(4) & 47 C.F.R. § 51.917(d)(1)(iii) – Improper Inclusion of Costs in Eligible Recovery

CONDITION

We obtained the Beneficiary general ledger account detail, supporting invoices, and incremental cost calculations for the applicable periods to validate the actual exogenous costs reported and used in the Beneficiary's Eligible Recovery true-up presented in its 2017 and 2018 CAF ICC filings. The Beneficiary reported the incremental (exogenous) costs associated with Telecommunication Relay Service (TRS) fees, FCC Regulatory fees, and North American Numbering Plan Administration (NANPA) fees in its 2017 and 2018 CAF ICC true up filings. We verified these incremental costs to general ledger account detail, supporting invoices, and incremental cost calculations for the applicable periods.

Pursuant to FCC requirements, the Beneficiary is limited in the inclusion of incremental exogenous costs only to the extent that such costs are associated with a rate that is capped in its Eligible Recovery.[6] As an average schedule company, the Beneficiary's Eligible Recovery includes its interstate

[6] See Criteria section below for Finding #3 - *In the Matter of Material to be Filed in Support of 2012 Annual Access Tariff Filings*, WCB/Pricing File No. 12-08, Order, DA 12-575, 27 FCC Rcd. 3960, 3962-63, para. 7 (2012).

switched access settlements derived by using average schedule formulas developed by the FCC;[7] those formulas do not include adjustments for exogenous costs. Because the Beneficiary's interstate switched access settlements included in its Eligible Recovery were derived from formulas that did not include exogenous costs, the Beneficiary may not include exogenous costs in its Eligible Recovery for CAF ICC purposes.

CAUSE

The process to prepare, review, and approve the CAF ICC filings for the 2018 disbursement period did not ensure the Beneficiary reported only the allowable Eligible Recovery elements in its CAF ICC filings.

EFFECT

The Beneficiary reported (1) $33,335 more in Eligible Recovery than it should have in its 2017 CAF ICC filing, affecting six months of 2018 HC program disbursements and (2) reported $29,627 less Eligible Recovery than it should have in its 2018 CAF ICC filing, affecting six months of 2018 HC program disbursements. We estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of $1,853 in CAF ICC support, with no impact to the Beneficiary's ICLS disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$0
CAF ICC	$1,853
Total	**$1,853**

[7] Under the average schedule procedures, NECA collects cost and demand data from a sample of representative cost carriers and accounting and collects demand data from a sample of average schedule carriers. NECA possesses the data for the cost companies through the Parts 64, 36, and 69 cost allocation procedures to reflect relative interstate costs per access element (interstate cost compared to total unseparated revenue requirement). These factors are applied to the dollar amounts recorded in the average schedule carrier's accounting books to produce representative interstate costs by access category. NECA then develops average schedule formulas based on the demand parameters to produce a carrier's interstate settlement formula. Wireline Competition Bureau approves the formulas which reflect how average schedule carriers' settlements are calculated. Note: a formula establishing an exogenous cost adjustment was not included.

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish additional controls to ensure its CAF ICC filings do not include incremental costs that are not attributable to the interstate switched access revenue requirement. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Lumos Networks agrees with this finding. Each year Lumos Networks receives the CAF ICC spreadsheets from a third party consultant, who also helps review and complete our USAC submissions for CAF ICC filings. This audit brought to our attention that the column in which the incremental fees of Telephone Relay Services (TRS) fee, FCC Regulatory fees, and North American Numbering Plan Administration (NANPA) fees was inadvertently considered in Lumos Telephone's CAF ICC true-up calculations. We discussed this finding with NECA and two telecommunication consulting firms and understand that in all future CAF ICC calculations, these incremental fees must be excluded.

CRITERIA

Finding	Criteria	Description
Finding #1	47 C.F.R. § 54.320(b) (2016)	All eligible telecommunications carriers shall retain all records to demonstrate to auditors that the support received was consistent with the universal service high cost program rules. This documentation must be maintained for at least ten years from the receipt of funding. All such documents shall be made available upon request to the Commission and any of its Bureaus or Offices, the Administrator, and their respective auditors.
Finding #1	47 C.F.R. § 54.903(a)(1) (2016)	Beginning July 31, 2002, each rate-of-return carrier shall submit to the Administrator in accordance with the schedule in §54.1306 the number of lines it serves, within each rate-of-return carrier study area showing residential and single-line business line counts and multi-line business line counts separately. For purposes of this report, and for purposes of computing support under this subpart, the residential and single-line business class lines reported include lines assessed the residential and single-line business End User Common Line charge pursuant to §69.104 of this chapter, and the multi-line business class lines reported include lines assessed the multi-line business End User Common Line charge pursuant to §69.104 of this chapter.
Finding #2	47 C.F.R. § 51.917(b)(6) (2016)	True-up Revenues from an access service are equal to (projected demand minus actual realized demand for that service) times the default transition rate for that service specified by § 51.909. True-up Revenues from a non-access service are equal to (projected demand minus actual realized net demand for that service) times the default transition rate for that service specified by § 20.11(b) of this chapter or § 51.705. Realized demand is the demand for which payment has been received, or has been made, as appropriate, by the time the true-up is made.
Finding #3	47 C.F.R. § 51.917(b)(4) (2012)	Revenue Requirement. Revenue Requirement is equal to a carrier's regulated operating costs plus an 11.25 percent return on a carrier's net rate base calculated in compliance with the provisions of parts 36, 65 and 69 of this chapter. For an average schedule carrier, its Revenue Requirement shall be equal to the average schedule settlements it received from the pool, adjusted to reflect an 11.25 percent rate of return, or what it would have received if it had been a participant in the pool. If the reference is to an operating segment, these references are to the Revenue Requirement associated with that segment.
Finding #3	47 C.F.R. § 51.917(d)(1)(iii) (2014)	Beginning July 1, 2014, a Rate-of-Return Carrier's eligible recovery will be equal to the 2011 Rate-of-Return Carrier Base Period Revenue multiplied by the Rate-of-Return Carrier Baseline Adjustment Factor less:

		(A) The Expected Revenues from Transitional Intrastate Access Service for the year beginning July 1, 2014, reflecting forecasted demand multiplied by the rates in the rate transition contained in § 51.909 (including the reduction in intrastate End Office Switched Access Service rates), adjusted to reflect the True-Up Adjustment for Transitional Intrastate Access Service for the year beginning July 1, 2012; **(B)** The Expected Revenues from interstate switched access for the year beginning July 1, 2014, reflecting forecasted demand multiplied by the rates in the rate transition contained in § 51.909, adjusted to reflect the True-Up Adjustment for Interstate Switched Access for the year beginning July 1, 2012; and **(C)** Expected Net Reciprocal Compensation Revenues for the year beginning July 1, 2014 using the target methodology required by § 51.705, adjusted to reflect the True-Up Adjustment for Reciprocal Compensation for the year beginning July 1, 2012. **(D)** An amount equal to True-up Revenues for Access Recovery Charges for the year beginning July 1, 2012 multiplied by negative one.
Finding #3	*In the Matter of Material to be Filed in Support of 2012 Annual Access Tariff Filings*, WC Docket No. 12-575, Order, 27 FCC Rcd 3960 para. 10 (2012).	In the *USF/ICC Transformation Order*, the Commission delegated to the Bureau and the Wireless Telecommunications Bureau the authority to revise and clarify rules as necessary to ensure that the reforms adopted in the order are properly reflected in the rules. Accordingly, in this Order, we provide the following clarification regarding this specific exogenous cost issue. ILECs will be permitted to recover any increase in TRS, regulatory, or NANPA fees through the SLC, if they are below the maximum cap. For this purpose, we grant a limited waiver of sections 69.104 and 69.152 of the Commission's rules, to the extent the rules prohibit certain carriers from charging the maximum rate of $6.50 for a residential or single-line business subscriber line or $9.20 for a multi-line business subscriber line. We also grant price cap LECs a limited waiver of section 69.152 to the extent that rule prohibits price cap carriers from charging the maximum rate of $7.00 for a non-primary residential subscriber line. For the purposes of including an increase in a mandatory fee in the SLC, price cap carriers will be permitted to raise the SLC to the maximum level permitted pursuant to sections 69.152(d)(1)(ii), 69.152(e)(1)(i), and 69.152(k)(1)(i) of the Commission's rules, and rate-of-return carriers will be permitted to raise the SLC to the maximum level permitted pursuant to sections 69.104(n)(1)(ii)(c) and 69.104(o)(1)(i) of the Commission's rules. However, if the carrier is already at the maximum SLC level, the carrier will be permitted to include that portion of increases in mandatory TRS, regulatory, or NANPA fees associated with a rate that is capped in their Eligible Recovery for the 2012 annual access charge tariff filing.

ATTACHMENT E

HC2019BE011

Poka Lambro Telephone Cooperative, Inc.
Audit ID: HC2019BE011
(SAC No.: 442131)

Performance audit for the Universal Service High Cost Program Disbursements made during the twelve-month period ended December 31, 2018

Prepared for: Universal Service Administrative Company

As of Date: January 5, 2021

KPMG LLP
1225 17th Street
Suite 800
Denver, CO 80202

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EXECUTIVE SUMMARY

January 5, 2021

Ms. Teleshia Delmar, Vice President – Audit and Assurance Division
Universal Service Administrative Company
700 12th Street, NW, Suite 900
Washington, DC 20005

Dear Ms. Delmar:

This report presents the results of our work conducted to address the performance audit objectives relative to Poka Lambro Telephone Cooperative, Inc. ("Beneficiary"), Study Area Code ("SAC") No. 442131, ("Poka" or "Beneficiary") for disbursements, of $2,681,979, made from the Universal Service High Cost Program ("HCP") during the twelve-month period ended December 31, 2018. Our work was performed during the period from November 5, 2019 to January 5, 2021, and our results are as of January 5, 2021.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards issued by the Comptroller General of the United States (2018 Revision, as amended) and *American Institute of Certified Public Accountants Consulting Standards*. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the Federal Communications Commission's ("FCC") Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP (collectively, the "Rules") relative to disbursements, of $2,681,979, made from the HCP during the twelve-month period ended December 31, 2018. Compliance with the Rules is the responsibility of the Beneficiary's management. Our responsibility is to evaluate the Beneficiary's compliance with the Rules based on our audit.

As our report further describes, KPMG identified two findings as discussed in the Audit Results and Recovery Action section. Based on these results, we estimate that disbursements made to the Beneficiary from the HCP for the twelve-month period ended December 31, 2018 were $26,014 higher than they would have been had the amounts been reported properly.

KPMG cautions that projecting the results of our evaluation to future periods is subject to the risks that controls may become inadequate because of changes in conditions or because compliance with controls may deteriorate.

In addition, we also noted other matters that we have reported to the management of the Beneficiary in a separate letter dated January 5, 2021.

This report is intended solely for the use of the Universal Service Administrative Company, the Beneficiary, and the FCC and is not intended to be and should not be relied upon by anyone other than these specified parties. This report is not confidential and may be released by USAC to a requesting third party.

Sincerely,

KPMG LLP

List of Acronyms

Acronym	Definition
ACAM	Alternative Connect America Cost Model
ARC	Access Recovery Charge
BLS	Broadband Loop Support
C.F.R.	Code of Federal Regulations
C&WF	Cable and Wire Facilities
CAF ICC	Connect America Fund Intercarrier Compensation
COE	Central Office Equipment
CLEC	Competitive Local Exchange Carrier
CPRs	Continuing Property Records
ETC	Eligible Telecommunications Carrier
FCC	Federal Communications Commission
Form 509	CAF BLS Annual Common Line Actual Cost Data Collection Form
G/L	General Ledger
HCL	High Cost Loop
HCL Form	National Exchange Carrier Association Universal Service Fund Data Collection Form
HCP	High Cost Program
ICLS	Interstate Common Line Support
ILEC	Incumbent Local Exchange Carrier
LEC	Local Exchange Carrier
NECA	National Exchange Carrier Association
Poka	Poka Lambro Telephone Cooperative, Inc.
SAC	Study Area Code
SNA	Safety Net Additive
SVS	Safety Valve Support
TPIS	Telecommunications Plant In Service
USAC	Universal Service Administrative Company
USF	Universal Service Fund

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect and Recommended Recovery[1]
HC2019BE011-F01: Inaccurate Allocations/Factors – The Beneficiary used outdated cost studies to allocate costs for general support facilities to regulated and non-regulated accounts.	$26,831
HC2019BE011-F02: Inaccurate Depreciation Calculation – The Beneficiary used beginning month balances instead of average monthly balances to compute depreciation expense as prescribed by FCC Rules.	($817)
Total Net Monetary Effect	**$26,014**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery of the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure compliance with FCC Rules and Orders.

	Support Type (A) ICLS	USAC Recovery Action	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$26,831	$26,831	
Finding #2	($817)	($817)	
Mechanism Total	**$26,014**	**$26,014**	

BACKGROUND, OBJECTIVES, SCOPE AND PROCEDURES

BACKGROUND

Program Overview

USAC is an independent not-for-profit corporation that operates under the direction of the FCC pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the USF through four support mechanisms: High Cost; Lifeline; Rural Health Care; and Schools and Libraries. These four support mechanisms ensure that all people regardless of location or income level have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations or advocate regarding any matter of universal service policy.

The High Cost Support Mechanism, also known as the HCP, ensures that consumers in all regions of the nation have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas, regardless of location or economic strata. Thus, the HCP provides support for telecommunications companies (Beneficiaries) that offer services to consumers in less-populated areas. Several legacy HCP support mechanisms are noted below:

1. HCL: HCL support is available for rural companies operating in service areas where the cost to provide service exceeds 115% of the national average cost per line. HCL support includes the following two sub-components:
    a. SNA: SNA support is available for carriers that make significant investment in rural infrastructure in years when HCL support is capped and is intended to provide carriers with additional incentives to invest in their networks.
    b. SVS: SVS support is available to rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.
2. CAF ICC: CAF ICC support is available to ILECs to recover revenue that is not covered by Access Recovery Charges (ARC) to the end user.
3. ICLS: ICLS is available to rate-of-return incumbent carriers and competitive carriers, and is designed to help carriers offset interstate access charges and to permit each rate-of-return carrier to recover its common line revenue requirement, while ensuring that its SLCs remain affordable to its customers.
4. CAF BLS: CAF BLS provides support for voice and broadband service, including stand-alone broadband. CAF BLS provides support for rate-of-return carriers to the extent that SLC caps do not permit them to recover their common line revenue requirements. CAF BLS replaced ICLS effective July 1, 2016.
5. ACAM: ACAM provides funding to rate-of-return carriers that voluntarily elected to transition to a new cost model for calculating High Cost support in exchange for meeting defined broadband build-out obligations.

USAC engaged KPMG to conduct a performance audit relating to the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $2,681,979, made from the HCP during the twelve-month period ended December 31, 2018.

Beneficiary Overview

Poka Lambro Telephone Cooperative, Inc. (SAC No.442131), the subject of this performance audit, is a rural ILEC located in Tahoka, TX that provides voice and broadband internet services to a service area of more than 4,200 square-miles in portions of West Texas.

Additionally, Poka Lambro Telephone Cooperative, Inc. has subsidiaries including Poka Lambro Fiber, Ltd, which owns and operates a fiber optic cable system and Poka Lambro Telecommunications, Ltd, a long-distance reseller that sells/installs/services telephone systems and security systems.

In the table below, we show the High Cost support disbursed by USAC to the Beneficiary during the twelve-month period ended December 31, 2018 by fund type:

High Cost Support	Disbursement Amount
Alternative Connect America Cost Model (ACAM)	$2,246,487
Connect America Fund (CAF) Intercarrier Compensation (ICC)	$342,198
Interstate Common Line Support (ICLS)	$93,294
Total	**$2,681,979**

Source: USAC

The High Cost support received by the Beneficiary during the twelve-month period ended December 31, 2018, was based on the following annual financial and operational data submitted by the Beneficiary to NECA and USAC:

- 2016 FCC Form 509, based on the twelve-month periods ended December 31, 2016 data, and
- 2016 CAF ICC Tariff Review Plan (TRP), based on program year 2016 data

The above referenced submissions capture the totals of certain pre-designated G/L Accounts including all asset accounts that roll into the TPIS account as well as certain deferred liabilities and operating expenses, subject to the allocation between regulated and non-regulated activities (Part 64 Cost Allocations), the separation between interstate and intrastate operations (Part 36 Separations) and the separation between access and non-access elements (Part 69 Separations). In addition, the Beneficiary is required to submit certain annual investment data, including the categorization of COE and C&WF on the HCP Forms.

OBJECTIVES

The audit objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $2,681,979, made from the HCP during the twelve-month period ended December 31, 2018.

SCOPE

The scope of this performance audit included, but was not limited to, review of HCP Forms or other correspondence and supporting documentation provided by the Beneficiary, assessment of the Beneficiary's methodology used to prepare or support the HCP Forms or other correspondence, and evaluation of disbursement amounts made by the Beneficiary or potentially due to the Beneficiary. The scope of our work was focused on the HCP Forms or other correspondence filed by the

Beneficiary that relate to disbursements made from the HCP during the twelve-month period ended December 31, 2018, as well as performing other procedures we considered necessary to form a conclusion relative to disbursements made from the HCP during the twelve-month period ended December 31, 2018.

KPMG identified the following areas of focus for this performance audit:[2]

1. General Procedures
2. Materiality Analysis
3. Reconciliation
4. Assets
5. Expenses
6. HCP Eligibility Forms
7. COE Categorization
8. C&WF Categorization
9. Overheads
10. Taxes
11. Part 64 Cost Allocations
12. Affiliate Transactions
13. Revenues
14. Revenue Requirement

PROCEDURES

1. General Procedures

KPMG obtained and examined the ETC designation order to determine whether the Beneficiary was designated as an ETC in the study area prior to receiving HCP support. We also obtained the Form 481 filed by the Beneficiary to determine whether the Beneficiary made the required certifications and whether the Beneficiary's supporting documentation agrees to the data reported for the certifications made.

2. Materiality Analysis

For applicable HCP Forms, we obtained the forms submitted for the period ended December 31, 2016, input the information into KPMG's HCP models, and ran a materiality analysis that increased and decreased the account balances by +/- 50%. If the impact generated a +/- 5% or $100,000 change to overall disbursements, the individual line item/account was considered material for purposes of our performance audit.

3. Reconciliation

[2] If exceptions were noted in areas other than the aforementioned in-scope areas as a result of our testing procedures and the execution of our performance audit, we identified those findings in the 'Results' section of the report.

KPMG obtained the audited 2016 financial statements and reconciled to the G/L, from the G/L we reconciled to the Part 64 cost allocation inputs and then to the applicable HCP Forms. We obtained explanations for any reconciling differences.

4. **Assets**

   KPMG utilized a monetary unit sampling methodology to select asset samples from material accounts identified in the relevant HCP Forms. Asset selections were made from CPR details, and material accounts included C&WF and certain general support asset accounts. We assessed whether asset balances were properly supported by reviewing underlying documentation such as work orders, third-party vendor invoices, and time and payroll documentation for labor-related costs; agreed dollar amounts charged to the work orders and verified proper Part 32 categorization; and validated the physical existence of selected assets.

5. **Expenses**

   KPMG utilized a monetary unit sampling methodology to select expense samples including payroll from material operating expense accounts identified in the relevant HCP Forms. Expense amounts were compared to the supporting documentation such as invoices and were reviewed for proper Part 32 account coding and categorization by expense type and nature of the costs incurred (regulated versus non-regulated activities). We also obtained and examined monthly depreciation expense and accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation.

6. **HCP Eligibility Forms**

   For the relevant HCP Forms (ICLS and CAF ICC) completeness of reported accounts was assessed via reconciliations to the audited financial statements via the 'Reconciliation' process described above. Reconciling items were discussed with the Beneficiary.

7. **COE Categorization**

   KPMG reviewed the methodology established by the Beneficiary for COE categorization including the process for updating the network map and COE cost studies as well as performing a virtual physical inspection. We assessed whether COE amounts reconciled to studies including reviewing power and common allocations.

8. **C&WF Categorization**

   KPMG reviewed the methodology established by the Beneficiary for C&WF categorization including the process for updating the network map and C&WF cost studies. We assessed whether C&WF amounts reconciled to studies and also performed a virtual route distance inspection.

9. **Overhead**

   KPMG performed a walkthrough of the overhead allocation and clearing process related to work orders and payroll for 2016. Additionally, we reviewed overhead clearing reports for a selected month and reviewed the overhead clearance process for compliance with Part 32 requirements.

10. **Taxes**

    KPMG noted that the Beneficiary is a tax-exempt cooperative. We obtained and reviewed the 2016 Form 990, and noted the Beneficiary is not required to pay federal or state income taxes on patronage activities.

11. **Part 64 Cost Allocations**

KPMG reviewed the Beneficiary's cost apportionment methodology and performed procedures to evaluate the apportionment factors which included performing a walkthrough with the Beneficiary and evaluating the reasonableness of the cost pool and regulated/non-regulated apportionment factors as compared to regulated and non-regulated activities performed by the Beneficiary, assessing the reasonableness of the allocation methods and corresponding data inputs used to calculate the material factors and recalculating each of the material factors.

12. Affiliate Transactions

KPMG performed procedures to assess the reasonableness of affiliate transactions via a joint management and operation agreement among other things that occurred during January 1, 2016 to December 31, 2016. These procedures included determining the population of affiliate transactions by reviewing the audited financial statements, trial balance, and intercompany accounts, and through inquiry, and utilizing attribute sampling to select a sample of the different types of affiliate transactions for testing. For the sample selected, we reviewed the business purpose of each transaction and determined if the transactions were recorded in accordance with 47 C.F.R. Section 32.27 and 47 C.F.R. Section 36.2 and categorized in the appropriate Part 32 accounts.

13. Revenues

KPMG examined revenue G/L accounts, invoices and other related documentation to verify the accuracy and existence of revenue account balances.

14. Revenue Requirement

KPMG reviewed the calculation of the Beneficiary's revenue requirement, including assessing the reasonableness and application of Part 64 cost allocation, Part 36 and Part 69 separations and other cost study adjustments utilized in the calculation of the common line revenue requirement. KPMG obtained the projected data reported on FCC Forms 508 and compared against associated FCC Form 509 representing actual data, as applicable. KPMG inquired of the Beneficiary regarding the process related to determination of projections related to ICLS and BLS funding mechanisms.

RESULTS

KPMG's performance audit results include a listing of findings, recommendations and Beneficiary responses, with respect to the Beneficiary's compliance with FCC requirements, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69, applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018. USAC management is responsible for any decisions and actions resulting from the findings or recommendations noted.

FINDINGS, RECOMMENDATIONS AND BENEFICIARY RESPONSES

KPMG's performance audit procedures identified two findings. The findings, including the condition, cause, effect, recommendation and Beneficiary response are as follows:

Finding # HC2019BE011-F01: 47 C.F.R. Section 64.901(a), (b) and (c)(2016) – Inaccurate Allocations/Factors

CONDITION

Through review of the Beneficiary's Part 64 allocations along with affiliate transactions, KPMG noted for the year-end December 31, 2016, the Beneficiary used outdated cost studies to determine their allocation factors for general support facilities between regulated and non-regulated accounts. See below for the variances noted between the outdated and updated amounts:

Account	Outdated study non-regulated amount	Updated study non-regulated amount	Difference to reduce or increase the regulated account by
2112 – Motor Vehicles	$165,685	$199,208	$ 33,523
2116 – Other Work Equipment	$211,754	$76,493	($135,261)
2121 – Buildings	$498,451	$1,153,473	$ 655,022
2122/2123 – Office Equipment and Furniture	$20,019	$66,056	$ 46,037
2124 – Computers	$370,857	$285,824	($85,033)
3100 – Accumulated Depreciation (General Support Assets)	$1,092,757	$1,575,762	$483,005
6112/6116 – Motor Vehicle and Other Work Equipment Expenses	$10,442	$12,555	$2,113
6121/6122/6123 – Building/Office Equipment and Furniture Expenses	$104,683	$242,248	$137,565
6124 – Computers Expense	$26,744	$20,612	($6,132)
6561- Depreciation Expense (General Support Assets)	$69,964	$85,887	$15,923

CAUSE

The Beneficiary did not update their general support facilities studies on a regular basis as such the factors utilized were not relevant for the reporting period. However, the studies were updated in 2017 using 2016 data, which was utilized in our calculations for the updated balances.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-payment of $26,831. See below for the summarization of the support mechanisms impacted by this finding:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$26,831
ACAM	N/A
CAF ICC	N/A
Total	**$26,831**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

KPMG recommends that the Beneficiary establish, document and implement procedures to address the preparation, review and approval processes related to performing periodic cost studies to determine regulated and non-regulated account factors to ensure compliance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Poka Lambro accepts this finding. Since 2017, Poka Lambro has updated the Part 64 allocations and affiliate transactions on an annual basis to ensure these allocations are current and accurate. These allocations and transactions are updated in conjunction with the annual update to Poka Lambro's Cost Allocation Manual, which is periodically reviewed by Poka Lambro's cost consultants, John Staurulakis, Inc.

Finding # HC2019BE011-F02: 47 C.F.R. Section 32.2000(g)(2016) – Inaccurate Depreciation Calculation

CONDITION

KPMG inspected the Beneficiary's general ledger and depreciation schedules to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. The Beneficiary used beginning month balances instead of average monthly balances to compute depreciation expense as prescribed by FCC Rules for the period of January 1, 2016 through December 31, 2016.

The differences noted in the Accumulated Depreciation and Depreciation Expense balances for the twelve-month period ended December 31, 2016 are as follows:

Account Description	Variance For the 12 months ended December 31, 2016
Account 3100 (2100): Accumulated Depreciation -Land and General Support Assets	($424)
Account 3100 (2210): Accumulated Depreciation -Central Office Switching Equipment	($21)
Account 3100 (2230): Accumulated Depreciation -Central Office Transmission Equipment	$1,256
Account 3100 (2410): Accumulated Depreciation - Cable and Wire Facilities	$3,971
Account 6560: Depreciation and Amortization Expense	$4,782

CAUSE

The Beneficiary had accounting system limitations as the National Information Systems Cooperative (NISC) software does not have the option of average monthly balance in the configuration that prevented them from calculating accumulated depreciation and depreciation expense in accordance with FCC Rules.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an under-payment of $817. See below for the summarization of the support mechanisms impacted by this finding:

Support Type	Monetary Effect and Recommended Recovery
ICLS	($817)
ACAM	N/A
CAF ICC	N/A
Total	**($817)**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

KPMG recommends that the Beneficiary enhance the preparation, review and approval processes governing the calculation of depreciation to ensure compliance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Poka Lambro accepts this finding. Poka Lambro has contacted its accounting software vendor and they were able to help us change the depreciation settings from beginning monthly balance to average monthly balance.

CRITERIA

Finding	Criteria	Description
#1	47 C.F.R. Section 64.901(a), (b) and (c)(2016)	"(a) Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose. (b) In assigning or allocating costs to regulated and nonregulated activities, carriers shall follow the principles described herein: (1) Tariffed services provided to a nonregulated activity will be charged to the nonregulated activity at the tariffed rates and credited to the regulated revenue account for that service. Nontariffed services, offered pursuant to a section 252(e) agreement, provided to a nonregulated activity will be charged to the nonregulated activity at the amount set forth in the applicable interconnection agreement approved by a state commission pursuant to section 252(e) and credited to the regulated revenue account for that service. (2) Costs shall be directly assigned to either regulated or nonregulated activities whenever possible. (3) Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and nonregulated activities in accordance with the following hierarchy: (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves. (ii) When direct analysis is not possible, common cost categories shall be allocated based upon an indirect, cost-causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available. (iii) When neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated based upon a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities. (4) The allocation of central office equipment and outside plant investment costs between regulated and nonregulated activities shall be based upon the relative regulated and nonregulated usage of the investment during the calendar year when nonregulated usage is greatest in comparison to regulated usage during the three calendar years beginning with the calendar year during which the investment usage forecast is filed. (c) A telecommunications carrier may not use services that are not competitive to subsidize services subject to competition. Services included in the definition of universal service shall bear no more than a reasonable share of the joint and common costs of facilities used to provide those services."

Finding	Criteria	Description
#1	47 C.F.R. Section 32.14(c)(2016)	"In the application of detailed accounting requirements contained in this part, when a regulated activity involves the common or joint use of assets and resources in the provision of regulated and nonregulated products and services, companies shall account for these activities within the accounts prescribed in this system for telephone company operations. Assets and expenses shall be subdivided in subsidiary records among amounts solely assignable to nonregulated activities, amounts solely assignable to regulated activities, and amounts related to assets used and expenses incurred jointly or in common, which will be allocated between regulated and nonregulated activities. Companies shall submit reports identifying regulated and nonregulated amounts in the manner and at the times prescribed by this Commission. Nonregulated revenue items not qualifying for incidental treatment, as provided in §32.4999(I), shall be recorded in Account 5280, Nonregulated operating revenue."
#2	47 C.F.R. Section 32.2000(g)(2)(iii)(2016)	"Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one- twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The average monthly balance shall be computed using the balance as of the first and last days of the current month."

CONCLUSION

KPMG's evaluation of the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018 identified inappropriate factors/allocations between regulated and non-regulated accounts, and improper depreciation calculation methodology. Detailed information relative to the findings is described in the Findings, Recommendations and Beneficiary Responses section above.

The combined estimated monetary impact of these findings is as follows:

Fund Type	Monetary Impact Overpayment (Underpayment)
ICLS	$ 26,014
ACAM	$ 0
CAF ICC	$ 0
Total Impact	**$ 26,014**

KPMG recommends that the Beneficiary enhance the preparation, review and approval processes related to regulated and non-regulated allocation factors and the calculation of depreciation, in accordance with FCC Rules and Orders.

ATTACHMENT F

HC2019BE023

Ragland Telephone Company

Performance Audit on Compliance with the Federal Universal Service Fund
High Cost Support Mechanism Rules
USAC Audit No. HC 2019BE023

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EXECUTIVE SUMMARY

October 30, 2020

Teleshia Delmar, Audit and Assurance Division
Universal Service Administrative Company
700 12th St NW, Suite 900
Washington, DC 20005

Dear Teleshia Delmar:

This report represents the results of Moss Adams LLP's (we, us, our, and Moss Adams) work conducted to address the performance audit obligations relative to Ragland Telephone Company (Beneficiary), study area code 250316 for disbursements of $758,222 made from the federal Universal Service High Cost Program (HCP) (Disbursements) during the year ended December 31, 2017.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2018 Revision). Those standards require that we plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form our conclusions. We believe the evidence we have obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. However, our performance audit does not provide a legal determination of the Beneficiary's compliance with specified requirements.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support for the HCP relative to the disbursements (collectively, the Rules).

Based on the test work performed, our audit disclosed three detailed audit findings discussed in the Audit Results section. For the purpose of this report, a finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations.

This report is intended solely for the use of USAC, the Beneficiary, and the FCC and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

Moss Adams LLP

Overland Park, Kansas
January 8, 2021

AUDIT RESULTS

Audit Results	Monetary Effect & Recommended Recovery
Finding #1: 47 C.F.R. § 64.901(a), (b) – Improper Inclusion of Nonregulated Assets: The Beneficiary did not remove nonregulated assets and accumulated depreciation from its HCP filings.	$3,372
Finding #2: 47 C.F.R. § 32.27(e) – Inaccurate S-Corporation Income Taxes: The Beneficiary incorrectly calculated its income taxes included in its 2016-1 HCL filing.	$1,684
Finding #3: 47 C.F.R. § 32.2000 (g)(2) – Inaccurate Depreciation Expense: The Beneficiary made errors in its calculation of depreciation expense for general support assets.	$(2,334)
Total	**$2,722**

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary for SAC 250316 for the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	HCL (A)	ICLS (B)	USAC Recovery Action (A) + (B) = (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$2,607	$765	$3,372	No Difference
Finding #2	$1,684	$0	$1,684	No Difference
Finding #3	$0	$(2,334)	$(2,334)	No Difference
Mechanism **Total**	$4,291	$(1,569)	**$2,722**	

BACKGROUND AND PROGRAM OVERVIEW

BACKGROUND

The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that provides telecommunications services, including local service and Internet to residential and business customers residing in northeastern Alabama.

PROGRAM

USAC is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (FCC) pursuant to 47 C.F.R. Part 54. USAC administers the federal Universal Service Fund (USF), which is designed to ensure that all people, regardless of location or income have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations, or advocate regarding any matter of universal service policy.

The High Cost Program (HCP), a component of the USF, ensures that consumers in rural areas of the country have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas. During the relevant audit period, the following support mechanisms were available to cost-based telecommunications carriers:

- High Cost Loop support (HCL): HCL is available for rural companies operating in services areas where the cost to provide service exceeds 115% of the national average cost per loop.
- Connect America Fund Intercarrier Compensation support (CAF ICC): CAF ICC support replaced Local Switching Support is available to ILECs to assist them in recovering a portion of the revenue requirement related to switching investment that is not covered by the access recovery charge (ARC) billed to the end user or certain other charges billed to other carriers. This revenue requirement was frozen based on forecasted switching investment filed by eligible carriers in 2011 and is being reduced by 5% per year. CAF ICC disbursements began July 1, 2012.
- Interstate Common Line Support (ICLS): ICLS is available to ILECs and is designed to help its recipients cover common line revenue requirement while ensuring the subscriber line charge (SLC) remains affordable to customers. The common line revenue requirement is related to facilities that connect end users to the carrier's switching equipment.

OBJECTIVE, SCOPE, AND PROCEDURES

OBJECTIVE

The objective of our performance audit was to evaluate the Beneficiary's compliance with 47 C.F.R. Part 54 Subparts C, D, K, and M; Part 36 Subpart F; Part 64 Subpart I; Part 69 Subparts D, E, and F; and Part 32 Subpart B, as well as FCC Orders governing federal Universal Service Support for the HCP relative to the disbursements for the 12-month period ended December 31, 2017.

This performance audit did not constitute an audit of financial statements in accordance with *Government Auditing Standards*. We were not engaged to, and therefore do not, render an opinion on the Beneficiary's internal control over financial reporting or internal control over compliance. We caution that projecting the results of our evaluation on future periods is subject to the risks that controls may become inadequate because of changes in conditions that affect compliance.

SCOPE

In the following chart, we summarize the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	12/31/2015	12/31/2017	$184,152
High Cost Loop (HCL)	12/31/2015	12/31/2017	$552,605
Interstate Common Line Support (ICLS)	12/31/2015	12/31/2017	$21,465
Total			**$758,222**

AUDIT METHODOLOGY

To accomplish our audit objective, we performed the following procedures:

Reconciliation

We reconciled the December 31, 2015 and December 31, 2014 trial balance accounts to the Part 36 separations and Part 64 cost study inputs, then to the applicable HCP Forms, and obtained explanations for any variances, and evaluated the explanations for reasonableness.

Rate Base and Investment High Cost Program Support Amount

We utilized an attribute sampling methodology[1] to select asset samples from central office equipment (COE) and cable and wire facilities (CWF) accounts. We made asset selections from continuing property record (CPR) detail. We determined that the Beneficiary had properly supported balances for the selected assets with underlying documentation, such as work order detail, third-party vendor invoices, materials used sheets, and time and payroll documentation for labor and related costs.

We agreed the amounts charged to work order detail and verified the proper general ledger coding under Part 32. In addition, we verified the physical existence of select assets.

Tax Filing Status

We verified the tax filing status for the Beneficiary and obtained and reviewed the tax expense and deferred income tax calculations, including supporting documentation, for reasonableness.

Expenses

We utilized an attribute sampling methodology to select expense samples from the Beneficiary's operating expense accounts that impact ICLS and HCL. We made payroll sample selections from a listing of employees. We agreed the amounts from the employee paystubs to supporting documentation such as time sheets, labor distribution reports, and approved pay rates, and verified the costs were coded to the proper Part 32 account. We reviewed benefits and clearings to ensure the Beneficiary's compliance with Part 32.

We made other disbursement selections from accounts payable transactions and agreed amounts to supporting documentation, reviewing for proper coding under Part 32. We selected a sample of manual journal entries to ensure reclassifications between expense accounts were appropriate and reasonable. We utilized MindBridge, a software program that uses data science and machine learning techniques to uncover outliers and anomalous transactions for 100% of the transactions within general ledger data, to identify keywords within the transaction descriptions to identify transaction for potential disallowed expenses and reviewed supporting documentation for a selection of transactions to determine if expenses were properly included or properly excluded from the cost study.

Affiliate Transactions

We performed procedures to assess the reasonableness of affiliate transactions that occurred during the period under audit. The affiliate transactions involved the transfer of assets or the provision of service between the Beneficiary and related parties. We noted the Beneficiary is

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[1] Attribute sampling is a methodology where the selections made from a representative population are tested to determine if selections contain predefined qualified characteristics (attributes).

under common control with another entity providing cable television service. We selected a sample of various transactions between the Beneficiary and its related party to determine whether the Beneficiary had recorded the transactions in accordance with 47 C.F.R. Section 32.27.

Revenues and Subscriber Listings

We tested general ledger accounts, subscriber bills, and other documentation to verify the accuracy and existence of revenues. We utilized an attribute sampling methodology to select revenue samples from subscriber listings. We tested subscriber bills with procedures to ensure the lines were properly classified as residential, single-line business, or multi-line business. In addition, we reconciled the ICLS related revenues reported to the National Exchange Carrier Association (NECA) to the general ledger and billing support, and we reconciled switched related revenues reported to USAC as part of the CAF ICC filing to general ledger and billing support. We obtained subscriber listings and billing records to determine the lines or loops reported in the HCP filings agreed to supporting documentation. We reviewed the subscriber listings for duplicate lines, invalid data, and nonrevenue producing lines.

Part 64 Allocations

We (1) reviewed the Beneficiary's cost apportionment methodology to assess the reasonableness of the allocation methods and corresponding data inputs used to calculate the factors, (2) recalculated the material factors, and (3) recalculated the material amounts allocated. We also evaluated the reasonableness of the assignment between regulated, nonregulated, and common costs and the apportionment factors as compared to the regulated and nonregulated activities performed by the Beneficiary.

Central Office Equipment (COE) and Cable and Wire Facilities (CWF) Categorization

We reviewed the Beneficiary's methodology for categorizing assets including a comparison to network diagrams. We reconciled the COE and CWF amounts to the cost studies and agreed them to the applicable HCP Forms. In addition, we reviewed common and power allocations and remotely viewed pictures a sample of COE assets and tested route distances of CWF for reasonableness.

Revenue Requirement

We recalculated the Beneficiary's revenue requirement using our cost allocation software program and reviewed the calculation of the revenue requirement including the applications of Part 64, 36, and 69 for reasonableness. In addition, we traced cost study adjustments that the Beneficiary had not recorded in the general ledger to supporting documentation and reviewed them for reasonableness.

DETAILED AUDIT FINDINGS

Our performance audit resulted in the following detailed audit findings and recommendations with respect to the Beneficiary's compliance with the Rules, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Part 54, Subparts C, D, K, and M, Part 36, Subpart F; Part 64 Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B, as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support applicable to the disbursements made from the HCP during the year ended December 31, 2017.

Finding #1: 47 C.F.R. § 64.901 (a), (b) – Improper Inclusion of Non-Regulated Assets

CONDITION

We obtained and examined the Beneficiary's general ledger, continuing property records (CPR) and cost study adjustments to determine whether the Beneficiary excluded non-regulated costs from the account balances reported in its HCP filings. The Beneficiary improperly included non-regulated email server assets of $22,905 in its regulated balances: circuit equipment asset (account 2232) and accumulated depreciation (account 3232).

CAUSE

The process to prepare, review, and approve the nonregulated cost study adjustments included in the Beneficiary's HCP filings did not identify the nonregulated equipment and properly remove it from the HCP filings.

EFFECT

The exception[2] identified above resulted in an overstatement of circuit equipment assets and accumulated depreciation of $22,905 included in the Beneficiary's HCP filings. We calculated the impact to HCL and ICLS disbursements by reducing circuit equipment assets and accumulated depreciation by $22,905 in the Beneficiary's HCP filings. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended

[2] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.

December 31, 2017, to be an overpayment of $3,372 and note that there was no impact to CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
HCL	$2,607
ICLS	$765
CAF ICC	$0
Total	**$3,372**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish a process to review its nonregulated adjustments to ensure that it removes nonregulated assets from its HCP filings. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Ragland Telephone has reclassified the equipment in question and will review its asset listing annually to determine proper non-reg. classification and allocation.

Finding #2: 47 C.F.R. § 32.27(e) – Inaccurate S-Corporation Income Taxes

CONDITION

We obtained from the Beneficiary worksheets that it used to calculate the imputed S-Corporation income tax[3] expenses for its 2016-1 HCL filing. The Beneficiary is a Sub Chapter S Corporation for income tax purposes and calculates income taxes for inclusion on HCL data line 650 as if it were a taxable corporation and derives income taxes by applying federal and state income tax rates to the net of regulated operating revenues and regulated operating expenses. The income tax calculation developed by the Beneficiary included regulated revenue minus regulated expenses ("regulated taxable income"). We reconciled the revenues and expenses to the Beneficiary's 2015 general ledger detail to its regulated balances utilized in the preparation of its HCP filings and identified an error in the regulated state taxable income calculation. The Beneficiary overstated revenues by $81,195 and

[3] *See* NECA Separations Cost Issue 3.1 Income Tax Treatment of Subchapter S Corporations, Partnerships and Certain Limited Liability Companies.

understated expenses by $41,218. Thus, the Beneficiary overstated state taxable income by $122,413 and overstated the resulting income tax expenses reported in the 2016-1 HCL filing by $4,408.

CAUSE

The process to prepare, review, and approve the 2016-1 HCL filing did not identify and correct the error in the S-Corporation income tax calculation.

EFFECT

The exception identified above resulted in an overstatement of the 2015 income taxes included in the 2016-1 HCL filing. To calculate the impact to HCL disbursements, we reduced income tax expense reported on HCL data line 650 by $4,408. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2017, to be an overpayment of HCL disbursements of $1,684. There was no impact to ICLS or CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
HCL	$1,684
ICLS	$0
CAF ICC	$0
Total	**$1,684**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish a process to review its S-Corporation income tax calculations to ensure the accuracy of the inputs used in the calculations. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Ragland Telephone will review its income tax calculation with its cost and tax consultant, as well as NECA to ensure accuracy of filing inputs.

Finding #3: 47 C.F.R. § 32.2000(g)(2) – Inaccurate Depreciation Expense

CONDITION

We obtained the Beneficiary's general ledger and depreciation records to determine whether the assets and depreciation records were accurately recorded, reconciled and tied to the Beneficiary's HCP filing. The Beneficiary did not accurately compute accumulated depreciation and depreciation expense for the vehicle asset account 2112. Specifically, the Beneficiary acquired vehicles in July 2015 and did not include those vehicles in its monthly depreciation expense computations for the period July 2015 through December 2015. The error in the Beneficiary's depreciation computation resulted in accumulated depreciation and depreciation expense for general support assets to be understated by $13,906.

CAUSE

The process to prepare, review, and approve the depreciation calculation included in the Beneficiary's HCP filings did not identify and correct the error in depreciation expense.

EFFECT

The exception identified above resulted in an understatement of accumulated depreciation and depreciation expense of $13,906, which impacted ICLS disbursements. To calculate the impact to ICLS disbursements, we increased general support accumulated depreciation and depreciation expense by $13,906 in the Beneficiary's HCP filings. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2017, to be an underpayment of ICLS of $2,334. There was no impact to HCL or CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$(2,334)
HCL	$0
CAF ICC	$0
Total	$(2,334)

RECOMMENDATION

We recommend that the Beneficiary update its policies and procedures to compute depreciation expense on asset additions when placed in service using the group asset depreciation methodology, as prescribed in § 32.2000(g)(2). In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Ragland Telephone will review its accounting policies and procedures with its accountant to ensure proper methodology and calculation.

CRITERIA

Finding	Criteria	Description
Finding #1	47 C.F.R. § 64.901 (a), (b) (2015)	(a) Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose. (b) In assigning or allocating costs to regulated and nonregulated activities, carriers shall follow the principles described herein. (1) Tariffed services provided to a nonregulated activity will be charged to the nonregulated activity at the tariffed rates and credited to the regulated revenue account for that service. Nontariffed services, offered pursuant to a section 252(e) agreement, provided to a nonregulated activity will be charged to the nonregulated activity at the amount set forth in the applicable interconnection agreement approved by a state commission pursuant to section 252(e) and credited to the regulated revenue account for that service. (2) Costs shall be directly assigned to either regulated or nonregulated activities whenever possible. (3) Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and nonregulated activities in accordance with the following hierarchy: (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves. (ii) When direct analysis is not possible, common cost categories shall be allocated based upon an indirect, cost-causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available. (iii) When neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated based upon a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities. (4) The allocation of central office equipment and outside plant investment costs between regulated and nonregulated activities shall be based upon the relative regulated and nonregulated usage of the investment

		during the calendar year when nonregulated usage is greatest in comparison to regulated usage during the three calendar years beginning with the calendar year during which the investment usage forecast is filed.
Finding #2	47 C.F.R. § 32.27(e) (2015)	Income taxes shall be allocated among the regulated activities of the carrier, its nonregulated divisions, and members of an affiliated group. Under circumstances in which income taxes are determined on a consolidated basis by the carrier and other members of the affiliated group, the income tax expense to be recorded by the carrier shall be the same as would result if determined for the carrier separately for all time periods, except that the tax effect of carry-back and carry-forward operating losses, investment tax credits, or other tax credits generated by operations of the carrier shall be recorded by the carrier during the period in which applied in settlement of the taxes otherwise attributable to any member, or combination of member, of the affiliated group.
Finding #2	*NECA Reporting Guidelines*, Guideline 3.1, Subchapter S Corporations at 58 (last updated December 2014) (referencing 47 C.F.R. § 32.27(e))	**NECA Separations Cost Issue 3.1 Income Tax Treatment of Subchapter S Corporations, Partnerships and Certain Limited Liability Companies** – "Subchapter S Corporations (S Corporations) are companies that are organized and taxed under Subchapter S of the Internal Revenue Code. Under this provision of the tax code, a pro-rata share of the S Corporation income, deductions, charitable contributions, credits, etc., are "passed through" to their shareholders who pay taxes on their pro-rata share of the S Corporation's net taxable income. This is essentially the same tax treatment as partnerships and Limited Liability Companies who pass through income to their member or members. Although no income tax is generally paid at the corporate level, S Corporations pass through their business income to their shareholders. The shareholders then pay taxes in lieu of the corporation. The relevant issue is whether the income earned by the corporation is, in fact, taxable or tax exempt. Subchapter S status is not equivalent to tax exempt status. Taxes on the income are not avoided; they are simply paid by shareholders instead of directly by the corporation. Thus, income that is taxable for C Corporations at the corporate level is similarly taxable for S Corporations but paid at the shareholder level. State decisions regarding ratemaking treatment of S Corporation taxes are mixed, with many states permitting S Corporations to recover taxes paid by shareholders in rates. On the interstate side, telephone companies have historically been permitted to recover taxes calculated on an imputed basis (*i.e.,* taxes calculated on operating income, not based on reported income)."

Finding #3	47 C.F.R. § 32.2000(g)(2) (2015)	(2) Depreciation charges. (i) A separate annual percentage rate for each depreciation category of telecommunications plant shall be used in computing depreciation charges. (ii) Companies, upon receiving prior approval from this Commission, or, upon prescription by this Commission, shall apply such depreciation rate, except where provisions of paragraph (g)(2)(iv) of this section apply, as will ratably distribute on a straight line basis the difference between the net book cost of a class or subclass of plant and its estimated net salvage during the known or estimated remaining service life of the plant. (iii) Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one-twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The average monthly balance shall be computed using the balance as of the first and last days of the current month. (iv) In certain circumstances and upon prior approval of this Commission, monthly charges may be determined in total or in part through the use of other methods whereby selected plant balances or portions thereof are ratably distributed over periods prescribed by this Commission. Such circumstances could include but not be limited to factors such as the existence of reserve deficiencies or surpluses, types of plant that will be completely retired in the near future, and changes in the accounting for plant. Where alternative methods have been used in accordance with this subparagraph, such amounts shall be applied separately or in combination with rates determined in accordance with paragraph (g)(2)(ii) of this section.

Summary of High Cost Support Mechanism Beneficiary Audit Reports Released: February - March 2021

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
Golden West-Vivian **Attachment G**	2	• Support Not Used for Intended Purposes: The cost study included expenses not related to the provisioning, maintaining, or upgrading of telecommunications services. • Inaccurate Allocation of Expenses: The cost study excluded expenses that should have been allocated to the Beneficiary using the internal cost allocation model.	$5,406,225	($36)	$0	N
Home Telephone ILEC, LLC **Attachment H**	9	• Support Not Used for Intended Purposes: The Beneficiary included transactions that were not necessary for the provision, maintenance, and upgrading of facilities	$4,134,177	($48,573)	$0	Y

Available For Public Use

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
		and services for which the support is intended. • Improper Inclusion of Non-Regulated Activities, Inadequate or Lack of Documentation for Affiliate Transactions: The Beneficiary did not exclude non-regulated amounts and failed to provide adequate documentation to support the amounts recorded for certain affiliate transactions. • Cost Allocations Between Regulated and Non-Regulated Activities Based on Outdated Inputs and Improper Inclusion of Regulated Amounts for Expenses and Assets Transactions: The Beneficiary used outdated allocation factors to allocate costs between regulated and non-				

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
		regulated activities in its accounts.				
La Harpe Telephone Company, Inc. **Attachment I**	7	• No significant findings.	$721,526	($6,888)	$0	N
Smart City Telecommunications, LLC **Attachment J**	3	• Incorrect Classification of Labor and Benefit Expenses as General Purpose Computers Expense: General-purpose computers expense included labor and benefits that were not spent maintaining physical computers or related operating systems.	$2,146,198	$115,504	$115,504	N
Wabash Telephone Cooperative, Inc. **Attachment K**	5	• Improper Inclusion of Non-Regulated Amounts (Operating Expenses): The Beneficiary did not accurately and appropriately allocate certain operating expenses between regulated and non-regulated activities, and between affiliates.	$6,913,652	$117,390	$117,390	Y

Entity Name	Number of Findings	Significant Findings	Amount of Support	Monetary Effect	USAC Management Recovery Action	Entity Disagreement
Waitsfied-Fayston Telephone Co., Inc. **Attachment L**	10	• No significant findings.	$4,891,989	($18,309)	$0	Y
Total	**36**		**$24,213,767**	**$159,088**	**$232,894**	

Available For Public Use

ATTACHMENT G

HC2019BE022

Golden West-Vivian

Limited Review Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC 2019BE022

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MOSSADAMS

EXECUTIVE SUMMARY

September 21, 2020

Teleshia Delmar, Audit and Assurance Division
Universal Service Administrative Company
700 12th St NW, Suite 900
Washington, DC 20005

Dear Teleshia Delmar:

This report represents the results of Moss Adams LLP's (we, us, our, and Moss Adams) work conducted to address the performance audit obligations relative to Golden West-Vivian (Beneficiary), study area code 391686 for disbursements of $5,406,225 made from the federal Universal Service High Cost Program (HCP) (Disbursements) during the year ended December 31, 2018.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2018 Revision). Those standards require that we plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and conclusions based on our audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form our conclusions. We believe the evidence we have obtained provides a reasonable basis for our observations and conclusions based on our audit objectives. However, our performance audit does not provide a legal determination of the Beneficiary's compliance with specified requirements.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R. Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's (FCC) orders governing federal Universal Service Support for the HCP relative to the disbursements (collectively, the Rules).

Based on the test work performed, our audit disclosed two detailed audit findings (Finding or Findings) discussed in the Audit Results section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC Management or other officials and/or details about internal operating processes or investigations.

This report is intended solely for the use of USAC, the Beneficiary, and the FCC and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

Moss Adams LLP

Spokane, Washington
January 18, 2021

AUDIT RESULTS

Audit Results	Monetary Effect & Recommended Recovery
Finding #1: 47 C.F.R. § 54.7 (a), and Report and Order FCC 18-29 – Support Not Used for Intended Purposes: The 2016 cost study included expenses that were not related to provisioning, maintaining, or upgrading telecommunications service.	$85,533
Finding #2: 47 C.F.R. § 64.901(b)(3)(i) – Inaccurate Allocation of Expenses: The 2016 cost study excluded expenses that should have been allocated to the beneficiary using the internal cost allocation model.	($85,569)
Total	**($36)**

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary of the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	Support Type ICLS (A)	Support Type HCL (B)	USAC Recovery Action (A) + (B) = (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$26,567	$58,966	$85,533	
Finding #2	($25,489)	($60,080)	($85,569)	
Mechanism Total	$1,078	($1,114)	($36)	

As the above findings represent a net underpayment, the total recommended recovery (and thus, the recommended recovery for each individual finding) is zero as USAC policy is not to issue support in the case of a net underpayment. Thus, USAC recovery action is $0.

BACKGROUND AND PROGRAM OVERVIEW

BACKGROUND

The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that provides telecommunications services, including local service and Internet to residential and business customers residing in areas of South Dakota.

PROGRAM

USAC is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (FCC) pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the federal Universal Service Fund (USF), which is designed to ensure that all people, regardless of location or income have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations, or advocate regarding any matter of universal service policy.

The High Cost Program (HCP), a component of the USF, ensures that consumers in all less populated areas of the country have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas. The HCP consists of the following support mechanisms that are available to cost-based telecommunications carriers:

- High Cost Loop support (HCL): HCL is available for rural companies operating in services areas where the cost to provide service exceeds 115% of the national average cost per loop.

- Connect America Fund Intercarrier Compensation support (CAF ICC): CAF ICC support replaced Local Switching Support and is available to ILECs to assist them in recovering a portion of the revenue requirement related to switching investment that is not covered by the access recovery charge (ARC) billed to the end user or certain other charges billed to other carriers. This revenue requirement was frozen based on forecasted switching investment filed by eligible carriers in 2011 and is being reduced by 5% per year. CAF ICC disbursements began July 1, 2012.

- Interstate Common Line Support (ICLS): ICLS is available to ILECs and is designed to help its recipients cover common line revenue requirement while ensuring the subscriber line charge (SLC) remains affordable to customers. The common line revenue requirement is related to facilities that connect end users to the carrier's switching equipment. With the transition to Connect America Fund Broadband Loop Support (CAF BLS), 2018 was the last year for ICLS true-up disbursements.

OBJECTIVE, SCOPE, AND PROCEDURES

OBJECTIVE

The objective of our performance audit was to evaluate the Beneficiary's compliance with 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's orders governing federal Universal Service Support for the HCP relative to the disbursements for the 12-month period ended December 31, 2018.

This performance audit did not constitute an audit of financial statements in accordance with *Government Auditing Standards*. We were not engaged to, and do not render an opinion on the Beneficiary's internal control over financial reporting or internal control over compliance. We caution that projecting the results of our evaluation on future periods is subject to the risks that controls may become inadequate because of changes in conditions that affect compliance.

SCOPE

The following chart summarizes the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	2016	2018	$1,950,274
High Cost Loop (HCL)	2016	2018	$3,399,270
Interstate Common Line Support (ICLS)	2016	2018	$56,681
Total			**$5,406,225**

AUDIT METHODOLOGY

To accomplish our audit objective, we performed the following procedures:

Reconciliation

We reconciled the December 31, 2016 and 2015, trial balances to the separations and Part 64 study inputs and then to the applicable HCP Forms, obtained explanations for any variances, and evaluated the explanations for reasonableness.

Rate Base and Investment High Cost Program Support Amount

We utilized an attribute sampling methodology[1] to select asset samples from central office equipment (COE) and cable and wire facilities (CWF) accounts. Asset selections were made utilizing a random number generator from continuing property record (CPR) detail. We determined that the balances for the selected assets were properly supported by underlying documentation such as work order detail, third-party vendor invoices, materials used sheets, and time and payroll documentation for labor and related costs.

We agreed the amounts charged to work order detail and verified the proper general ledger coding under Part 32. In addition, we verified the physical existence of select assets.

Tax Filing Status

We verified the tax filing status for the Beneficiary.

[1] Attribute sampling is a methodology where the selections made from a representative population are tested to determine if they contain predefined qualified characteristics (attributes).

Expenses

We utilized an attribute sampling methodology to randomly select expense samples from operating expense accounts that impact ICLS and HCL utilizing a random number generator. We made payroll sample selections from a listing of employees utilizing a random number generator. We agreed the amounts from the employee paystubs to supporting documentation such as time sheets, labor distribution reports, and approved pay rates, and verified the costs were coded to the proper Part 32 account. We reviewed benefits and clearings to ensure the Beneficiary's compliance with Part 32. We made other disbursement selections from accounts payable transactions and agreed amounts to supporting documentation, reviewing for proper coding under Part 32. We selected a sample of manual journal entries to ensure reclassifications between expense accounts were appropriate and reasonable. We utilized MindBridge, a software program that uses data science and machine learning techniques to uncover outliers and anomalous transactions for 100% of the transactions within general ledger data, to identify keywords within the transaction descriptions to identify transaction for potential disallowed expenses and reviewed supporting documentation for a selection of transactions to determine if expenses were properly included or properly excluded from the cost study.

Affiliate Transactions

We performed procedures to assess the reasonableness of affiliate transactions that occurred during the period under audit. The affiliate transactions involved the transfer of assets or the provision of service between the Beneficiary and its wholly owned subsidiaries. We noted the Beneficiary, and associated study area, is accounted for as an operating division of Golden West Telecommunications Cooperative, Inc. which is the parent of a wholly-owned controlled group of entities consisting of Golden West Technologies, Inc., Golden West Wireless, LLC and Golden West Cablevision, Inc. Additionally, we noted Golden West Telecommunications Cooperative, Inc. also operates other divisions which are separate study areas and separate beneficiaries of the HCP. As such our procedures over affiliate transactions included allocation of costs between the separate operating divisions as well as transactions with wholly-owned subsidiaries. We judgmentally selected a sample of various transactions to determine if the transactions were recorded in accordance with 47 C.F.R. Section 32.27 and categorized in the appropriate Part 32 accounts. The following transactions represent the different types of affiliates transactions entered into by the Beneficiary:

- Trunk charges priced at tariffed rates (transactions with wholly-owned subsidiaries)
- DSL wholesale charged at tariffed rates (transactions with wholly-owned subsidiaries)
- Customer, general and administrative services (allocations of costs between operating divisions)

Revenues and Subscriber Listings

We tested general ledger accounts, subscriber bills, and other documentation to verify the accuracy and existence of revenues. We utilized an attribute sampling methodology to select revenue samples from subscriber listings utilizing a random number generator. We tested subscriber bills with procedures to ensure the lines were properly classified as residential, single-line business, or multi-line business. In addition, we reconciled the ICLS related revenues reported to the National Exchange Carrier Association (NECA) to the general ledger and billing support, and we reconciled switched related revenues reported to USAC as part of the CAF ICC filing to general ledger and billing support. We obtained subscriber listings and billing records to determine the lines or loops reported in the HCP filings agreed to supporting documentation. We reviewed the subscriber listings for duplicate lines, invalid data, and nonrevenue producing lines.

Part 64 Allocations

We (1) reviewed the Beneficiary's cost apportionment methodology to assess the reasonableness of the allocation methods and corresponding data inputs used to calculate the factors, (2) recalculated the material factors, and (3) recalculated the material amounts allocated. We also evaluated the reasonableness of the assignment between regulated, nonregulated, and common costs and the apportionment factors as compared to the regulated and nonregulated activities performed by the Beneficiary.

Central Office Equipment (COE) and Cable and Wire Facilities (CWF) Categorization

We reviewed the Beneficiary's methodology for categorizing assets including a comparison to network diagrams. We reconciled the COE and CWF amounts to the cost studies and agreed them to the applicable HCP Forms. In addition, we reviewed power and common allocations and remotely viewed via video call a judgmentally-selected sample of COE assets and tested route distances of CWF for reasonableness.

Revenue Requirement

We recalculated the Beneficiary's revenue requirement using our cost allocation software program and reviewed the calculation of revenue requirement including the applications of Part 64, 36, and 69 for reasonableness. In addition, we traced cost study adjustments that were not recorded in the general ledger to supporting documentation and reviewed them for reasonableness.

DETAILED AUDIT FINDINGS

Our performance audit resulted in the following detailed audit findings and recommendations with respect to the Beneficiary's compliance with the Rules and an estimate of the monetary impact of such findings relative to 47 C.F.R. Part 54, Subparts C, D, K, and M, Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B, as well as the FCC's orders governing federal Universal Service Support applicable to the disbursements made from the HCP during the year ended December 31, 2018.

Finding #1: 47 C.F.R. § 54.7(a), and Report and Order FCC 18-29 – Support Not Used for Intended Purposes

CONDITION

We obtained general ledger detail for all regulated expense accounts for the year ended December 31, 2016 to determine whether the Beneficiary only reported in its HCP filings, expenses used for the provision, maintenance, or upgrading facilities and services for which the support was intended. We then extracted expense details using audit software to identify terms included in the general ledger entries that were specifically emphasized in FCC 15-133.[2] From our search, we identified expenses related to holiday and other gifts, sponsorships of conference and community events, membership fees and dues, donations and scholarships totaling $110,253 that were included as regulated expenses in the Beneficiary's HCP filings. These expenses are deemed ineligible for cost recovery and should not have been included in the HCP filings as they are not for the provision, maintenance, or upgrading of facilities or services for which the support is intended. [3]

CAUSE

The process to review, approve, and prepare the 2016 cost study did not identify and adjust for the expenses that should be excluded from regulated expenses.

[2] *FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821 (2015).
[3] Third Order on Reconsideration, and Notice of Proposed Rulemaking FCC 18-29(III)(A)(1) (2018).

EFFECT

The exceptions[4] identified above resulted in an overstatement of regulated expenses of $110,253, which impacted ICLS and HCL disbursements. To calculate the monetary impact of this Finding, Moss Adams reduced regulated expenses by $110,253 in the Beneficiary's cost study balances reported in its HCP filings. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018 to be an overpayment of $85,533 and is summarized by support mechanism as follows:

Support Type	Monetary Effect & Recommended Recovery
ICLS	$26,567
HCL	$58,966
Total	**$85,533**

RECOMMENDATION

We recommend USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary establish a process to identify all expenses that are disallowed and remove these expenses from the cost study and HCP Forms. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at http://www.usac.org/about/about/program-integrity/findings/common-audit-hc.aspx.

BENEFICIARY RESPONSE

We acknowledge the results of the findings and we have implemented appropriate procedures to correct this going forward.

MOSS ADAMS RESPONSE

We recommend that the Beneficiary provide a more detailed explanation of the amended or new procedures that were implemented. This information can be provided in response to the corrective action letter it will receive High Cost Program Management.

[4] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.

Finding #2: 47 C.F.R. § 64.901(b)(3)(i) – Inaccurate Allocation: Expenses

CONDITION

We obtained and examined the Beneficiary's documentation that supported its common cost allocation factors to determine whether the Beneficiary's common cost adjustments were accurately calculated for High Cost Program purposes. Pursuant to 47 § C.F.R. 64.901(b)(3)(i), beneficiaries must allocate common cost categories based upon direct analysis of the origin of the cost themselves. The Beneficiary assigns common cost allocations between multiple study areas (i.e. intercompany affiliates) based on access lines counts. We noted a variance in how the formula was applied, resulting in an understatement of common costs. We performed a recalculation of the Beneficiary's common cost allocations utilizing the proper formula and noted that general and administrative expense (6720) was understated by $219,643.

The Beneficiary is required to report accurate expenses for High Cost Program purposes. Because the Beneficiary inaccurately calculated the common cost allocations amongst its intercompany affiliates, Moss Adams concludes that these expenses were not recorded in the proper amount to the proper general ledger accounts; and thus, the cost study balances for High Cost Program purposes were inaccurate.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to ensure that allocations for intercompany common cost allocations are based on accurate calculations.

EFFECT

The exception[5] identified above resulted in an understatement of regulated expenses of $219,643, which impacted ICLS and HCL disbursements. To calculate the monetary impact of this Finding, Moss Adams increased regulated expenses by $219,643 in the Beneficiary's cost study balances reported in its High Cost filings. We estimate the monetary impact of this Finding relative to disbursements for the 12-month period ended December 31, 2018, to be an underpayment of $85,569, and is summarized by support mechanism as follows:

Support Type	Monetary Effect & Recommended Recovery
ICLS	($25,489)
HCL	($60,080)
Total	**($85,569)**

[5] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.

RECOMMENDATION

We recommend that the Beneficiary review the cost allocation manual formulas and verify that the allocation is properly applied to the joint and common costs. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at http://www.usac.org/about/about/program-integrity/findings/common-audit-hc.aspx.

BENEFICIARY RESPONSE

We acknowledge the results of the findings and we have implemented appropriate procedures to correct this going forward. We also agree that these two findings basically offset each other and feel this should conclude the audit.

MOSS ADAMS RESPONSE

We recommend that the Beneficiary provide a more detailed explanation of the amended or new procedures that were implemented. This information can be provided in response to the corrective action letter it will receive High Cost Program Management.

CRITERIA

Finding	Criteria	Description
Finding #1	47 C.F.R. § 54.7(a) (2016)	A Carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.
Finding #1	*FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821 (2015)	The Commission reminds all eligible telecommunications carriers (ETCs) that receive support from the Universal Service Fund's high-cost mechanisms (whether legacy high-cost program support or Connect America Fund support) of their obligations to use such support only for its intended purposes of maintaining and extending communications service to rural, high-cost areas of the nation. Expenditure of legacy high-cost or Connect America support for any other purpose is misuse and may subject the recipient to recovery of funding, suspension of funding, enforcement action by the Enforcement Bureau pursuant to the Communications Act of 1934 or our rules, and/or prosecution under the False Claims Act.
Finding #1	Third Order on Reconsideration, and Notice of Proposed Rulemaking FCC 18-29(III)(A)(1) (2018)	In this Report and Order, we adopt reforms to ensure that high-cost universal service support provided to eligible telecommunications carriers (ETCs) is used only for the provision, maintenance, and upgrading of facilities and services for which the high-cost support is intended pursuant to section 254(e) of the Act. We also adopt reforms to ensure that the investments and expenses that rate-of-return carriers recover through interstate rates are reasonable pursuant to section 201(b) of the Act. Our findings here do not prevent rate-of return carriers from incurring any particular investment or expense, but simply clarify the extent to which investments and expenses may be recovered through federal high-cost support and interstate rates. The rules we adopt are prospective but the underlying obligations are preexisting and many of the rules we adopt today codify existing precedent. Our rules and the used and useful standard have long governed ETCs and rate-of-return carriers' behavior. Nothing we do in this Report and Order is intended to undermine our precedent.
Finding #2	47 C.F.R. § 64.901(b)(3)(ii) (2016)	When direct analysis is not possible, common cost categories shall be allocated based upon an indirect, cost causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available.

ATTACHMENT H

HC2017LR013

Universal Service Administrative Co.

Home Telephone ILEC, LLC

Limited Review Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC2017LR013

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Universal Service Administrative Co.

EXECUTIVE SUMMARY

November 17, 2020

Denny Thompson
Director Administrative Services
Home Telephone ILEC, LLC
579 Stoney Landing Road
Moncks Corner, SC 29461

Dear Mr. Thompson:

The Universal Service Administrative Company (USAC) Audit and Assurance Division (AAD) audited the compliance of Home Telephone ILEC, LLC (Beneficiary), study area code 240527 disbursements for the year ending December 31, 2016, using the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R. Parts 32, 36, 51, 54, 64, and 69, as well as other program requirements (collectively, the Rules). Compliance with the Rules is the responsibility of the Beneficiary's management. AAD's responsibility is to make a determination regarding the Beneficiary's compliance with the Rules based on our limited review performance audit.

AAD conducted the audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2011 Revision, as amended). Those standards require that AAD plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for its findings and conclusions based on the audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form a conclusion. The evidence obtained provides a reasonable basis for AAD's findings and conclusions based on the audit objectives.

Based on the test work performed, our examination disclosed nine detailed audit findings (Findings), as discussed in the Audit Results and Recovery Action section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations. This report is intended solely for the use of USAC, the Beneficiary, and the Federal Communications Commission (FCC) and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

We appreciate the cooperation and assistance extended by your staff during the audit.

Sincerely,

Teleshia Delmar

Teleshia Delmar
USAC Vice President, Audit and Assurance Division

cc: Radha Sekar, USAC Chief Executive Officer
Vic Gaither, USAC Vice President, High Cost Division

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect and Recommended Recovery[1]
Finding #1: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support. The Beneficiary included transactions that were not necessary for the provision, maintenance, and upgrading of facilities and services for which the support is intended for High Cost Program purposes.	$67,447
Finding #2: 47 C.F.R. § 64.901(b), 47 C.F.R. § 32.27 and 47 C.F.R. § 54.320(b) – Improper Inclusion of Non-Regulated Activities, Inadequate or Lack of Documentation for Affiliate Transactions. The Beneficiary's process for removing the non-regulated portion of expenses for High Cost Program purposes was inadequate. In addition, certain expenses transactions were not supported by proper documentation partially or for the entire amount reported for High Cost purposes.	$57,595
Finding #3: 47 C.F.R. § 64.901 – Cost Allocations Between Regulated and Non-Regulated Activities Based on Outdated Inputs and Improper Inclusion of Regulated Amounts for Expenses and Assets Transactions. The Beneficiary used outdated allocation factors to allocate costs between regulated and non-regulated accounts for High Cost Program purposes.	$54,716
Finding #4: 47 C.F.R. § 64.901 – Improper Inclusion of Non-Regulated Amounts – Category 1 Investment. The Beneficiary incorrectly calculated its regulated Category 1 Cable and Wire Facilities investment for High Cost Program purposes.	$17,783
Finding #5: 47 C.F.R. § 51.917(d)(v) - Interstate Switched Access and Intrastate Terminating Switched Access Service Revenues. The intrastate terminating switched access revenues identified on the Beneficiary's billing reports and general ledger did not agree to the reported revenues for High Cost Program purposes.	$16,646
Finding #6: 47 C.F.R. § 32.4340, 47 C.F.R. § 54.1305 (c)(f)(h) and 47 C.F.R. § 36.506 – Inaccurate Net Non-Current and Current Deferred Operating Income Taxes Reporting. The Beneficiary inaccurately reported deferred taxes for High Cost Program purposes.	$3,724
Finding #7: 47 C.F.R. § 32.2000 (e)(7) and (f)(2)(iii) – Improper Continuing Property Records. The Beneficiary's continuing property records for Cable and Wire Facilities lacked sufficient detail for High Cost Program purposes.	$0
Finding #8: 47 C.F.R. § 64.901(b) and 47 C.F.R. § 54.320(b) – Improper Inclusion of Non-Regulated Balances and Lack of Documentation for Assets. The Beneficiary improperly included non-regulated assets, customer premise equipment, and/or retired assets as switching and transmission equipment in service in the amounts reported for High Cost purposes.	$(26,324)

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

Finding #9: 47 C.F.R. § 32.2000 (g)(2)(iii) – Inaccurate Depreciation Expense and Accumulated Depreciation Calculation. The Beneficiary incorrectly calculated its depreciation expense for High Cost Program purposes.	$(240,160)
Total	**$(48,573)**

USAC MANAGEMENT RESPONSE

USAC management concurs with the audit results for SAC 240527 for the High Cost Program support. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	ICLS (A)	CAF ICC (B)	USAC Recovery Action (A) + (B) [2]	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$67,447	$0	$67,447	
Finding #2	$57,595	$0	$57,595	
Finding #3	$54,716	$0	$54,716	
Finding #4	$17,783	$0	$17,783	
Finding #5	$0	$16,646	$16,646	
Finding #6	$3,724	$0	$3,724	
Finding #7	$0	$0	$0	
Finding #8	$(26,324)	$0	$(26,324)	
Finding #9	$(240,160)	$0	$(240,160)	
Mechanism Total	**$(65,219)**	**$16,646**	**$0[3]**	

As the above findings represent a net underpayment, the total recommended recovery (and thus the recommended recovery for each individual finding) is zero as USAC policy is not to issue support in the case of a net underpayment. Thus, USAC recovery action is $0.

PURPOSE, SCOPE AND PROCEDURES

PURPOSE

The purpose of our audit was to determine whether the Beneficiary complied with the Rules.

SCOPE

[2] *Id.*

[3] As the findings represent a net underpayment, the total USAC Recovery Action is $0.

In the following chart, AAD summarizes the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	2014-2015	2016	$1,239,954
Interstate Common Line Support (ICLS)	2014	2016	$2,894,223
Total			**$4,134,177**

BACKGROUND
The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that operates in South Carolina. Home Telephone ILEC, LLC is a wholly owned subsidiary of Home Telephone Inc.

PROCEDURES
AAD performed the following procedures:

A. High Cost Program Support Amount
AAD recalculated the support that the Beneficiary received for each High Cost component and determined that there were no more than nominal differences between the amounts received and those recorded in the High Cost system.

B. High Cost Program Process
AAD obtained an understanding of the Beneficiary's processes related to the High Cost Program to determine whether the Beneficiary complied with the Rules. AAD also obtained and examined documentation to determine whether the Beneficiary reported the information in its High Cost data filings based on the dates established by the Rules (*i.e.,* month or year-end, as appropriate).

C. Subscriber Listing and Billing Records
AAD obtained and examined the Beneficiary's subscriber listings and billing records. AAD used computer-assisted auditing techniques to analyze the data files and to determine whether:

- The number and type of lines in the data files agreed to the number and type of lines reported on the Beneficiary's High Cost data filings;
- The data files contained duplicate lines;
- The data files contained blank or invalid data;
- The data files contained non-revenue producing or non-working loops; and
- The lines in the data files were identified with the proper residential/single line business (Res/SLB) or multi-line business (MLB) classification.

D. Fixed Assets
AAD obtained and examined the Beneficiary's continuing property records (CPRs) and related documentation to determine whether the Beneficiary reported accurate central office switching equipment balances as well as cable and wire facility equipment balances. AAD also examined documentation and conducted a physical inventory to determine whether the Beneficiary categorized fixed assets to the proper accounts.

E. Operating Expenses

AAD obtained and examined tax reports, accrual schedules, and related documentation to determine whether the Beneficiary reported accurate tax expenses and deferred tax liabilities. AAD obtained and examined monthly depreciation and plant accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation. AAD obtained and examined the allocation method and summary schedules to determine whether the Beneficiary reported accurate benefit and rent expenses. AAD obtained and examined general ledger details for select expenses and examined invoices to support the existence of the general support, corporate operations, plant specific, and plant non-specific expenses.

F. Revenues

AAD obtained and examined the general ledger, invoices, and other related documentation to determine whether the Beneficiary reported accurate common line and other revenue balances.

G. Form 481

AAD obtained and examined the Beneficiary's FCC Form 481 (Form 481) for accuracy by comparing select reported information to the Beneficiary's data files.

DETAILED AUDIT FINDINGS

Finding #1: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support

CONDITION

AAD obtained and examined the Beneficiary's general ledger, Continuing Property Records (CPRs) and cost study adjustments documentation to determine whether High Cost Program support was only used for the provision, maintenance, or upgrading of facilities and services for which the support is intended. The Beneficiary did not exclude 33 expense transactions totaling $466,720 related to entertainment, food, charitable donations, membership fees and dues in clubs and organizations, sponsorships of conferences or community events, and gifts to employees that were not necessary for the provision, maintenance, and upgrading of facilities as summarized in the table below. [4]

Account Description	Transaction Amount
Customer Services Marketing Expense (Account 6610)	$4,510
Customer Services Marketing Expense (Account 6620)	$88
General Administration Expense (Account 6720)	$22,149
Special Charges (Account 7300)	$439,720
Total	**$466,467**

AAD clarifies that while FCC 15-33 and FCC 18-29 were released after the audit period, the FCC rule that was effective during the audit period states that, "a carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."[5] Thus, the Beneficiary should have removed the entire value of these unallowable transactions during its cost study process.

Because the Beneficiary's reported balances included unallowable transactions, AAD concludes that the 33 expenses totaling $466,467 was not used for the provision, maintenance, and upgrading of facilities and services for which the support is intended.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly exclude unallowable expenses from the amounts reported for High Cost Program purposes.[6] The Beneficiary believes that these expenses were not deemed as not includable transactions until the 2015 FCC Public Notice 15-133 was released in 2015.[7]

[4] *See FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821, 11822 (2015). *See also* 47 U.S.C. § 254(e).

[5] *See* 47 U.S.C. § 254(e).

[6] See Finding #2 for further details regarding the Beneficiary's inclusion of unallowable expenses in the amounts reported for High Cost Program purposes.

[7] Beneficiary responses to audit results summary, received Mar. 28, 2019.

EFFECT

AAD calculated the monetary effect for this finding by subtracting the portion of the expense transactions that were not adjusted by the non-regulated allocation factor from the total amount reported by the Beneficiary in the respective accounts in its High Cost filing. AAD summarized the results below:

Support Type	**Monetary Effect and Recommended Recovery**
ICLS	$67,447

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amounts identified in the Effect section above. Because the Beneficiary voluntarily elected the Alternative Connect America Cost Model (ACAM) for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> Home Telephone's position is that these costs are includable in the 2014 USF year as many categories of these costs were not deemed "not includable" until the 2015 FCC PN was released. Specifically, Home believes that charitable contributions are allowable in USF and in ratemaking for 2014 filings. At the time that the 2014 Cost Study was submitted to NECA, NECA (who admisters [sic] the filings for ICLS) reviewed the amount of Charitable Contributions that we included, and based on their criteria, determined that Home's filing was over their "capped" amount. This cap is a soft cap computed by NECA based on Charitable Contributions as a % of total Operating Expenses. After this adjustment was made, NECA approved the inclusion of "Charitable Contributions" in the 2014 Toll Cost Study. The fact that NECA, who administers this program, had in place a process to determine the maximum allowable amounts, and that they in fact reviewed Home's filing and adjusted it based on this criteria, gives a strong signal that Charitable Contributions were in fact allowable as includable expenses, albeit at a pre-determined maximum level. Documentation regarding NECA's review and edit can be found below. Other than the Charitable Contributions found in Account 7300, Home does not dispute the other findings detailed above, primarily based on their level of materiality.
>
> On a going forward basis, Home has reviewed the inclusion of eligible expenses (as the FCC PN was released in 2015), and will not include non-allowed expenses in future filings.
>
> Please be aware that Home Telephone is now an ACAM carrier and will no longer utilize reported costs in determining High Cost Support.

AAD RESPONSE

AAD clarifies that the Beneficiary should not have recorded the expenses, including charitable contributions, in regulated accounts pursuant to the FCC's Public Notice in WC Docket Nos. FCC 15-133 and FCC 18-29 which clarified existing FCC Rules and Regulations. The FCC did not make new rules but provided additional clarity on existing rules, such as:

"The Commission reminds all eligible telecommunications carriers (ETCs) that receive support from the Universal Service Fund's high-cost mechanisms (whether legacy high-cost program support or Connect America Fund support) of their obligations to use such support only for its intended purposes of maintaining and extending communications service to rural, high-cost areas of the nation…"

"Just as carriers must not use USF funds for inappropriate expenses, we remind rate-of-return carriers that section 65.450 of our rules prohibits them from including expenses in their revenue requirements unless such expenses are "recognized by the Commission as necessary to the provision" of interstate telecommunications services."

Finding #2: 47 C.F.R. § 64.901(b), 47 C.F.R. § 32.27 and 47 C.F.R. § 54.320(b) – Improper Inclusion of Non-Regulated Activities, Inadequate or Lack of Documentation for Affiliate Transactions

CONDITION

AAD obtained and examined documentation to determine whether the Beneficiary properly recorded its affiliate transactions. AAD judgmentally selected 10 transactions to review and identified exceptions with 5 of the transactions. Specifically,

1) 1 of the 5 affiliate transactions was related to a building lease recorded as general support expense (account 6120), in which the Beneficiary provided supporting documentation to show a comprehensive fair market analysis was completed in 2011. However, the Beneficiary the fair market analysis was outdated (i.e., not updated to 2014). In addition, the Beneficiary failed to provide the lease agreement or contract associated with this transaction. Due to the lack of a lease agreement, the terms were not validated to determine whether the transaction was properly classified as operating or capital lease.[8]
2) 2 of the 5 affiliate transactions were related to the general services that the Beneficiary provides its affiliated entities and were recorded as central office equipment (COE) switching expense (account 6210) and network operating expense (account 6530), respectively. However, the Beneficiary failed to provide any supporting documentation to substantiate the transaction and its fair market analysis for valuation purposes.
3) 2 of the 5 sample transactions were related to the general services that the Beneficiary provides its affiliated entities and were recorded as general expense support (account 6120) that includes both regulated and non-regulated activities. However, the Beneficiary did not excluded the non-regulated portion of the business expense.

[8] 47 C.F.R. § 32.2681.

AAD have summarized the exceptions in the table below:

Account Description[9]	Classification of the Exceptions[10] Noted	Number of Samples with Exception	Total Sample Value	Value of Exceptions[11]
COE Switching Expense (Account 6210)	Lack of Documentation	1	$2,000	$24,000
Network Operating Expense (Account 6530)	Lack of Documentation	1	$3,027	$17,762
General Support Expense (Account 6120)	Inadequate Documentation – Lease Agreement	1	$2,688	$32,255
General Support Expense (Account 6120)	Improper Inclusion of Non-Regulated Activities	2	$97,442	$278,383
	Total	**5**	**$105,157**	**$352,400**

AAD concludes that the Beneficiary did not properly record five affiliate transactions.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly record its transactions to the correct general ledger account. The Beneficiary informed AAD that it did not use the current year's percentages for non-regulated amounts that were reported for affiliate transactions.[12]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the transactions in the general ledger for the year from the total amount reported by the Beneficiary in its respective accounts in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$57,595

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate

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[9] 47 C.F.R. § 32.6210; 47 C.F.R. § 32.6720.

[10] In this report, AAD identifies and "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting from audit testing. An exception results in a finding based on the materiality of the exception.

[11] The valuation of exceptions is higher than the total value of sample as it is calculated by the number of occurrence throughout the year.

[12] Beneficiary responses to audit results summary, received Mar., 2019.

controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

Home Telephone acknowledges that that the current years' percentages were not used in the non-regulated calculations. Current balances were applied to factors calculated within the past three years. Home believes that it has been standard and approved industry practice to update these percentages on a periodic basis, and that annual updates were not required. This belief was based on the reviews that Home had been subject to by NECA and others.

Home has reviewed this internal practice and it will be corrected going forward basis for all future filings.

AAD RESPONSE

AAD clarifies that cost categories shall be allocated based upon a cost-causative linkage to another cost category applicable to the period subject to the cost study. Therefore, the factors should have been recalculated to identify the correct percentage to be applied to the balances for High Cost purposes.

Finding #3: 47 C.F.R. § 64.901 – Cost Allocations between Regulated and Non-Regulated Activities Based on Outdated Inputs and Improper Inclusion of Regulated Amounts for Expenses and Assets Transactions

CONDITION

AAD obtained and examined the Beneficiary's general ledger, cost study adjustments, and underlying support for the allocation factors to determine whether cost study adjustments were accurate, supported , cost causative and only report regulated account balances. The Beneficiary's indirect cost allocations between regulated and nonregulated activities were based on outdated inputs. Specifically, certain rate base and expense accounts were allocated based on underlying data that ranged from 2000 through 2013. The Beneficiary's allocation factors were not based on cost causative data for the 2014 data period. During the audit, AAD obtained and reviewed updated inputs related to 2014, and recalculated the non-regulated adjustments that the Beneficiary did not consider, as summarized in the table below. Thus, AAD concludes that the Beneficiary overstated (understated) the following accounts as a result of the inclusion non-regulated costs in its account balances reported for High Cost filings:

Account Description	Part 64 Cost Study As Reported A	Part 64 Cost Study Recalculation B	Variance Overstated/ (Understated) A-B
Land & General Support (Account 2110)	$14,979,708	$12,918,158	$2,061,550
Accumulated Depreciation - Land & Support Assets (Account 3100-2110)	$11,968,301	$10,306,520	$1,661,781
Depreciation Expense – General Support (Account 6560)	$697,644	$707,866	($10,222)
Depreciation Expense – Central Office Equipment (COE) Switching (Account 6560-2210)	$220,183	$224,164	($3,981)
Depreciation Expense – COE Transmission (Account 6560-2230)	$1,510,470	$1,534,647	($24,177)
Depreciation Expense – Cable and Wire Facilities (Account 6560-2431)	$3,248,412	$3,303,632	($55,220)
Network Support Expense (Account 6110)	($134,863)	($107,263)	($27,600)
General Support Expense (Account 6120)	2,697,273	2,560,062	$137,211
Central Office Transmission Expense (Account 6230)	$1,247,722	$1,391,295	($143,573)
Network Operations Expense (Account 6530)	$2,094,937	$2,205,078	($110,141)
Customer Services Marketing Expense (Account 6610)	$497,304	$264,504	$232,800
Customer Operations Service Expense (Account 6620)	$2,544,794	$1,678,394	$866,400
Executive Expense (Account 6710)	$471,207	$420,807	$50,400
General and Administrative Expense (Account 6720)	$1,734,482	$1,586,882	$147,600
Operating Taxes (Account 7200)	$789,362	$849,362	($60,000)

In addition, The Beneficiary did not apply the non-regulated allocation factor to remove the non-regulated portion on the balance for General Support Expense (account 6120) and Customer Services Marketing Expense (account 6610), even though it did include regulated allocations for General Support assets and related asset and/or expense accounts. AAD recalculated the non-regulated allocation factor based on the Beneficiary's general support expense to total plant assets ratio, applied the factor to the total of general support expense balance, and determined that the Beneficiary should have removed the non-regulated portion of the general support expense for High Cost filing as summarized on the table below.

Account Description	Transaction Amount
Customer Services Marketing Expense (Account 6610)	$18,998
General Administration Expense (Account 6720)	$75,046
Total	**$94,044**

Because the Beneficiary improperly included non-regulated amounts in its High Cost filing, AAD concludes that the Beneficiary did not report accurate general support expense and customer services marketing expense balance. The Beneficiary must separate the regulated costs from non-regulated costs reported for High Cost Program purposes.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data for High Cost Program (HCP) purposes. The preparation, review, and approval process for cost study adjustments used in the Beneficiary's HCP filings did not detect the outdated inputs. The Beneficiary informed AAD that its policy includes updating non-regulated percentages every three to four years, but applies current yearly balances to these non-regulated percentages.[13]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the over/under values from the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$54,716

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

Home Telephone acknowledges that that the current years' percentages were not used in the non-regulated calculations. Current balances were applied to factors calculated within the past three years. Home believes that it has been standard and approved industry practice to update these percentages on a periodic basis, and that annual updates were not required. This believe was based on the reviews that Home had been subject to by NECA and others.

Home has reviewed this internal practice and it will be corrected on a going forward basis for all future filings.

AAD RESPONSE

AAD clarifies that cost categories shall be allocated based upon a cost-causative linkage to another cost category applicable to the period subject to the cost study. Therefore, the factors should have been recalculated to identify the correct percentage to be applied to the balances for High Cost purposes.

Finding #4: 47 C.F.R. § 64.901 – Improper Inclusion of Non-Regulated Amounts – Category 1 Investment

CONDITION

AAD obtained and examined the Beneficiary's Cable and Wire Facilities (CWF) route allocation to determine whether the allocation of the investment were assigned to the proper category and accurately reported for

[13] Beneficiary responses to audit results summary, received Mar. 28, 2019.

High Cost Program purposes. Based on examination of the Beneficiary's CWF route allocation, AAD identified a non-regulated adjustment of $4,973,411 for the Fiber to the Home (FTTH) allocation. AAD reviewed the supporting documentation for the FTTH non-regulated adjustment and determined that it was calculated based on outdated inputs. These outdated inputs included a forecast of subscribers which was unsupported rather than the actual number of subscribers per ILEC homes. AAD recalculated the non-regulated adjustment based on updated inputs the Beneficiary provided during the audit, and the adjustment should have been $5,332,761. Therefore, the reported Category 1 investment related to GL account 2423 was overstated by $359,350. Because the Beneficiary improperly included non-regulated amounts in its High Cost filing, AAD concludes that the Beneficiary improperly included non-regulated amounts in its CWF balance.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly exclude non-regulated amounts from the amounts reported for High Cost Program purposes. The Beneficiary informed AAD that the reported non-regulated amounts were based on a future percentage utilizing a three year forecast, rather than the current year's customers.[14]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the value of the FTTH project amount from the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$17,783

RECOMMENDATION

AAD recommends USAC management seek recovery of the recommended recovery amounts identified in the Effect section above. Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> Home based FTTH non-regulated amounts on a future percentage utilizing a 3 year forecast vs. the current year's customers, as is a standard practice in the industry; however, these projectsions [sic] yielded a lower non regulated allocation than current customers, which Home acknowledges is not the intent of the FCC's rules.
>
> Home has changed procedures to use current year customer counts. As an ACAM carrier, Home will no longer utilize reported costs in determining High Cost Support.

[14] Beneficiary responses to audit results summary, received Mar. 28, 2019.

Finding #5: 47 C.F.R. § 51.917(d)(v) – Interstate Switched Access and Intrastate Terminating Switched Access Service Revenues

CONDITION

AAD obtained and examined the Beneficiary's billing reports, general ledger, and Tariff Review Plan data to determine whether the Beneficiary reported accurate Interstate Switched Access Revenues (Interstate Revenues) and Intrastate Terminating Switched Access Service Revenues (Intrastate Revenues) for High Cost Program purposes. The total Interstate and Intrastate Revenues that were identified on the Beneficiary's billing reports did not agree to the revenue amounts recorded in its general ledger. The differences are summarized below:

Program Year 2013 (07/01/2013 – 06/30/2014)	Interstate Billed Switched Access Revenues	Transitional Intrastate Access Service Revenues
As Reported/Billing Report	$578,359	$202,609
Per the General Ledger	$608,648	$205,628
Variance	**$30,289**	**$3,019**

Because the Beneficiary could not explain nor provide supporting documentation for the variances between the general ledger and its revenues on the billing report, AAD placed reliance on the Beneficiary's audited general ledger amounts for the actual Interstate and Intrastate Revenues. Per the FCC Rules, the true-up revenues from an access service are equal to the projected demand minus the actual realized demand for that service times the default transition rate for that service.[15] Thus, AAD used the general ledger as the basis for the actual realized demand for the Interstate and Intrastate revenues.[16] The Beneficiary must report accurate Interstate and Intrastate revenues for High Cost Program purposes.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to report accurate tariffed revenues for High Cost Program purposes. The Beneficiary stated that it used the billing report to report the Interstate and Intrastate revenues for High Cost Program purposes instead of the general ledger.[17]

EFFECT

AAD calculated the monetary effect for this finding by adding the recorded value of the Interstate and Intrastate revenues in the general ledger to the total amount reported by the Beneficiary in its respective accounts on the CAF ICC filing. AAD summarized the results below:

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[15] 47 CFR § 51.917(b)(6).

[16] The billing report may not represent the actual realized demand because of timing differences and other adjustments included in the general ledger.

[17] Beneficiary responses to audit results summary, received Mar. 28, 2019.

Support Type	Monetary Effect and Recommended Recovery
CAF ICC	$16,646

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above.

The Beneficiary must implement policies and procedures to ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must ensure that the information within its accounting records and the amounts reported for High Cost Program purpose are consistent. AAD recommends the Beneficiary examine the FCC Rules detailed in the Criteria section of this report to familiarize itself with the Rules related to CAF ICC documentation and reporting requirements. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> The minor discrepancy here is a result of timing differences between the Billing Reports and the GL / Annual Financials. In the future, Home will make adjusting entries to balance Billing Reports against Yearly Financials to avoid any future discrepancies.

Finding #6: 47 C.F.R. § 32.4340, 47 C.F.R. § 54.1305(c)(f)(h) and 47 C.F.R. § 36.506 – Inaccurate Net Non-Current and Current Deferred Operating Income Taxes Reporting

CONDITION

AAD obtained and examined the Beneficiary's supporting calculations for net non-current and current deferred operating income taxes (deferred taxes) reported for Interstate Common Line Support (ICLS) purposes to determine whether the Beneficiary reported accurate deferred taxes as of December 31, 2014. AAD reviewed the Beneficiary's general ledger, cost study adjustments detail and tax documentation to verify the accuracy of the information reported, and was not able to reconcile the amounts reported to the Beneficiary's supporting documentation. The Beneficiary under-reported deferred taxes in its High Cost Program (HCP) filings by $246,941. AAD determined the information used for reporting purposes was based on outdated, calendar year 2013 balances for both the general ledger amounts and cost study adjustments. Thus, AAD concludes that the Beneficiary did not report accurate deferred tax amounts.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data to report deferred taxes for HCP purposes. The preparation, review, and approval process over cost study adjustments used in the Beneficiary's HCP filings did not detect the error in the general ledger and adjustment. The

Beneficiary informed AAD that the pre-audit balances were used and they did not revise the study after the audited balances were available.[18]

EFFECT

AAD calculated the monetary effect for this finding by adding the recorded value of the omitted portion of the deferred taxes to the total amount reported by the Beneficiary in its respective accounts on the High Cost Program filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$3,724

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amounts identified in the Effect section above. Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> At the time that the Cost Study was filed with NECA, the final Audit Report was not completed nor available. It was made available after the filing later in the summer of 2015. Home acknowledeges [sic] that any pre-Audit Balances should have been updated with post-Audit balances, and a revised filing should have been made with NECA.
>
> In subsequent years, the audits were available and all Cost Study and USF filings were completed using final, audited balances.

Finding #7: 47 C.F.R. §§ 32.2000(e)(7) and (f)(2)(iii) – Improper Continuing Property Records

CONDITION

AAD obtained and examined the Beneficiary's Continuing Property Records (CPR) to determine whether the Beneficiary properly recorded and reported its assets for High Cost Program purposes. AAD noted that the Beneficiary did not provide a detailed CPR for its cable and wire facilities (CWF) assets totaling $59,487,350 per the general ledger as of December 31, 2014. The Beneficiary reported the assets per its general ledger instead of the CPR for High Cost Program purposes. In lieu of a CPR, the Beneficiary provided a CWF asset listing during the audit, which appeared to be general ledger transactions related to assets totaling $34,706,645. AAD noted that the CWF asset listing did not contain historical assets information prior to 1999 totaling $24,780,705; therefore, it did not agree to the Beneficiary's general ledger or the amount the Beneficiary reported for High Cost purposes. AAD concludes that the Beneficiary's CWF CPR was not maintained with the

[18] Beneficiary responses to audit results summary received Mar. 28, 2019.

detail required by FCC rules. The Beneficiary must maintain detailed CPR that includes the description, location, date of placement, the essential details of construction, and the original cost of the property record units.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly maintain the CWF CPR to ensure that the Beneficiary reported accurate information for High Cost Program purposes. The Beneficiary acknowledged that it did not have a complete CPR for CWF and stated that it has been able to provide its cost consultant CWF information for purposes of cost study and USF filings.[19]

EFFECT

There is no monetary effect for this finding. AAD was able to perform alternative procedures using the general ledger detail to select assets for testing to validate the assets were in service and that proper plant amounts were included in the 2014 cost study. However, detailed continuing property records are an integral component of retiring assets when they are removed from service, transferring assets between locations, and ensuring that the general ledger accurately reflects the investment in assets that are providing service in the Beneficiary's network. While there is no monetary impact of this finding, the failure to maintain continuing property records that support the full amounts in the general ledger balances for plant in service accounts increases the probability for errors and/or omissions in future High Cost Program filings.

RECOMMENDATION

Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> At the time of filing the 2014 Cost Study, Home Telephone did not have a complete Continuing Property Record (CPR) for Cable and Wire Facilities. Home was able to provide information to JSI (Cost consultant) that was believed to be sufficient, based on industry experience and prior NECA reviewd [sic], for purposes of the Cost Study and USF filings.
>
> Home has since acquired updated software that may facilitate completion of a Cable and Wire CPR or other required documentation needed for FCC filings in the near future.

[19] Beneficiary responses to audit results summary, received Mar. 28, 2019.

In addition, as an ACAM Carrier, Home will no longer utilze [sic] internal accounting records to determine their levels of USF Support.

Finding #8: 47 C.F.R. § 64.901(b) and 47 C.F.R. § 54.320(b) – Improper Inclusion of Non-Regulated Balances and Lack of Documentation for Assets

CONDITION

AAD obtained and examined the Beneficiary's Central Office Equipment (COE) Continuing Property Records (CPR) and judgmentally selected samples to determine whether the existence, classification, and categorization of investments were accurately reported for Interstate Common Line Support (ICLS) purposes. AAD identified non-regulated assets, customer premise equipment, and/or retired assets that were misclassified as switching and transmission equipment in service and were improperly included in the Beneficiary's reported balances. During the site visit, AAD identified four assets that were retired and the Beneficiary was unable to provide retirement support for the asset removals and therefore AAD could not determine the period the assets were in service during the audit period (i.e., 2014). AAD concludes that the Beneficiary overstated its account balances as reported in its High Cost filings. See details in table below:

Account Description	Part 64 Cost Study As Reported (A)	Part 64 Cost Study Recalculated (B)	Variance Overstated/ (Understated) (A – B)
COE Switching (Account 2210)	$4,371,383	$3,334,430	$1,036,953
COE Transmission (Account 2230)	$24,852,782	$24,839,992	$12,790
Accumulated Depreciation – COE Switching (Account 3100)	$3,671,552	$3,374,762	$296,790
Accumulated Depreciation – COE Transmission (Account 3100)	$18,766,521	$18,764,661	$1,860
Depreciation Expense – COE Switching (Account 6560)	$220,183	$106,118	$114,065
Depreciation Expense – COE Transmission (Account 6560)	$1,510,470	$1,508,610	$1,860

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data for High Cost Program (HCP) purposes. The preparation, review, and approval process for cost study adjustments in the Beneficiary's HCP filings did not detect that certain non-regulated assets, customer premise equipment, and/or retired assets were classified as switching and transmission equipment in service and were improperly included in the Beneficiary's reported balances. The Beneficiary informed AAD that it mistakenly did not file retirement paperwork for the selected assets.[20]

[20] Beneficiary responses to audit results summary, received Mar. 28, 2019.

EFFECT

AAD calculated the monetary effect for this finding by subtracting the overstated values from the total amount reported by the Beneficiary in the respective accounts in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	($26,324)

RECOMMENDATION

Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> Home has reviewed internal accounting practices as well as adjustments made in the course of completing the annual Cost Study, including calculation of Non Regulated adjustments and retirements. Prior findings have detailed changes that will be made with regard to allocation percentages and the application of customer and other data points. With regard to the specific asset (COE Switching) that is generating the vast majority of the impact of this finding, the asset in question has been retired and removed from reported financials subsequent to this audit.
>
> In addition, as an ACAM carrier, Home will no longer utilize reported costs in determining High Cost Support.

Finding #9: 47 C.F.R. § 32.2000(g)(2)(iii) – Inaccurate Depreciation Expense and Accumulated Depreciation Calculation

CONDITION

AAD obtained and reviewed the Beneficiary's depreciation, amortization, and related expense schedules to determine whether the Beneficiary calculated depreciation expense and accumulated depreciation expense in accordance with FCC Rules. Upon review, AAD determined that the Beneficiary did not calculate its depreciation using the average monthly balance. AAD recalculated the carrier's depreciation by taking the average of the beginning and ending balance of each month to determine the appropriate depreciation and accumulated depreciation amounts. The Beneficiary under reported depreciation expense and accumulated depreciation in its High Cost Program (HCP) filings by $1,282,019. Thus, AAD concludes that the Beneficiary did not properly calculated its depreciation and accumulated depreciation amounts.

CAUSE

The Beneficiary did not have adequate processes in place governing the proper calculation of accumulated depreciation and depreciation expense using the appropriate methodology as prescribed by FCC Rules. The

Beneficiary informed AAD that they calculated their depreciation using actual amounts, rather than using the average monthly balance.[21]

EFFECT

AAD calculated the monetary effect for this finding by adding the under reported value of the depreciation expense and accumulated depreciation to the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
ICLS	($240,160)

RECOMMENDATION

Because the Beneficiary voluntarily elected the ACAM for High Cost support since 2017 and the Beneficiary is no longer submitting cost study information for ICLS purposes, AAD does not have an additional recommendation specific for ICLS. However, the Beneficiary must implement adequate controls and procedures to ensure it retains documentation to demonstrate compliance with the Rules and reports accurate data for High Cost Program purposes.

BENEFICIARY RESPONSE

> Based on their understanding of FCC Part 32 requirements, as well as their reivew [sic] of industry practices and procedures, Home's financial software calculated monthly Depreciation Expense using monthly ending balances, or "actual" balances. Home did not use the "Monthly Averages" method. Typcially [sic], Home believed that these methods would generate a similar result, taken over the useful life of a particular assets. However, Home acknowledges that in this particular period a material differnce [sic] resulted, a difference that served to actually generate lower USF payments for Home in this actual period.
>
> In addition, as an ACAM carrier, Home will no longer utilize reported costs in determining High Cost Support

[21] Beneficiary responses to audit results summary, received Mar. 28, 2019.

CRITERIA

Finding	Criteria	Description
#1	47 C.F.R. § 54.7(a) (2014).	"A carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."
#1	47 U.S.C.§ 254 (e)(2014).	"After the date on which Commission regulations implementing this section take effect, only an eligible telecommunications carrier designated under section 214(e) of this title shall be eligible to receive specific Federal universal service support. A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Any such support should be explicit and sufficient to achieve the purposes of this section.
#1	*FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821, 11822 (2015).	"Under federal law, high-cost support provided to an ETC must be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. The following is a non-exhaustive list of expenditures that are not necessary to the provision of supported services and therefore may not be recovered through universal service support: • Personal travel; • Entertainment; • Alcohol; • Food, including but not limited to meals to celebrate personal events, such as weddings, births, or retirements; • Political contributions; • Charitable donations; • Scholarships; • Penalties or fines for statutory or regulatory violations; • Penalties or fees for any late payments on debt, loans or other payments • Membership fees and dues in clubs and organizations; • Sponsorships of conferences or community events; • Gifts to employees; and" • Personal expenses of employees, board members, family members of employees and board members, contractors, or any other individuals affiliated with the ETC, including but not limited to personal expenses for housing, such as rent or mortgages."
#1	*Connect America Fund, et al.*, WC Docket Nos. 10-90 et al., Report and Order, Third Order on Reconsideration, and Notice of Proposed Rulemaking, FCC 18-29, 33 FCC Rcd 2990, 2994, para. 10 (2018).	"In this Report and Order, we adopt reforms to ensure that high-cost universal service support provided to eligible telecommunications carriers (ETCs) is used only for the provision, maintenance, and upgrading of facilities and services for which the high-cost support is intended pursuant to section 254(e) of the Act. We also adopt reforms to ensure that the investments and expenses that rate-of-return carriers recover through interstate rates are reasonable pursuant to section 201(b) of the Act. Our findings here do not prevent rate-of-return carriers from incurring any particular investment or expense, but simply clarify the extent to which investments and expenses may be recovered through federal high-cost support and interstate rates.

Finding	Criteria	Description
		The rules we adopt are prospective but the underlying obligations are preexisting and many of the rules we adopt today codify existing precedent. Our rules and the used and useful standard have long governed ETCs and rate-of-return carriers' behavior. Nothing we do in this Report and Order is intended to undermine our precedent."
#2, 3, 4, 8	47 C.F.R. § 64.901(a)(b) (2014).	"(a) Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose. (b) In assigning or allocating costs to regulated and nonregulated activities, carriers shall follow the principles described herein. Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and nonregulated activities in accordance with the following hierarchy: (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves. (ii) When direct analysis is not possible, common cost categories shall be allocated based upon an indirect, cost causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available."
#2	47 C.F.R. § 54.320(b) (2014).	"All eligible telecommunications carriers shall retain all records required to demonstrate to auditors that the support received was consistent with the universal service high-cost program rules. This documentation must be maintained for at least ten years from the receipt of funding. All such documents shall be made available upon request to the Commission and any of its Bureaus or Offices, the Administrator, and their respective auditors."
#2	47 C.F.R. § 32.27 (2014).	"(a) Unless otherwise approved by the Chief, Wireline Competition Bureau, transactions with affiliates involving asset transfers into or out of the regulated accounts shall be recorded by the carrier in its regulated accounts as provided in paragraphs (b) through (f) of this section. (b) Assets sold or transferred between a carrier and its affiliate pursuant to a tariff, including a tariff filed with a state commission, shall be recorded in the appropriate revenue accounts at the tariffed rate. Non-tariffed assets sold or transferred between a carrier and its affiliate that qualify for prevailing price valuation, as defined in paragraph (d) of this section, shall be recorded at the prevailing price. For all other assets sold by or transferred from a carrier to its affiliate, the assets shall be recorded at no less than the higher of fair market value and net book cost. For all other assets sold by or transferred to a carrier from its affiliate, the assets shall be recorded at no more than the lower of fair market value and net book cost."
#2	47 C.F.R. § 32.2681 (2014).	"Finance leases.

Finding	Criteria	Description
		(a) This account shall include all property acquired under a finance lease. A lease qualifies as a finance lease when one or more of the following criteria is met: (1) By the end of the lease term, ownership of the leased property is transferred to the leasee. (2) The lease contains a bargain purchase option. (3) The lease term is substantially (75% or more) equal to the estimated useful life of the leased property. However, if the beginning of the lease term falls within the last 25% of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. (4) At the inception of the lease, the present value of the minimum lease payments, excluding that portion of the payments representing executory costs to be paid by the lessor, including any profit thereon, equals or exceeds 90% or more of the fair value of the leased property. However, if the beginning of the lease term falls within the last 25% of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. (b) All other leases are operating leases."
#2	47 C.F.R. § 32.6210 (2014)	"Central office switching expenses. Class B telephone companies shall use this account for expenses of the type and character required of Class A companies in Accounts 6211 through 6212."
#2	47 C.F.R. § 32.6720 (2014)	"General and administrative. This account shall include costs incurred in the provision of general and administrative services as follows: (a) Formulating corporate policy and in providing overall administration and management. Included are the pay, fees and expenses of boards of directors or similar policy boards and all board-designated officers of the company and their office staffs, e.g., secretaries and staff assistants. (b) Developing and evaluating long-term courses of action for the future operations of the company. This includes performing corporate organization and integrated long-range planning, including management studies, options and contingency plans, and economic strategic analysis. (c) Providing accounting and financial services. Accounting services include payroll and disbursements, property accounting, capital recovery, regulatory accounting (revenue requirements, separations, settlements and corollary cost accounting), non-customer billing, tax accounting, internal and external auditing, capital and operating

Finding	Criteria	Description
		budget analysis and control, and general accounting (accounting principles and procedures and journals, ledgers, and financial reports). Financial services include banking operations, cash management, benefit investment fund management (including actuarial services), securities management, debt trust administration, corporate financial planning and analysis, and internal cashier services. (d) Maintaining relations with government, regulators, other companies and the general public…."
#5	47 C.F.R. § 51.917(d)(v)(2014).	"If a Rate-of-Return Carrier receives payments for intrastate or interstate switched access services or for Access Recovery Charges after the period used to measure the adjustments to reflect the differences between estimated and actual revenues, it shall treat such payments as actual revenue in the year the payment is received and shall reflect this as an additional adjustment for that year."
#5	47 CFR § 51.917(b)(6) (2014)	"(6) True-up Revenues. True-up Revenues from an access service are equal to (projected demand minus actual realized demand for that service) times the default transition rate for that service specified by §51.909. True-up Revenues from a non-access service are equal to (projected demand minus actual realized net demand for that service) times the default transition rate for that service specified by §20.11(b) of this chapter or §51.705. Realized demand is the demand for which payment has been received, or has been made, as appropriate, by the time the true-up is made."
#6	47 C.F.R. § 32.4340 (a) (2014).	"(a) This account shall include the balance of income tax expense related to noncurrent items from regulated operations which have been deferred to later periods as a result of comprehensive interperiod tax allocation related to temporary differences that arise from regulated operations."
#6	47 C.F.R. § 54.1305 (c)(f)(h) (2014).	"(c) Unseparated accumulated depreciation and noncurrent deferred federal income taxes, attributable to Exchange Line C&WF Subcategory 1.3 investment, and Exchange Line CO Circuit Equipment Category 4.13 investment. These amounts shall be calculated as of December 31st of the calendar year preceding each July 31st filing, and shall be stated separately. (f) Unseparated corporate operations expenses, operating taxes, and the benefits and rent proportions of operating expenses. The amount for each of these categories of expense shall be the actual amount for that expense for the calendar year preceding each July 31st filing. The amount for each category of expense listed shall be stated separately. (h) Unseparated accumulated depreciation and noncurrent deferred federal income taxes attributable to local unseparated telecommunications plant investment. This amount shall be calculated as of December 31st of the calendar year preceding each July 31st filing.

Finding	Criteria	Description
#6	47 C.F.R. § 36.506 (2014).	"(a) Amounts in these accounts are maintained by plant account and are apportioned among the operations on the basis of the separations of the related plant accounts."
#7	47 C.F.R. §§ 32.2000(e)(7) and (f)(2)(iii) (2014).	"(7) The basic property record components (see paragraph (c) of this section) shall be arranged in conformity with the regulated plant accounts prescribed in this section of accounts as follows: (i) The continuing property records shall be compiled on the basis of original cost (or other book cost consistent with this system of accounts). The continuing property records shall be maintained as prescribed in §32.2000(f)(2)(iii) of this subpart in such manner as will meet the following basic objectives: (A) Provide for the verification of property record units by physical examination. (B) Provide for accurate accounting for retirements. (C) Provide data for use in connection with depreciation studies. (iii) The continuing property record shall reveal the description, location, date of placement, the essential details of construction, and the original cost (note also §32.2000(f)(3) of this subpart) of the property record units. The continuing property record and other underlying records of construction costs shall be so maintained that, upon retirement of one or more retirement units or of minor items without replacement when not included in the costs of retirement units, the actual cost or a reasonably accurate estimate of the cost of the plant retired can be determined."
#8	47 C.F.R. § 54.320(b) (2014)	"(b) All eligible telecommunications carriers shall retain all records required to demonstrate to auditors that the support received was consistent with the universal service high-cost program rules. This documentation must be maintained for at least ten years from the receipt of funding. All such documents shall be made available upon request to the Commission and any of its Bureaus or Offices, the Administrator, and their respective auditors."
#9	47 C.F.R. § 32.2000(g)(2)(iii) (2014).	"Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one-twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The average monthly balance shall be computed using the balance as of the first and last days of the current month."

ATTACHMENT I

HC2017LR015

Available For Public Use

Universal Service
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La Harpe Telephone Company, Inc.

Limited Review Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules USAC Audit No. HC2017LR015

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EXECUTIVE SUMMARY

December 1, 2020

Harry Lee
President
La Harpe Telephone Company, Inc.
109 W. 6th Street
La Harpe, KS 66751

Dear Mr. Lee:

The Universal Service Administrative Company (USAC) Audit and Assurance Division (AAD) audited the compliance of La Harpe Telephone Company, Inc. (La Harpe), study area code 411791 disbursements for the year ended December 31, 2016, using the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R. Parts 32, 36, 51, 54, 64, and 69, as well as other program requirements (collectively, the Rules). Compliance with the Rules is the responsibility of the Beneficiary's management. AAD's responsibility is to make a determination regarding the Beneficiary's compliance with the Rules based on our limited review performance audit.

AAD conducted the audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2011 Revision, as amended). Those standards require that AAD plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for its findings and conclusions based on the audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form a conclusion. The evidence obtained provides a reasonable basis for AAD's findings and conclusions based on the audit objectives.

Based on the test work performed, our examination disclosed seven detailed audit findings (Findings) as discussed in the Audit Results and Recovery Action section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations. This report is intended solely for the use of USAC, the Beneficiary, and the Federal Communications Commission (FCC) and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

We appreciate the cooperation and assistance extended by your staff during the audit.

Sincerely,

Teleshia Delmar

Teleshia Delmar
USAC Vice President, Audit and Assurance Division

cc: Radha Sekar, USAC Chief Executive Officer
Vic Gaither, USAC Vice President, High Cost Division

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect and Recommended Recovery[1]
Finding #1: 47 C.F.R. § 64.901(a)(3),(4) – Improper Inclusion of Non-Regulated Amounts. The Beneficiary did not perform a route allocation analysis and the cost related to the two leased fibers was not allocated as non-regulated, and therefore not properly removed from submitted High Cost data. In addition, the Beneficiary did not properly allocate a portion of its December monthly invoice from a vendor between regulated and non-regulated activities.	$11,515
Finding #2: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support. The Beneficiary included transactions that were not necessary for the provision, maintenance, and upgrading of facilities and services for which the support is intended for High Cost Program purposes.	$6,123
Finding #3: 47 C.F.R. 54.1305(i) and 47 C.F.R. § 54.903(a)(1) – Inaccurate Loops and Access Line Counts. The Beneficiary reported inaccurate loops and access line counts as of December 31, 2014 for High Cost Loop and Interstate Common Line Support purposes.	$4,260
Finding #4: 47 C.F.R. § 36.121(c) – Improper Power and Common Equipment Allocation. The Beneficiary did not accurately calculate the Power and Common allocation due to the use of incorrect number of access lines used for allocation purposes.	$(1,159)
Finding #5: 47 C.F.R. § 32.2000(e)(7),(f)(2)(iii) – Incomplete/Inaccurate Continuing Property Records. The Beneficiary's continuing property records (CPR) had carry forward balances for which the Beneficiary did not include the required information by the Rules. In addition, the Beneficiary included overhead and retirement entries as separate lines within the CPR while not associating them with a specific asset.	$(6,263)
Finding #6: 47 C.F.R. § 51.917(d)(v – Inaccurate Interstate Switched Access and Intrastate Terminating Switched Access Service Revenues. The Beneficiary did not report the correct amounts on their Tariff Review Plan submission. The total Interstate and Intrastate Revenues reported on the billing reports and general ledger did not agree to the revenues reported by the Beneficiary.	$(9,334)
Finding #7: 47 C.F.R. § 32.4340, 47 C.F.R. § 36.506 and 47 C.F.R. § 54.1305(a)(f) – Inaccurate Deferred Operating Taxes Reporting. The Beneficiary did not calculate and report deferred taxes 2014 High Cost Data submission.	$(12,030)
Total	**$(6,888)**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC management concurs with the audit results from the Beneficiary for SAC 411791 for the High Cost Program support. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	HCL (A)	ICLS (B)	CAF ICC (C)	USAC Recovery Action (A) + (B) + (C)[2]	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$8,799	$2,716	$0	$11,515	
Finding #2	$4,535	$1,588	$0	$6,123	
Finding #3	$4,037	$223	$0	$4,260	
Finding #4	$(926)	$(233)	$0	$(1,159)	
Finding #5	$(6,866)	$603	$0	$(6263)	
Finding #6	$0	$0	$(9,334)	$(9,334)	
Finding #7	$(10,574)	$(1,456)	$0	$(12,030)	
Mechanism Total	**$(995)**	**$3,441**	**$(9,334)**	**$0[3]**	

As the above findings represent a net underpayment, the total recommended recovery (and thus the recommended recovery for each individual finding) is zero as USAC policy is not to issue support in the case of a net underpayment. Thus, USAC recovery action is $0.

PURPOSE, SCOPE AND PROCEDURES

PURPOSE

The purpose of our audit was to determine whether the Beneficiary complied with the Rules.

SCOPE

The following chart summarizes the High Cost Program support that was included in the scope of this audit:

[2] *Id.*

[3] As the findings represent a net underpayment, the total USAC Recovery Action is $0.

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	2014-2015	2016	$117,036
High Cost Loop (HCL)	2014	2016	$473,757
Interstate Common Line Support (ICLS)	2014	2016	$130,733
Total			**$721,526**

BACKGROUND

The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that operates in Kansas.

PROCEDURES

AAD performed the following procedures:

A. High Cost Program Support Amount

AAD recalculated the support that the Beneficiary received for each High Cost component and determined that there were no more than nominal differences between the amounts received and those recorded in the High Cost system.

B. High Cost Program Process

AAD obtained an understanding of the Beneficiary's processes related to the High Cost Program to determine whether the Beneficiary complied with the Rules. AAD also obtained and examined documentation to determine whether the Beneficiary reported the information in its High Cost data filings consistent with based on the dates established by the Rules (*i.e.,* month or year-end, as appropriate).

C. Subscriber Listing and Billing Records

AAD obtained and examined the Beneficiary's subscriber listings and billing records. AAD used computer assisted auditing techniques to analyze the data files and determine whether:

- The number and type of lines in the data files agreed to the number and type of lines reported on the Beneficiary's High Cost data filings.
- The data files contained duplicate lines.
- The data files contained blank or invalid data.
- The data files contained non-revenue producing or non-working loops.
- The lines in the data files were identified with the proper residential/single line business (Res/SLB) or multi-line business (MLB) classification.

D. Fixed Assets

AAD obtained and examined the Beneficiary's continuing property records (CPRs) and related documentation to determine whether the Beneficiary reported accurate central office switching equipment balances as well as cable and wire facility equipment balances. AAD also examined documentation and conducted a physical inventory to determine whether the Beneficiary categorized fixed assets to the proper accounts.

E. Operating Expenses

AAD obtained and examined tax reports, accrual schedules, and related documentation to determine whether the Beneficiary reported accurate tax expenses and deferred tax liabilities. AAD obtained and examined monthly depreciation and plant accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation. AAD obtained and examined the allocation method and summary schedules to determine whether the Beneficiary reported accurate benefit and rent expenses. AAD obtained and examined general ledger details for select expenses and examined invoices to support the existence of the general support, corporate operations, plant specific, and plant non-specific expenses.

F. Revenues

AAD obtained and examined the general ledger, invoices, and other related documentation to determine whether the Beneficiary reported accurate common line and other revenue balances.

G. Form 481

AAD obtained and examined the Beneficiary's FCC Form 481 (Form 481) for accuracy by comparing select reported information to the Beneficiary's data files.

DETAILED AUDIT FINDINGS

Finding #1: 47 C.F.R. § 64.901(a)(3),(4) - Improper Inclusion of Non-Regulated Amounts

CONDITION

AAD obtained and examined the Beneficiary's Cable and Wire Facilities (CWF) route allocation to determine whether the Beneficiary allocated/assigned the costs of its investment to the proper category and accurately reported the costs for High Cost Program purposes. Although the Beneficiary accounted for the allocation of its original route, the Beneficiary did not perform a route allocation analysis for the new route created by the fiber-to-the-home project, which included two fibers that it leased to another entity. With respect to the costs related to the leased fibers, the Beneficiary did not allocate the cost as non-regulated, and therefore, the improperly included related costs in the CWF (account 2423), Accumulated Depreciation (account 3423) and Depreciation Expense (account 6561) in the amounts of $65,936, $29,942, and $3,737, respectively.

In addition, AAD obtained and examined documentation to determine whether the Beneficiary recorded its cost study balances, including a judgmental sample of 19 expense transactions totaling $55,546, to the proper general ledger account and whether any non-regulated amounts were excluded from the account balances reported for High Cost Program purposes. For two of the 19 expense transactions, the Beneficiary did not exclude the non-regulated portion of the value of expense. Specifically,

- For one transaction totaling $18,030 related to various telecommunication services, the Beneficiary did not allocate a portion of its December monthly invoice from a vendor between regulated and non-regulated activities, resulting in the improper inclusion of $1,615 of non-regulated activities in the Central Office Equipment (COE) Switching Expense (account 6212).

- For one transaction totaling $2,246 related to the reimbursement of a 401K retirement fund overpayment that was received by the Beneficiary and subsequently paid to employees, and was recorded to general and administrative expense for regulated activities (account 6720). In addition, in our review of the general ledger, AAD determined that the Beneficiary recorded a second transaction of the same nature for $1,300, for a collective total of $3,546. Pursuant to 47 C.F.R §32.6720, costs related to benefit investment fund management are acceptable incurred costs. However, because the Beneficiary did not incur any actual regulated expense, but rather received funds to be remitted to its employees, AAD concludes that these two reimbursements transactions were improperly included as regulated activities in the general and administrative expense account.

Because the Beneficiary improperly included non-regulated amounts in its High Cost filing, AAD concludes that the Beneficiary did not report an accurate CWF and COE balance.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly exclude non-regulated amounts from the regulated amounts reported for High Cost Program purposes. The Beneficiary informed AAD that it erred in the inclusion of the non-regulated amounts.[4] On the two leased fibers that were not allocated as non-regulated and removed from the account balances submitted for High Cost Program purposes, the Beneficiary indicated that once realized, it implemented immediately in its cost study for future USF submissions.[5]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the two leased fibers, the non-regulated portion of the COE switching expense and the two reimbursements transactions of the general and administrative expense from the total amount reported by the Beneficiary in the respective accounts in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
HCL	$8,799
ICLS	2,716[6]
Total	**$11,515**

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amounts identified in the Effect section above, subject to netting of the underpayments noted in other findings in this audit report. The Beneficiary must ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describe how the Beneficiary will remove non-regulated transactions from the account balances submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> In the case of each of the samples discussed within this finding, the original instances occurred in error and were quickly remedied upon realization of this error. In the case of not including the leased fibers, these were properly documented by segment within the route determined to contain fiber leases and removed every year since. Where expenses were determined to not be in accordance within Part 32 rules, the company has setup processes to review expense allocations upon yearend finalization.

[4] Beneficiary responses to audit results summary, received Jan. 17, 2019.
[5] *Id.*
[6] The Beneficiary elected not to participate in the National Exchange Carrier Association (NECA) pool; therefore, NECA did not calculate the ICLS monetary effect for this Finding. AAD provided the Beneficiary with the amounts that needed to be changed based on the results of this Finding and the Beneficiary performed a recalculation to determine its ICLS monetary effect.

Finding #2: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support

CONDITION

AAD obtained and examined documentation to determine whether the Beneficiary recorded its cost study balances, including a judgmental sample of 19 expenses totaling $55,546 to determine whether only costs necessary for the provision, maintenance, or upgrading of facilities were included in the account balances reported for High Cost Program purposes. AAD identified transactions that were not necessary for the provision, maintenance, and upgrading of facilities and services for which the support is intended. One expense transaction was for the 2014 association dues paid to the Kansas Rural Independent Telecommunications Coalition (KRITC) for $2,989 that was related to lobbying and recorded in general and administrative expense (account 6720). The original invoice amount was $5,978. Per a letter provided by the KRITC, 50% of the dues were determined to be nondeductible, therefore 50% of the invoice amount or $2,989 was not an allowable expense. In addition, in our examination of the general ledger, AAD noted that the Beneficiary recorded a second transaction of the same nature for the 2015 KRITC association dues, totaling $6,063.[7] AAD also noted that the Beneficiary included two transactions in its general ledger with the memo field noted as relating to lobbying expense totaling $1,432 in special charges included in the non-operating income and expense (account 7300).

Because the Beneficiary's reported balances included unallowable transactions, AAD concludes that four transactions totaling $10,484 were not necessary for the provision, maintenance, and upgrading of facilities and services for which the support is intended.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly exclude unallowable expenses from the amounts reported for High Cost Program purposes. The Beneficiary informed AAD that the lobbying expenses were only shown as an expense disallowance in the 2014 cost study, as opposed to a study adjustment, and these charges have since been removed via a separations study adjustment.[8]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the unallowable expense transactions from the total amount reported by the Beneficiary in the respective accounts in its High Cost filing. AAD summarized the results below:

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[7] AAD deemed this entire amount was unallowable.

[8] Beneficiary responses to audit results summary, received Jan. 17, 2019. Account 7370 was included in the "Expense Reclassifications" cost study adjustments worksheet, but had no actual dollar amount assigned. Therefore, no adjusting entry was made to remove the lobbying expense from cost study balances.

Support Type	Monetary Effect and Recommended Recovery
HCL	$4,535
ICLS	1,588[9]
Total	**$6,123**

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amounts identified in the Effect section above, subject to netting of the underpayments noted in other findings in this audit report.

The Beneficiary must ensure it has an adequate system to only use High Cost Program support for the provision, maintenance, and upgrading of facilities and services for which the support is intended, and must maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describes how the Beneficiary will remove transactions from the account balances that are not related to the provision, maintenance, and upgrading of facilities and services for which the support is intended to ensure exclusion from costs submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> Since discovering this issue, these charges nonregulated charges have been removed from the study via a study adjustment where applicable. Concerning the amount incurred for a prepayment, the company has ensured that expenses are recorded in the correct period where they should be recovered.

Finding #3: 47 C.F.R. 54.1305(i) and 47 C.F.R. § 54.903(a)(1) – Inaccurate Loops and Access Line Counts

CONDITION

AAD obtained and examined the Beneficiary's subscriber listing to determine whether the Beneficiary reported accurate loops and access line counts as of December 31, 2014 for High Cost Loop (HCL) and Interstate Common Line Support (ICLS) purposes. AAD identified the following differences between the Beneficiary's subscriber listing and the loops and access line counts it reported:

[9] *See supra* n.6.

	Total Loops (HCL)	Residential/Single Line Business (ICLS)
Loops/Access Line Counts Reported	260	221
Eligible Loops/Access Lines per Subscriber Listing	268	225
Difference: Under-Reported	**(8)**	**(4)**

Because the Beneficiary's supporting documentation did not agree to what it reported, AAD concludes that the Beneficiary reported inaccurate access line and working loop counts.[10]

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data to report the correct number of loops and access line counts for High Cost Program purposes. The Beneficiary informed AAD that this instance occurred in error and the Beneficiary will review line count accuracy upon year-end finalization.[11]

EFFECT

AAD calculated the monetary effect for this finding as follows:

- For the under-reported loop count: AAD added the number of under-reported loops to the total amount reported by the Beneficiary in its High Cost filing.
- For the under-reported access line count: AAD added the annualized revenue per loop of the under-reported lines to the Subscriber Line Charge Revenue amount reported by the Beneficiary in its High Cost filing.

AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
HCL	$4,037
ICLS	$223[12]
Total	**$4,260**

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amounts identified in the Effect section above, subject to netting of the underpayments noted in other findings in this audit report.

The Beneficiary must ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describes how the Beneficiary accumulates and reconciles loop/access lines between its billing and other loop/line count systems to what is submitted for High Cost Programs purposes. In addition, the Beneficiary can learn more about documentation and

[10] 47 C.F.R. 54.903(a)(1) and 47 C.F.R. 54.1305(i).
[11] Beneficiary responses to audit results summary, received Jan. 17, 2019.
[12] *See supra* n.6.

reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Company has implemented processes to better review monthly line count accuracy and the documentation is now maintained by the billing vendor.

Finding #4: 47 C.F.R. § 36.121(c) – Improper Power and Common Equipment Allocation

CONDITION

AAD obtained and examined the Beneficiary's supporting documentation to determine whether the Beneficiary's power and common (P&C) equipment allocations were correctly calculated for High Cost Program purposes. AAD determined that the Beneficiary's calculation used to allocate power and common equipment among Central Office Equipment (COE) accounts was incorrect. The Beneficiary did not accurately calculate the power and common allocation due to the incorrect number of access lines it used for allocation purposes.[13] Based on this exception, AAD recalculated the power and common allocation, based on the correct number of access lines, to the COE amounts and identified the following differences, as summarized below:

	Part 36 Cost Study As Reported (A)	**Part 36 Cost Study AAD Recalculation (B)**	**Variance Overstated/ (Understated) (A – B)**
Cat 4.11 Wideband-Line	$116,706	$114,5921	$2,114
Cat 4.11 Direct Assignment	7,154	7,024	130
Cat 4.13 Ex Line x/WB	494,431	496,675	(2,244)
Cat 4.22 Interexchange PL	1,387	1,670	(283)
Cat 4.22 Direct Assignment	1,446	1,741	(295)
Cat 4.23 All Others	4,104	3,526	578
Total 2230	**$625,228**	**$625,228**	**$0**

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to report the correct amount for High Cost Program purposes. In addition, the Beneficiary also informed AAD that for the power and common allocation, incorrect lines were provided and utilized throughout cost study and USF submission.[14] The Beneficiary indicated that processes have been implemented to ensure billing system records are utilized in the preparation of the cost study.[15]

[13] *See* Finding #3: 47 C.F.R. § 54.903(a)(1) – Inaccurate Loops and Access Line Counts for further details.
[14] *Id.*
[15] *Id.*

EFFECT

AAD calculated the monetary effect for this finding using the correct number of access lines (identified in Finding #3) and subtracting the recalculated amount from the total amount reported by the Beneficiary in the respective accounts in the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
HCL	$(926)
ICLS	(233)[16]
Total	**$(1,159)**

RECOMMENDATION

The Beneficiary must ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that identifies the specific asset allocations among categories using accurate data (access lines for this specific finding) that is up-to-date and fully supported by source documentation for all asset balances that are submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> Processes have been implemented to ensure billing system records are utilized in the preparation of the cost study to ensure accuracy of Common and Power allocation within the Central Office workpaper development.

Finding #5: 47 C.F.R. § 32.2000(e)(7),(f)(2)(iii) – Incomplete/Inaccurate Continuing Property Records

CONDITION

AAD obtained and examined the Beneficiary's Continuing Property Records (CPR) to determine whether the Beneficiary properly recorded and reported its assets for High Cost Program purposes. While the totals of the CPR account details tied to the general ledger balances in the Beneficiary's Part 64 Cost Study, AAD noted that the Beneficiary's CPR had carry forward balances (*i.e.* pre-2006 assets totaling a $231,099),[17] for which the Beneficiary did not include the required information (description, location, date of placement, the essential details of construction, and the original cost of the property record units). Using the Beneficiary's state regulated depreciation rates and the actual year of asset implementation or 2006 (for the pre-2006 assets) as the base year, AAD calculated the estimated accumulated depreciation amounts, net asset balance and the current audit period depreciation expense associated with pre-2006 asset balances that had the missing information. AAD summarized the results below:

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[16] *See supra* n.6.

[17] See Table below; note: the $231,099 total is inclusive of the Land and Support Assets overstated amount of $79,983 which is not reflected in the table.

Part 64 Cost Study Lines	Part 64 Cost Study As Reported (A)	Part 64 Cost Study AAD Recalculation (B)	Variance Overstated / (Understated) (A – B)
Central Office Equipment (COE) Switching	$306,923	$289,459	$17,464
COE Transmission	$613,187	$495,877	$117,310
Accumulated Depreciation - COE Switching	$296,934	$279,470	$17,464
Accumulated Depreciation - COE Transmission	$603,486	$486,177	$117,309
Depreciation Expense - COE Switching	$35,514	$34,228	$1,286
Cable & Wire Facilities (CWF)	$2,535,182	$2,518,840	$16,342
Accumulated Depreciation - CWF	$1,156,041	$1,142,118	$13,923
Depreciation Expense - CWF	$143,692	$142,764	$928
Telephone Plant in Service	$3,651,587	$3,420,488	$231,099
Total Accumulated Depreciation[18]	$2,187,913	$1,994,651	$193,262

Because the Beneficiary did not provide the required details in the CPR or adequate documentation to substantiate the carry forward balances of its pre-2006 assets, AAD concludes that the Beneficiary did not properly record and report the assets.

In addition, AAD noted that the Beneficiary included overhead and retirement entries as separate line items within the CPR and did not associate the transactions with a specific asset. Because the Beneficiary did not properly associate overhead and asset retirements with specific assets within the CPR, AAD was unable to verify that the proper asset value was deducted from the CPR and the General Ledger upon asset retirement. The CPR and other underlying records of construction costs of the assets shall be properly maintained that, upon retirement of one or more retirement units, the actual cost or a reasonably accurate estimate of the cost of the asset retired can be determined.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly maintain its CPRs to ensure that the Beneficiary recorded and reported accurate information for High Cost Program purposes. The Beneficiary informed AAD that details of carryforward balances were not available because the Beneficiary went through a system upgrade in 2006 along with major upgrades to plant.[19] The Beneficiary has been refining its process for invoice tracking and record keeping to prevent future occurrence.[20] In addition, the Beneficiary informed AAD that the reason for not associating overhead

[18] This total is inclusive of the Land and Support Assets overstated amount of $44,566, which is not reflected in the table.
[19] Beneficiary responses to audit exception summary, received Jan. 17, 2019.
[20] *Id.*

and asset retirements with specific assets was due to oversight prior to establishing the Beneficiary's new process.[21] The Beneficiary has been refining its work order process to correctly identify labor distributions associated with material and this process is being further evaluated.[22]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the pre-2006 assets, including the associated accounts, from the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
HCL	$(6,866)
ICLS	603[23]
Total	**$(6,263)**

RECOMMENDATION

The Beneficiary must maintain detailed CPRs that include the description, location, date of placement, the essential details of construction, and the original cost of the property record units and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describes how the Beneficiary will update and maintain detailed CPRs that include the description, location, date of placement, the essential details of construction, and the original cost of the property record units, and other required elements and maintain adequate documentation for CPR balances submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> Company has been refining its processes for invoice tracking and record keeping to prevent future occurrences where they now scan each invoice to be stored in a central location. In regards to overhead and retirement entries, the company has improved its workorder [sic] process to correctly identify labor distributions associated with material.

Finding #6: 47 C.F.R. § 51.917(d)(v) – Inaccurate Interstate Switched Access and Intrastate Terminating Switched Access Service Revenues

CONDITION

AAD obtained and examined the Beneficiary's Tariff Review Plan (TRP) submissions to verify the accuracy of the Switched Access Revenues (Interstate Revenues) and Intrastate Terminating Switched Access Service

[21] *Id.*
[22] *Id.*
[23] *See supra* n.6.

Revenues (Intrastate Revenues) reported for the 2013-2014 and 2014-2015 programs years. AAD noted a difference between the amounts in the TRP and the amounts in the Beneficiary's CAF ICC filing. AAD obtained and examined the Beneficiary's billing reports and general ledger and noted that the total Interstate Revenues and Intrastate Revenues that were identified on the Beneficiary's billing reports and general ledger did not reconcile. Further, the general ledger did not reconcile to the revenues reported by the Beneficiary in the CAF ICC filing. Based on revenues per the general ledger, the Beneficiary did not report the correct amounts on their TRP submission. The differences are summarized below:

Interstate Revenues	Program Year 2013-2014	Program Year 2014-2015
As Reported	$40,106	$21,997
Per the General Ledger	$39,257	$36,390
Per the Billing Report	$39,602	$28,011
Variance Between Reported Amount and General Ledger Over/(Under)	$849	($14,393)

Intrastate Revenues	Program Year 2013-2014	Program Year 2014-2015
As Reported	$50,542	$41,022
Per the General Ledger	$47,999	$37,537
Per the Billing Report	$50,061	$22,456
Variance Between Reported Amount and General Ledger Over/(Under)	$2,543	$3,485

Because the Beneficiary's supporting documentation (the general ledger and the billing report) did not agree to the revenue amounts that the Beneficiary reported, AAD concludes that the Beneficiary did not accurately report its Interstate and Intrastate Revenues.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data to report accurate tariffed revenues for High Cost Purposes. The Beneficiary informed AAD that after review with USAC and its recalculation, the Beneficiary understand there were errors in the filing.[24]

EFFECT

AAD calculated the monetary effect for this finding by subtracting/ adding the recorded intrastate and interstate values per the general ledger from/to the total amount reported by the Beneficiary in its respective accounts on the CAF ICC filing. AAD summarized the results below:

Support Type	Monetary Effect
CAF ICC	$(9,334)
Total	**$(9,334)**

[24] Beneficiary responses to audit exception summary, received Mar. 6, 2019.

RECOMMENDATION

The Beneficiary must ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describes how the Beneficiary identifies, accumulates, and reconciles the revenue balances from its billing or other systems to the Tariff Review Plans to ensure the accuracy of revenue balances that are submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

The root cause of this error has since been corrected and preparation of this submission goes through substantial review to prevent further occurrences.

Finding #7: 47 C.F.R. § 32.4340, 47 C.F.R. § 36.506 and 47 C.F.R. § 54.1305(a)(f) – Inaccurate Deferred Operating Taxes Reporting

CONDITION

AAD obtained and examined the Beneficiary's supporting calculations to determine whether the Beneficiary reported accurate net non-current and current deferred operating income taxes (deferred taxes) as of December 31, 2014. AAD confirmed with the Beneficiary that it did not calculate and report deferred taxes in its 2014 High Cost filing. Upon AAD inquiry during the audit, the Beneficiary compiled its calculation of the deferred operating taxes, and allocated the amount to Account 4340 based on plant asset account balances. The Beneficiary's calculation resulted in a total of $26,302 in net non-current deferred taxes. Because the Beneficiary did not calculate and report its deferred taxes, AAD concludes that the Beneficiary did not report accurate deferred tax amounts in its High Cost filing.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data to report its deferred taxes for High Cost Program purposes. The Beneficiary informed AAD that this issue was realized at the time of the USAC audit and there was an error in preparation.[25]

EFFECT

AAD calculated the monetary effect for this finding by adding the net non-current deferred operating income taxes amount to the respective accounts in its High Cost filing. AAD summarized the results below:

[25] Beneficiary responses to audit results summary, received Jan. 17, 2019.

Support Type	Monetary Effect
HCL	$(10,574)
ICLS	(1,456)[26]
Total	**$(12,030)**

RECOMMENDATION

The Beneficiary must implement policies and procedures to ensure it has an adequate system to report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with FCC Rules. The Beneficiary must develop and implement policies, procedures, and processes that describes the process of calculating, reporting and documenting deferred tax balances that are submitted for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Since this finding occurred tax versus book depreciation schedules are provided by the tax preparer for cost study preparation and have been incorporated into the cost study and USF submissions.

[26] *See supra* n.6.

CRITERIA

Finding	Criteria	Description
#1	47 C.F.R. § 64.901(a)(3),(4)(2014).	"(a) Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose. (3) Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and nonregulated activities in accordance with the following hierarchy: (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves. (ii) When direct analysis is not possible, common cost categories shall be allocated based upon an indirect, cost causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available. (4)The allocation of central office equipment and outside plant investment costs between regulated and nonregulated activities shall be based upon the relative regulated and nonregulated usage of the investment during the calendar year when nonregulated usage is greatest in comparison to regulated usage during the three calendar years beginning with the calendar year during which the investment usage forecast is filed."
#1	47 C.F.R. § 32.6212 (2014).	"(a) This account shall include expenses associated with digital electronic switching. Digital electronic switching expenses shall be maintained in the following subaccounts: 6212.1 Circuit, 6212.2 Packet. (b) This subaccount 6212.1 Circuit shall include expenses associated with digital electronic switching equipment used to provide circuit switching. (c) This subaccount 6212.2 Packet shall include expenses associated with digital electronic switching equipment used to provide packet switching."
#1, 2	47 C.F.R. § 32.6720(c), (e) (2014).	"This account shall include costs incurred in the provision of general and administrative services as follows: (c) Providing accounting and financial services. Accounting services include payroll and disbursements, property accounting, capital recovery, regulatory accounting (revenue requirements, separations, settlements and corollary cost accounting), non-customer billing, tax accounting, internal and external auditing, capital and operating budget analysis and control, and general accounting (accounting principles and procedures and journals, ledgers, and financial reports). Financial services include banking operations, cash management, benefit investment fund management (including actuarial services), securities management, debt trust administration,

Finding	Criteria	Description
		corporate financial planning and analysis, and internal cashier services. (e) Performing personnel administration activities. This includes: (1) Equal Employment Opportunity and Affirmative Action Programs; (2) Employee data for forecasting, planning and reporting; (3) General employment services; (4) Occupational medical services; (5) Job analysis and salary programs; (6) Labor relations activities; (7) Personnel development and staffing services, including counseling, career planning, promotion and transfer programs; (8) Personnel policy development; (9) Employee communications; (10) Benefit administration; (11) Employee activity programs; (12) Employee safety programs; and (13) Nontechnical training course development and presentation."
#2	47 C.F.R. § 54.7(a) (2014).	"A carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."
#2	*See All Universal Service High-Cost Recipients are Reminded that Support Must be Used for its Intended Purpose*, Public Notice, FCC 15-133 (30 FCC Rcd 11821) (rel. Oct. 19, 2015).	"Under federal law, high-cost support provided to an ETC must be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. The following is a non-exhaustive list of expenditures that are not necessary to the provision of supported services and therefore may not be recovered through universal service support: • Personal travel; • Entertainment; • Alcohol; • Food, including but not limited to meals to celebrate personal events, such as weddings, births, or retirements; • Political contributions; • Charitable donations; • Scholarships; • Penalties or fines for statutory or regulatory violations; • Penalties or fees for any late payments on debt, loans or other payments • Membership fees and dues in clubs and organizations; • Sponsorships of conferences or community events; • Gifts to employees; and" • Personal expenses of employees, board members, family members of employees and board members, contractors, or any other individuals affiliated with the ETC, including but not limited to personal expenses for housing, such as rent or mortgages."
#2	*See FCC Provides Additional $500 Million in Funding for Rural Broadband*, Report	32. Membership fees and dues in clubs and organizations, including social, service, and recreational or athletic clubs and organizations, as well as trade associations and organizations that provide professional or trade certifications such as state bar associations, are expenses

Finding	Criteria	Description
	and Order, FCC 18-29, (33 FCC Rcd 2990) (rel. Mar. 23, 2018).	unrelated to operations excluded from high-cost support.90 Commenters agree that these expenses related to social and recreational clubs and organizations are already excluded from high-cost support recovery. But those same and other commenters also argue that membership fees and dues in trade associations, chambers of commerce, state bar associations and professional certifications for specialized employees should be recoverable. We recognize the educational and training benefits that trade associations provide and that membership in chambers of commerce may help stimulate business. However, as other commenters acknowledge, a function of many of these organizations is advocacy on behalf of their members for the purpose of influencing public policy which is not used for the provision, maintenance, and upgrading of facilities and services for which support is intended. Just as ETCs may not recover lobbying expenses under our rules, similarly, they may not recover membership fees in organizations that engage in lobbying. Further, professional affiliations or certifications such as state bar associations, accounting associations, or other professional groups may facilitate general corporate functions but are not used only for the provision of supported facilities and services.
#2	47 C.F.R. § 32.7300 (2014).	"This account shall be used to record the results of transactions, events and circumstances affecting the company during a period and which are not operational in nature. This account shall include such items as nonoperating taxes, dividend income and interest income. Whenever practicable, the inflows and outflows associated with a transaction or event shall be matched and the result shown as a net gain or loss…"
#3	47 C.F.R. § 54.1305(i) (2014).	"The number of working loops for each study area. For universal service support purposes, working loops are defined as the number of working Exchange Line C&WF loops used jointly for exchange and message telecommunications service, including C&WF subscriber lines associated with pay telephones in C&WF Category 1, but excluding WATS closed end access and TWX service. These figures shall be calculated as of December 31st of the calendar year preceding each July 31st filing."
#3	47 C.F.R. § 54.903(a)(1) (2014).	"Each rate-of-return carrier shall submit to the Administrator on March 31 of each year the number of lines it served as of the prior December 31, within each rate-of-return carrier study area showing residential and single-line business line counts, multi-line business line counts, and consumer broadband-only line counts separately. For purposes of this report, and for purposes of computing support under this subpart, the residential and single-line business class lines reported include lines assessed the residential and single-line business End User Common Line charge pursuant to § 69.104 of this chapter, the multi-line business class lines reported include lines assessed the multi-line business End User Common Line charge pursuant to § 69.104 of this chapter, and consumer broadband-only lines reported include lines assessed the Consumer Broadband-only Loop rate charged pursuant to § 69.132 of this chapter or provided on

Finding	Criteria	Description
		a detariffed basis. For purposes of this report, and for purposes of computing support under this subpart, lines served using resale of the rate-of-return local exchange carrier's service pursuant to section 251(c)(4) of the Communications Act of 1934, as amended, shall be considered lines served by the rate-of-return carrier only and must be reported accordingly..”
#4	47 C.F.R. § 36.121(c)(1) (2004).	“In the separation of the cost of central office equipment among the operations, the first step is the assignment of the equipment in each study area to categories. The basic method of making this assignment is the identification of the equipment assignable to each category, and the determination of the cost of the identified equipment by analysis of accounting, engineering and other records. (1) The cost of common equipment not assigned to a specific category, e.g., common power equipment, including emergency power equipment, aisle lighting and framework, including distributing frames, is distributed among the categories in proportion to the cost of equipment, (excluding power equipment not dependent upon common power equipment) directly assigned to categories.”
#5	47 C.F.R. § 32.2000(e)(7),(f)(2)(iii) (2004).	“(7) The basic property record components (see paragraph (c) of this section) shall be arranged in conformity with the regulated plant accounts prescribed in this section of accounts as follows: (i) The continuing property records shall be compiled on the basis of original cost (or other book cost consistent with this system of accounts). The continuing property records shall be maintained as prescribed in §32.2000(f)(2)(iii) of this subpart in such manner as will meet the following basic objectives: (A) Provide for the verification of property record units by physical examination. (B) Provide for accurate accounting for retirements. (C) Provide data for use in connection with depreciation studies. (iii) The continuing property record shall reveal the description, location, date of placement, the essential details of construction, and the original cost (note also §32.2000(f)(3) of this subpart) of the property record units. The continuing property record and other underlying records of construction costs shall be so maintained that, upon retirement of one or more retirement units or of minor items without replacement when not included in the costs of retirement units, the actual cost or a reasonably accurate estimate of the cost of the plant retired can be determined.”
#6	47 C.F.R. § 51.917(d)(v) (2014).	“If a Rate-of-Return Carrier receives payments for intrastate or interstate switched access services or for Access Recovery Charges after the period used to measure the adjustments to reflect the differences between estimated and actual revenues, it shall treat such payments as actual revenue in the year the payment is received and shall reflect this as an additional adjustment for that year.”
#7	47 C.F.R. § 32.4340 (a) (2014).	“(a) This account shall include the balance of income tax expense related to noncurrent items from regulated operations which have been deferred to later periods as a result of comprehensive

Finding	Criteria	Description
		interperiod tax allocation related to temporary differences that arise from regulated operations.”
#7	47 C.F.R. § 36.506 (2014).	“(a) Amounts in these accounts are maintained by plant account and are apportioned among the operations on the basis of the separations of the related plant accounts.”
#7	47 C.F.R. § 54.1305(a), (f) (2014).	“(a) In order to allow determination of the study areas and wire centers that are entitled to an expense adjustment pursuant to §54.1310, each incumbent local exchange carrier (LEC) must provide the National Exchange Carrier Association (NECA) (established pursuant to part 69 of this chapter) with the information listed for each study area in which such incumbent LEC operates, with the exception of the information listed in paragraph (h) of this section, which must be provided for each study area. This information is to be filed with NECA by July 31st of each year. The information provided pursuant to paragraph (i) of this section must be updated pursuant to §54.1306. Rural telephone companies that acquired exchanges subsequent to May 7, 1997, and incorporated those acquired exchanges into existing study areas shall separately provide the information required by paragraphs (b) through (i) of this section for both the acquired and existing exchanges. (f) Unseparated corporate operations expenses, operating taxes, and the benefits and rent proportions of operating expenses. The amount for each of these categories of expense shall be the actual amount for that expense for the calendar year preceding each July 31st filing. The amount for each category of expense listed shall be stated separately.”

ATTACHMENT J

HC2019BE026

Smart City Telecommunications, LLC

Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC2019BE026

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MOSSADAMS

EXECUTIVE SUMMARY

January 15, 2021

Teleshia Delmar, Audit and Assurance Division
Universal Service Administrative Company
700 12th St NW, Suite 900
Washington, DC 20005

Dear Teleshia Delmar:

This report represents the results of Moss Adams LLP's (we, us, our, and Moss Adams) work conducted to address the performance audit obligations relative to Smart City Telecommunications, LLC (Beneficiary), study area code 210330 for disbursements of $2,146,198 made from the federal Universal Service High Cost Program (HCP) (Disbursements) during the year ended December 31, 2018.

We conducted our performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2018 Revision). Those standards require that we plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form our conclusions. We believe the evidence we have obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. However, our performance audit does not provide a legal determination of the Beneficiary's compliance with specified requirements.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's (FCC) Orders governing federal Universal Service Support for the HCP relative to the disbursements (collectively, the Rules).

Based on the test work performed, our audit disclosed three detailed audit findings (Finding or Findings) discussed in the Audit Results section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC management or other officials and/or details about internal operating processes or investigations. This report is intended solely for the use of USAC, the Beneficiary, and the FCC and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

Moss Adams LLP

Overland Park, Kansas
February 26, 2021

AUDIT RESULTS

Audit Results	Monetary Effect & Recommended Recovery
Finding #1: 47 C.F.R. § 32.6124, 47 C.F.R. § 32.6623, and 47 C.F.R. § 32.6720(f) – Incorrect Classification of Labor and Benefit Expenses as General Purpose Computers Expense: General purpose computers expense included labor and benefits that were not spent maintaining physical computers or related operating systems resulting in overstatement of plant specific expense of $753,745, understatement of customer service expense of $237,120, and understatement in corporation operations expense of $516,625.	$109,989
Finding #2: 47 C.F.R. § 32.27(c)(3) – Affiliate Transaction Expenses in Excess of Fully Distributed Costs: Expenses charged by nonregulated affiliates to the Beneficiary were recorded at an amount greater than fully distributed cost resulting in a $39,345 overstatement of plant specific and plant nonspecific expenses.	$3,467
Finding #3: 47 C.F.R. § 64.903(b) – Inaccurate Cost Allocations: The Beneficiary's indirect cost allocation factors to allocate costs between regulated and nonregulated activities were based on outdated factors. As a result, regulated rate base was overstated by $20,405 and regulated expenses were overstated by $21,110.	$2,048
Total	**$115,504**

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery from the Beneficiary of the High Cost Program support amount noted in the chart below. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	ICLS (A)	USAC Recovery Action (A) + (B) = (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$109,989	$109,989	None
Finding #2	$3,467	$3,467	None
Finding #3	$2,048	$2,048	None
Mechanism Total	$115,504	$115,504	

BACKGROUND AND PROGRAM OVERVIEW

BACKGROUND

The Beneficiary is an eligible telecommunications carrier (ETC) that provides telecommunications services, including local service to residential and business customers residing in Florida. The Beneficiary also provides non-regulated services such as Internet. The Beneficiary elected to receive model-based support (Alternative Connect America Model, or A-CAM) beginning January 2017.

PROGRAM

USAC is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (FCC) pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the federal Universal Service Fund (USF), which is designed to ensure that all people, regardless of location or income have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations, or advocate regarding any matter of universal service policy.

The High Cost Program (HCP), a component of the USF, ensures that consumers in rural areas of the country have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas. The HCP consists of the following support mechanisms that are available to telecommunications carriers that elected A-CAM support effective January 2017:

- Connect America Fund Intercarrier Compensation support (CAF ICC): CAF ICC support replaced Local Switching Support is available to ILECs to assist them in recovering a portion of the revenue requirement related to switching investment that is not covered by the access recovery charge (ARC) billed to the end user or certain other changes billed to other carriers. This revenue requirement was frozen based on forecasted switching investment filed by eligible carriers in 2011 and is being reduced by 5% per year. CAF ICC disbursements began July 1, 2012.

- Interstate Common Line Support (ICLS): ICLS is available to ILECs and is designed to help its recipients cover common line revenue requirement while ensuring the subscriber line charge (SLC) remains affordable to customers. The common line revenue requirement is related to facilities that connect end users to the carrier's switching equipment. For A-CAM recipients, ICLS received during 2018 is related to the final ICLS true-up of actual costs for the period ending December 31, 2016.

OBJECTIVE, SCOPE, AND PROCEDURES

OBJECTIVE

The objective of our performance audit was to evaluate the Beneficiary's compliance with 47 C.F.R Part 54, Subparts C, D, K, and M; Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B as well as the Federal Communications Commission's Orders governing federal Universal Service Support for the HCP relative to the disbursements for the 12-month period ended December 31, 2018.

This performance audit did not constitute an audit of financial statements in accordance with *Government Auditing Standards*. We were not engaged to, and do not render an opinion on the Beneficiary's internal control over financial reporting or internal control over compliance. We caution that projecting the results of our evaluation on future periods is subject to the risks that controls may become inadequate because of changes in conditions that affect compliance.

SCOPE

The following chart summarizes the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	12/31/2016	12/31/2018	$2,154,034
Interstate Common Line Support (ICLS)	12/31/2016	12/31/2018	$(7,836)
Total			**$2,146,198**

AUDIT METHODOLOGY

To accomplish our audit objective, we performed the following procedures:

Reconciliation

We reconciled the December 31, 2016 and December 31, 2015, trial balances to the separations and Part 64 study inputs and then to the applicable HCP Forms, obtained explanations for any variances, and evaluated the explanations for reasonableness.

Rate Base and Investment High Cost Program Support Amount

We utilized an attribute sampling methodology[1] to select asset samples from central office equipment (COE) and cable and wire facilities (CWF) accounts. We made asset selections from continuing property record (CPR) detail. Certain assets were judgmentally selected, and others were selected using a random number generator. We determined that the balances for the selected assets were properly supported by underlying documentation such as work order detail, third-party vendor invoices, materials used sheets, and time and payroll documentation for labor and related costs.

We agreed the amounts charged to work order detail and verified the proper general ledger coding under Part 32. In addition, we verified the physical existence of select assets.

Tax Filing Status

We verified the tax filing status for the Beneficiary and obtained and reviewed the imputed tax provision and deferred income tax provision calculations, including supporting documentation, for reasonableness.

[1] Attribute sampling is a methodology where the selections made from a representative population are tested to determine if they contain predefined qualified characteristics (attributes).

Expenses

We utilized an attribute sampling methodology to select expense samples utilizing a random number generator from operating expense accounts that impact ICLS. We made payroll sample selections from a listing of employees utilizing a random number generator. We agreed the amounts from the employee paystubs to supporting documentation such as time sheets, labor distribution reports, and approved pay rates, and verified the costs were coded to the proper Part 32 account. We reviewed benefits and clearings to ensure the Beneficiary's compliance with Part 32. We made other disbursement selections from accounts payable transactions and agreed amounts to supporting documentation, reviewing for proper coding under Part 32. We judgmentally selected a sample of manual journal entries to ensure reclassifications between expense accounts were appropriate and reasonable. We utilized MindBridge, a software program that uses data science and machine learning techniques to uncover outliers and anomalous transactions for 100% of the transactions within general ledger data, to identify keywords within the transaction descriptions to identify transaction for potential disallowed expenses and reviewed supporting documentation for a selection of transactions to determine if expenses were properly included or properly excluded from the cost study.

Affiliate Transactions

We performed procedures to assess the reasonableness of affiliate transactions that occurred during the period under audit. The affiliate transactions involved the transfer of assets or the provision of service between the Beneficiary and its commonly owned affiliate Smart City Solutions, LLC. We noted the Beneficiary is 100% owned by Smart City Finance, LLC whose sole member is Smart City Holding, LLC. We judgmentally selected a sample of various transactions between the Beneficiary and its affiliates to determine whether the Beneficiary had recorded the transactions in accordance with 47 C.F.R. Section 32.27 and if they were categorized in the appropriate Part 32 accounts. The Beneficiary entered into the following transactions with its affiliates during the period under audit:

- Accounting services priced at fully distributed cost
- Allocation of third-party Ethernet and cell service backhaul charges based on proportionate amount of equipment used to provide service
- Dark fiber lease based on market rates
- Switch usage based on tariff rates
- Wholesale DSL charges priced at tariff rates
- Alarm monitoring and 611 repair services at fully distributed cost

- Colocation lease based on fully distributed cost
- Finance management services priced at fully distributed cost

Revenues and Subscriber Listings

We tested general ledger accounts, subscriber bills, and other documentation to verify the accuracy and existence of revenues. We utilized an attribute sampling methodology to select revenue samples utilizing a random number generator from subscriber listings. We tested subscriber bills with procedures to ensure the lines were properly classified as residential, single-line business, or multi-line business. In addition, we reconciled the ICLS related revenues reported to the National Exchange Carrier Association (NECA) to the general ledger and billing support, and we reconciled switched related revenues reported to USAC as part of the CAF ICC filing to general ledger and billing support. We obtained subscriber listings and billing records to determine the lines or loops reported in the HCP filings agreed to supporting documentation. We reviewed the subscriber listings for duplicate lines, invalid data, and nonrevenue producing lines.

Part 64 Allocations

We (1) reviewed the Beneficiary's cost apportionment methodology to assess the reasonableness of the allocation methods and corresponding data inputs used to calculate the factors, (2) recalculated the material factors, and (3) recalculated the material amounts allocated. We also evaluated the reasonableness of the assignment between regulated, nonregulated, and common costs and the apportionment factors as compared to the regulated and nonregulated activities performed by the Beneficiary.

Central Office Equipment (COE) and Cable and Wire Facilities (CWF) Categorization

We reviewed the Beneficiary's methodology for categorizing assets including a comparison to network diagrams. We reconciled the COE and CWF amounts to the cost studies and agreed them to the applicable HCP Forms. In addition, we reviewed power and common allocations and remotely viewed via video call a judgmentally selected sample of COE assets and tested route distances of CWF for reasonableness.

Revenue Requirement

We recalculated the Beneficiary's revenue requirement using our cost allocation software program and reviewed the calculation of revenue requirement including the applications of Part 64, 36, and 69 for reasonableness. In addition, we traced cost adjustments that were not recorded in the general ledger to supporting documentation and reviewed them for reasonableness.

DETAILED AUDIT FINDINGS

Our performance audit resulted in the following detailed audit findings and recommendations with respect to the Beneficiary's compliance with the Rules, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Part 54, Subparts C, D, K, and M, Part 36, Subpart F; Part 64, Subpart I; Part 69, Subparts D, E, and F; and Part 32, Subpart B, as well as the FCC's orders governing federal Universal Service Support applicable to the disbursements made from the HCP during the year ended December 31, 2018.

Finding #1: 47 C.F.R. §§ 32.6124, 32.6623, and § 32.6720(f) – Incorrect Classification of Labor and Benefit Expenses as General Purpose Computers Expense

CONDITION

We obtained and reviewed the Beneficiary's employee time sheets, check stubs, payroll registers, labor distributions by account, and formal employee job descriptions for a random sample selection of 35 employees. We found that three of the employees selected were included in the Beneficiary's IT department and coded either all, or the majority, of their time to general purpose computer functions (Part 32 account 6124 general purpose computers expense). However, the employees actual job functions were substantially application or database work, business systems analysis, and processing of end user billing, which are functions consistent with Part 32 account 6724 corporate operations and in some instances Part 32 account 6623 customer services.[2] We expanded our sample selection of employees to the entire IT department, adding an additional 5 IT department employees, noting the additional five employees also coded all, or the majority, of their time to 6124 instead of 6724 and 6623 consistent with their job duties. Allocation of time to the proper expense account based on job duties would have resulted in a reduction of account 6124 general purpose computers expense of $753,745, an increase to account 6623 customer services expense of $237,120 and an increase to account 6724 corporate operations expense of $516,625.

CAUSE

The process to review and approve timesheets did not identify and adjust general purpose computers expense for work performed related to end user billing and work performed related to planning and maintaining application systems and databases.

[2] Responsible Accounting Officers; Part 32, Uniform System of Accounts for Class A and Class B Carriers – Questions and Answers in reply to RAO Letter 7 – Question and Answer #8

EFFECT

The exception[3] identified above resulted in overstatement of plant specific expense of $753,745, understatement of customer service expense of $237,120, and understatement in corporation operations expense of $516,625, which impacted ICLS disbursements[4]. We adjusted the expense accounts above in the HCP filings to calculate the impact on ICLS disbursements. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of $109,989. There was no impact to CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$109,989
Total	**$109,989**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

We recommend that the Beneficiary provide training to its managers and employees to ensure time is recorded to the proper job duties and Part 32 account. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Smart City Telecom understands the nature of the finding and has taken action to modify and enhance their current procedures to ensure proper classification of expenses.

Finding #2: 47 C.F.R. § 32.27(c)(3) – Affiliate Transaction Expenses in Excess of Fully Distributed Costs

[3] In the report, Moss Adams identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of exception.
[4] The effect on ICLS disbursements was impacted by the corporate operations expense limitation included in the calculation of ICLS support. Therefore, shifting expenses reported in the Beneficiary's ICLS filing from plant specific expenses to corporate operations expense resulted in a reduction to ICLS support.

CONDITION

We obtained a listing of affiliate transactions from the Beneficiary. We judgmentally selected charges from a nonregulated affiliate to the Beneficiary for 10 services and determined that the nonregulated affiliate only provides the selected services to the Beneficiary and its affiliate.[5] We agreed one month of charges to invoices from the affiliate without exception. We also compared the charges per the invoice to the fully distributed cost calculation provided by the Beneficiary noting the invoice charges were greater than the fully distributed cost for 2 of the 10 services selected (alarm monitoring and 611 repair services). We summarized the monthly charges recorded to the regulated expense accounts for 2016 as compared to the annual fully distributed cost amount, noting the amounts recorded were greater than fully distributed cost, resulting in an overstatement of central office digital switch expense account 6212 of $12,577 and an overstatement of testing expense account 6533 of $26,768.

CAUSE

The process to review, approve, and prepare affiliate transactions recorded to regulated accounts did not include a process to ensure recorded charges were not in excess of fully distributed cost.

EFFECT

The exception identified above resulted in an overstatement of regulated expenses of $39,345, which impacted ICLS disbursements. We decreased the expense accounts above in the HCP filings to calculate the impact on ICLS disbursements. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of $3,467[6]. There was no impact to CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$3,467
Total	**$3,467**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

[5] Part 32.27(c)(3) requires that all services received by a carrier from its affiliate(s) that exist solely to provide services to members of the carrier's corporate family shall be recorded at fully distributed cost.

[6] A portion of the overstated regulated expenses were specific to switching, which could have a minimal impact on ICLS. Based on factors imposed by the FCC Rules, only a portion of the remaining overstated amount would be reimbursed to the Beneficiary from the ICLS fund. Therefore, only that portion of the overstated amount would be recovered in the monetary effect.

The Beneficiary has elected A-CAM support. The Beneficiary should ensure that it has an adequate system in place to ensure its reporting is in compliance with FCC requirements. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Smart City Telecom understands that affiliate transactions are based on fully distributed cost and has made the necessary correction going forward.

Finding #3: 47 C.F.R. § 64.903(b)[7] – Inaccurate Cost Allocations

CONDITION

We obtained and reviewed the Beneficiary's cost allocation manual and supporting documentation to determine whether the Beneficiary made cost allocations based on cost causative factors when costs were not directly assignable to regulated and nonregulated activities. Accounts that could not be directly assigned were allocated based on cost causative allocators or a general allocator. Our review of the cost causative allocators and general allocator indicated the Beneficiary's indirect cost allocators and general cost allocator to allocate costs between regulated and nonregulated activities were based on 2012 inputs, which were outdated.

The following table presents a list of allocators used by the Beneficiary, the allocation factor based on 2012 inputs and the revised factor based on 2016 inputs:

Cost allocator	Nonregulated Factor Based on 2012 Inputs	Updated Nonregulated Factor Based on 2016 Inputs
Operating expense and taxes	10.58%	11.91%
Billing analysis	33.02%	29.68%
Total plant in service	7.42%	7.49%
AC 2124 - Computers	15.13%	19.64%
AC 2210, 2230, & 2410 – COE & CWF	4.90%	7.26%
AC 2121 - Buildings	0.67%	1.53%
AC 2122 – Furniture & 2123 Office Equipment	3.01%	8.46%
AC 2210 & 2230 - COE	4.70%	11.37%
Network operations wages	3.68%	2.78%
General allocator	10.58%	11.91%

[7] *In the Matter of Separation of Costs and Regulated Telephone Service from Costs of Nonregulated Activities*, CC Docket No. 86-111, Order on Reconsideration, FCC 87-305, 2 FCC Rcd 6283, 6299, para. 143-45 (1987)

Using updated indirect cost allocation factors would have resulted in decreases to the Beneficiary's 2016 regulated rate base and expense accounts as follows:

Regulated Account	Increase (Decrease)
2112	(19,930)
2122	(24,414)
2123	(21,557)
2124	(139,784)
3112	14,632
3122	17,378
3123	16,853
3124	136,417
Total Rate Base Impact	**$(20,405)**
6122	(375)
6123	(1,189)
6124	(5,298)
6500	(11,670)
6531	5,677
6532	789
6623	2,370
6711	(1,540)
6721	(2,460)
6723	(604)
6724	(1,856)
6728	**(4,470)**
7240	**(484)**
Total Expense Impact	**$(21,110)**

CAUSE

The Beneficiary was not aware of the requirement to update its cost allocation manual annually.

EFFECT

The exception identified above resulted in an overstatement of rate base of $20,405 and an overstatement of regulated expenses of $21,110, which impacted ICLS disbursements. We decreased the rate base accounts and decreased the regulated expense accounts above in the HCP filings to calculate the impact on ICLS disbursements. As summarized below, we estimate the monetary impact of this finding, relative to disbursements for the 12-month period ended December 31, 2018, to be an overpayment of $2,048.[8] There was no impact to CAF ICC disbursements.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$2,048
Total	**$2,048**

RECOMMENDATION

We recommend that USAC Management seek recovery of the amounts identified in the Effect section above.

The Beneficiary has elected A-CAM support. The Beneficiary should ensure that it has an adequate system in place to ensure its reporting is in compliance with FCC requirements. In addition, the Beneficiary may learn more about the reporting requirements and record retention policies on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Smart City Telecom is an ACAM company, however, it understands the nature of the finding and has taken action to ensure that it is following FCC requirements.

[8] The effect of the overstated rate base and expenses is not as high as the overstated balances because only a portion of the total regulated costs are allocated to the interstate jurisdiction and ICLS via Parts 36 and 69. In addition, over one-half of the overstated expenses were related to corporate operations in which FCC rules limit the amount of the Beneficiary's recovery from the ICLS fund for such expenses.

CRITERIA

Finding	Criteria	Description
Finding #1	47 C.F.R. § 32.6124 (2016)	This account shall include the costs of personnel whose principal job is the physical operation of general purpose computers and the maintenance of operating systems. This excludes the cost of preparation of input data or the use of outputs which are chargeable to the accounts appropriate for the activities being performed. Also excluded are costs incurred in planning and maintaining application systems and databases for general purpose computers. (See also §32.6720, General and administrative.) Separately metered electricity for general purpose computers shall also be included in this account.
Finding #1	47 C.F.R. § 32.6623(a) (2016)	(a) This account shall include costs incurred in establishing and servicing customer accounts. This includes: (1) Initiating customer service orders and records; (2) Maintaining and billing customer accounts; (3) Collecting and investigating customer accounts, including collecting revenues, reporting receipts, administering collection treatment, and handling contacts with customers regarding adjustments of bills; (4) Collecting and reporting pay station receipts; and (5) Instructing customers in the use of products and services.
Finding #1	47 C.F.R. § 32.6720(f) (2016)	This account shall include costs incurred in the provision of general and administrative services as follows: (f) Planning and maintaining application systems and databases for general purpose computers.
Finding #1	*See* Letter from Clifford M. Rand, Acting Chief of Accounting and Audits Division, FCC to Responsible Accounting Officers at question 8, (July 1, 1987); available at https://transition.fcc.gov/Bureaus/Common_Carrier/RAO_Letters/1994_pre/ra870701.txt.	Q. What is the expense/capitalization policy for software for network operations? A. Expenses incurred in planning, developing, testing, implementing and maintaining data bases and application systems for general purpose computers are to be recorded in Account 6724. This is in contrast to the noncapitalizable expenditures for maintaining general purpose computers and their operating system software which are classifiable to the plant specific account for general purpose computers, Account 6124. The February 18, 1987, Memorandum Opinion and Order in CC Docket 78-196 maintains the distinction of Accounts 6724 and 6124 for recording the respective costs of maintaining data bases and application systems as contrasted with those for maintaining general purpose computers and their operating systems. However, certain remarks need further clarification to be more explanatory of the workings of these accounts in conjunction with data processing activities which directly benefit other functions (as illustrated by the assignment of data

		processing costs to Account 6623, Customer Services). The following is offered as a clarifying interpretation of the assignment of various information management and data processing costs related to customer billing: The costs for the input and output of data associated with the processing of bills, whether on service center computers or on computers used exclusively for billing purposes, are chargeable to Account 6623, Customer Services. Any general purpose computer used in the billing function, regardless of size and amount of time dedicated to billing, is to be recorded in Account 2124, General Purpose Computers. The costs for maintaining these general purpose computers and their operating system software used for billing customer accounts are to be recorded in Account 6124, General Purpose Computer Expense. Where a general purpose computer utilized in the billing function is large, a computer operator may be required to run the computer. Where such individuals are skilled in the operations of computers as opposed to any aspect of the billing process or the process of merely updating or otherwise manipulating data contained in the database, their time is chargeable to Account 6124. Generally, such individuals will be in the information management department and not the billing department. Regardless, their time is chargeable to Account 6124. On the other hand, an individual within the billing department who works at a computer--even full time--doing a billing function would not usually charge time to General Purpose Computers but to Account 6623. Likewise, the time for a service center employee who works full time or part time at a computer doing a billing function (e.g., updating billing data) would charge time to Account 6623, either directly or by the appropriate means established for charging service center work to user groups. The costs incurred in planning, developing, testing, implementing, and maintaining the data bases and the application systems for billing customer accounts are to be recorded in Account 6724, information Management. Database maintenance, however, does not include the input and update of billing data and accounts receivable and the use of the outputs. Such maintenance of database records (i.e. billing records) would be charged to Account 6623.
Finding #2	47 C.F.R. § 32.27(c)(3) (2016)	(c) Services provided between a carrier and its affiliate pursuant to a tariff, including a tariff filed with a state commission, shall be recorded in the appropriate revenue accounts at the tariffed rate. Non-tariffed services provided between a carrier and its affiliate pursuant to publicly-filed agreements submitted to a state commission pursuant to section 252(e) of the Communications Act of 1934 or statements of generally

		available terms pursuant to section 252(f) shall be recorded using the charges appearing in such publicly-filed agreements or statements. Non-tariffed services provided between a carrier and its affiliate that qualify for prevailing price valuation, as defined in paragraph (d) of this section, shall be recorded at the prevailing price. For all other services sold by or transferred from a carrier to its affiliate, the services shall be recorded at no less than the higher of fair market value and fully distributed cost. For all other services sold by or transferred to a carrier from its affiliate, the services shall be recorded at no more than the lower of fair market value and fully distributed cost. (1) Floor. When services are sold by or transferred from a carrier to an affiliate, the higher of fair market value and fully distributed cost establishes a floor, below which the transaction cannot be recorded. Carriers may record the transaction at an amount equal to or greater than the floor, so long as that action complies with the Communications Act of 1934, as amended, Commission rules and orders, and is not otherwise anti-competitive. (2) Ceiling. When services are purchased from or transferred from an affiliate to a carrier, the lower of fair market value and fully distributed cost establishes a ceiling, above which the transaction cannot be recorded. Carriers may record the transaction at an amount equal to or less than the ceiling, so long as that action complies with the Communications Act of 1934, as amended, Commission rules and orders, an is not otherwise anti-competitive. (3) Threshold. For purposes of this section, carriers are required to make a good faith determination of fair market value for a service when the total aggregate annual value of that service reaches or exceeds $500,000, per affiliate. When a carrier reaches or exceeds the $500,000 threshold for a particular service for the first time, the carrier must perform the market valuation and value the transaction in accordance with affiliate transactions rules on a going-forward basis. All services received by a carrier from its affiliate(s) that exist solely to provide services to members of the carrier's corporate family shall be recorded at fully distributed cost.
Finding #3	47 C.F.R. §64.903(b) (2016)	(b) Each carrier shall ensure that the information contained in its cost allocation manual is accurate. Carriers must update their cost allocation manuals at least annually, except that changes to the cost apportionment table and to the description of time reporting procedures must be filed at the time of implementation. Annual cost allocation manual updates shall be filed on or before the last working day of each calendar year. Proposed changes in the description of time reporting procedures, the statement concerning affiliate transactions, and the cost apportionment table must be accompanied by a

		statement quantifying the impact of each change on regulated operations. Changes in the description of time reporting procedures and the statement concerning affiliate transactions must be quantified in $100,000 increments at the account level. Changes in cost apportionment tables must be quantified in $100,000 increments at the cost pool level. The Chief, Wireline Competition Bureau may suspend any such changes for a period not to exceed 180 days, and may thereafter allow the change to become effective or prescribe a different procedure.
Finding #3	*In the Matter of Separation of Costs and Regulated Telephone Service from Costs of Nonregulated Activities*, CC Docket No. 86-111, Order on Reconsideration, FCC 87-305, 2 FCC Rcd 6283, 6299, para. 143-45 (1987).	143. The *Order* adopted in this proceeding applies to joint and common costs standards and the affiliate transaction rules to all local exchange and dominant interexchange carriers. We found that these carriers, large and small, have both the opportunity and incentive to cross subsidize nonregulated operations. In fact, companies that have not been subject to our structural separations provisions have long had the opportunity to integrate regulated and nonregulated activities. We determined that all ratepayers, whether served by large or small companies, were entitled to the protections our rules were intended to afford. 144. We rejected arguments concerning the burden and expense of complying with our rules. We reasoned that all telephone companies offering nonregulated services or products must apportion costs between their regulated and nonregulated offerings in order to support their various tariff filings, as well as for internal purposes. Our cost allocation rules at most represented a requirement that carriers modify their existing cost accounting systems. Compliance with our rule was therefore mandated for all local exchange companies and AT&T. 145. While all exchange carriers are required to comply with our accounting procedures, we exempted all but Tier 1 carriers from certain specific enforcement provisions, including the provision that carriers submit their cost allocation manuals to this Commission for review and approval. We also exempted smaller carriers from the requirement that they commission an annual audit from an independent auditing firm to verify that they are adhering to the accounting procedures established in their manuals.

ATTACHMENT K

HC2019BE012

Wabash Telephone Cooperative, Inc.
Audit ID: HC2019BE012
(SAC No.: 341088)

Performance audit for the Universal Service High Cost Program Disbursements made during the twelve-month period ended December 31, 2018

Prepared for: Universal Service Administrative Company

As of Date: March 1, 2021

KPMG LLP
800 S. Gay St, Suite 910
Knoxville, TN 37929

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EXECUTIVE SUMMARY

March 1, 2021

Ms. Teleshia Delmar, Vice President – Audit and Assurance Division
Universal Service Administrative Company
700 12th Street, NW, Suite 900
Washington, DC 20005

Dear Ms. Delmar:

This report presents the results of our work conducted to address the performance audit objectives relative to Wabash Telephone Cooperative, Inc. Study Area Code ("SAC") No. 341088 ("WTCI" or "Beneficiary") for disbursements of $6,913,652 made from the Universal Service High Cost Program ("HCP") during the twelve-month period ended December 31, 2018. Our work was performed during the period from October 22, 2019 to March 1, 2021, and our results are as of March 1, 2021.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards issued by the Comptroller General of the United States (2018 Revision, as amended) and American Institute of Certified Public Accountants Consulting Standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the Federal Communications Commission's ("FCC") Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP (collectively, the "Rules") relative to disbursements, of $6,913,652, made from the HCP during the twelve-month period ended December 31, 2018. Compliance with the Rules is the responsibility of the Beneficiary's management. Our responsibility is to evaluate the Beneficiary's compliance with the Rules based on our audit.

As our report further describes, KPMG identified five findings as discussed in the Audit Results and Recovery Action section as a result of the work performed. Based on these results, we estimate that disbursements made to the Beneficiary from the HCP for the twelve-month period ended December 31, 2018 were $117,390 higher than they would have been had the amounts been reported properly.

KPMG cautions that projecting the results of our evaluation to future periods is subject to the risks that controls may become inadequate because of changes in conditions or because compliance with controls may deteriorate.

In addition, we also noted other matters that we have reported to the management of the Beneficiary in a separate letter dated March 1, 2021.

This report is intended solely for the use of the Universal Service Administrative Company, the Beneficiary, and the FCC and is not intended to be and should not be relied upon by anyone other than these specified parties. This report is not confidential and may be released by USAC to a requesting third party.

Sincerely,

KPMG LLP

List of Acronyms

Acronym	Definition
ACAM	Alternative Connect America Cost Model
BLS	Broadband Loop Support
C.F.R.	Code of Federal Regulations
C&WF	Cable and Wire Facilities
CAF ICC	Connect America Fund Intercarrier Compensation
COE	Central Office Equipment
CPR	Continuing Property Record
ETC	Eligible Telecommunications Carriers
FCC	Federal Communications Commission
Form 509	CAF BLS Annual Common Line Actual Cost Data Collection Form
G/L	General Ledger
GSF	General Support Facilities
HCL	High Cost Loop
HCL Form	National Exchange Carrier Association Universal Service Fund Data Collection Form
HCM	High Cost Model
HCP	High Cost Program
ICLS	Interstate Common Line Support
ILEC	Incumbent Local Exchange Carrier
MLB	Multi-Line Business
NECA	National Exchange Carrier Association
ONT	Optical Network Terminal
SAC	Study Area Code
SLB	Single-Line Business
SLC	Subscriber Line Charge
SNA	Safety Net Additive
SVS	Safety Valve Support
TB	Trial Balance
TPIS	Telecommunications Plant In Service
TPUC	Telecommunications Plant Under Construction
USAC	Universal Service Administrative Company
USF	Universal Service Fund
WTCI	Wabash Telephone Cooperative, Inc.

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect	Recommended Recovery[1]
HC2019BE012-F01: Improper Inclusion of Non-Regulated Amounts[2] (Operating Expenses) – The Beneficiary did not accurately and appropriately allocate certain operating expenses between regulated and non-regulated activities, and between affiliates.	$136,581	$136,581
HC2019BE012-F02: Improper Distribution of Overhead Amounts – The Beneficiary inappropriately cleared specific overhead expense amounts to ineligible and/or inaccurate expense accounts.	$28,927	$28,927
HC2019BE012-F03: Improper Inclusion of Non-Regulated Amounts[2] (Payroll Expenses) – The Beneficiary did not accurately and appropriately allocate certain payroll expenses between regulated and non-regulated activities, and between affiliates.	$5,025	$5,025
HC2019BE012-F04: Improper Allocation Methodology - The Beneficiary did not allocate property taxes related to certain GSF assets between regulated and non-regulated activities.	$4,327	$4,327
HC2019BE012-F05: Inaccurate Depreciation Calculation – The Beneficiary used month end balances instead of average monthly balances to compute depreciation expense as prescribed by FCC Rules.	($57,470)	($57,470)
Total Net Monetary Effect	**$117,390**	**$117,390**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount will not exceed the proposed recovery amount.
[2] The results for Findings 1 and 3 are independent from one another and do not overlap. Each finding has its own monetary impacts and proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC management concurs with the audit results and will seek recovery of the High Cost Program support amount noted in the chart below. Note: USAC's High Cost Program Management does not net findings across SACs and High Cost does not pay additional support in the event of a finding of underpayment. The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

	HCL (A)	ICLS (B)	USAC Recovery Action (A) + (B) + (C)	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$108,031	$28,550	$136,581	
Finding #2	$20,377	$8,550	$28,927	
Finding #3	$4,135	$890	$5,025	
Finding #4	$3,064	$1,263	$4,327	
Finding #5	($44,274)	($ 13,196)	($57,470)	
Mechanism Total	**$91,333**	**$26,057**	**$117,390**	

BACKGROUND, OBJECTIVES, SCOPE AND PROCEDURES

BACKGROUND

Program Overview

USAC is an independent not-for-profit corporation that operates under the direction of the FCC pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the USF through four support mechanisms: High Cost; Lifeline; Rural Health Care; and Schools and Libraries. These four support mechanisms ensure that all people regardless of location or income level have affordable access to telecommunications and information services. USAC is the neutral administrator of the USF and may not make policy, interpret regulations or advocate regarding any matter of universal service policy.

The High Cost Support Mechanism, also known as the HCP, ensures that consumers in all regions of the nation have access to and pay rates for telecommunications services that are reasonably comparable to those services provided and rates paid in urban areas, regardless of location or economic strata. Thus, the HCP provides support for telecommunications companies (Beneficiaries) that offer services to consumers in less-populated areas. Several legacy HCP support mechanisms are noted below:

1. HCL: HCL support is available for rural companies operating in service areas where the cost to provide service exceeds 115% of the national average cost per line. HCL support includes the following two sub-components:
    a. SNA: SNA support is available for carriers that make significant investment in rural infrastructure in years when HCL support is capped and is intended to provide carriers with additional incentives to invest in their networks.
    b. SVS: SVS support is available to rural carriers that acquire high cost exchanges and make substantial post-transaction investments to enhance network infrastructure.
2. CAF ICC: CAF ICC support is available to ILECs to recover revenue that is not covered by Access Recovery Charges (ARC) to the end user.
3. ICLS: ICLS is available to rate-of-return incumbent carriers and competitive carriers, and is designed to help carriers offset interstate access charges and to permit each rate-of-return carrier to recover its common line revenue requirement, while ensuring that its SLCs remain affordable to its customers.
4. CAF BLS: CAF BLS provides support for voice and broadband service, including stand-alone broadband. CAF BLS provides support for rate-of-return carriers to the extent that SLC caps do not permit them to recover their common line revenue requirements. CAF BLS replaced ICLS effective July 1, 2016.
5. ACAM: ACAM provides funding to rate-of-return carriers that voluntarily elected to transition to a new cost model for calculating High Cost support in exchange for meeting defined broadband build-out obligations.

USAC engaged KPMG to conduct a performance audit relating to the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $6,913,652, made from the HCP during the twelve-month period ended December 31, 2018.

Beneficiary Overview

Wabash Telephone Cooperative, Inc. (SAC No. 340188), the subject of this performance audit, is a rural ILEC located in Louisville, IL that along with its subsidiaries/affiliates provides local access, long distance, internet, and video services and telecommunications equipment to its customers. WTCI owns 9 exchanges that serve over 4,000 customers in southeastern Illinois.

WTCI through its wholly-owned subsidiary Wabash Independent Networks, Inc. provides long distance, cable, internet and video services to its customers. In the table below, we show the High Cost support disbursed by USAC to the Beneficiary during the twelve-month period ended December 31, 2018 by fund type:

High Cost Support	Disbursement Amount
Connect America Fund (CAF) Broadband Loop Support (BLS)	$2,646,324
Connect America Fund (CAF) Intercarrier Compensation (ICC)	$390,204
High Cost Loop (HCL)	$3,582,530
Interstate Common Line Support (ICLS)	$294,594
Total	**$6,913,652**

Source: USAC

The High Cost support received by the Beneficiary during the twelve-month period ended December 31, 2018, was based on the following annual financial and operational data submitted by the Beneficiary to NECA and USAC:

- 2017-1, 2017-2, 2017-3 and 2017-4 HCL Forms, based on the twelve-month periods ended December 31, 2016, March 31, 2017, June 30, 2017 and September 30, 2017, respectively,
- 2016 FCC Form 509, based on calendar year 2016 data, and
- 2016 CAF ICC Tariff Review Plan (TRP), based on program year 2016 data

The above referenced Forms capture line count data and the totals of certain pre-designated G/L Accounts including all asset accounts that roll into the TPIS account as well as certain deferred liabilities and operating expenses, subject to the allocation between regulated and non-regulated activities (Part 64 Cost Allocations), the separation between interstate and intrastate operations (Part 36 Separations) and the separation between access and non-access elements (Part 69 Separations). In addition, the Beneficiary is required to submit certain annual investment data, including the categorization of COE and C&WF on the HCP Forms.

OBJECTIVES

The audit objective of this performance audit was to evaluate the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 of the FCC's Rules as well as specified FCC Orders governing federal Universal Service Support for the HCP relative to disbursements, of $6,913,652, made from the HCP during the twelve-month period ended December 31, 2018.

SCOPE

The scope of this performance audit included, but was not limited to, review of HCP Forms or other correspondence and supporting documentation provided by the Beneficiary, assessment of the Beneficiary's methodology used to prepare or support the HCP Forms or other correspondence, and evaluation of disbursement amounts made by the Beneficiary or potentially due to the Beneficiary. The scope of our work was focused on the HCP Forms or other correspondence filed by the Beneficiary that relate to disbursements made from the HCP during the twelve-month period ended December 31, 2018, as well as performing other procedures we considered necessary to form a conclusion relative to disbursements made from the HCP during the twelve-month period ended December 31, 2018.

KPMG identified the following areas of focus for this performance audit:[3]

1. General Procedures
2. Materiality Analysis
3. Reconciliation
4. Assets
5. Expenses
6. HCP Eligibility Forms
7. COE Categorization
8. C&WF Categorization
9. Overheads
10. Taxes
11. Part 64 Cost Allocations
12. Affiliate Transactions
13. Revenues, Subscriber Listings and Billing Records
14. Revenue Requirement

[3] If exceptions were noted in areas other than the aforementioned in-scope areas as a result of our testing procedures and the execution of our performance audit, we identified those findings in the 'Results' section of the report.

PROCEDURES

1. General Procedures

KPMG obtained and examined the ETC designation order to assess whether the Beneficiary was designated as an ETC in the study area prior to receiving HCP support. We obtained and examined the Beneficiary's state and/or self-certification letters for timeliness and the notation that all federal HCP support provided was used in the preceding calendar year and will be used in the coming calendar year only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. We also obtained the Form 481 filed by the Beneficiary to assess whether the Beneficiary made the required certifications and whether the Beneficiary's supporting documentation agrees to the data reported for the certifications made.

2. Materiality Analysis

For the applicable HCP Forms, we obtained the forms submitted for the periods ended December 31, 2016, March 30, 2017, June 30, 2017 and September 30, 2017, input the information into KPMG's HCP models, and ran a materiality analysis that increased and decreased the account balances by +/- 50%, if the impact generated a +/- 5% or $100,000 change to overall disbursements, the individual line item/account was considered material for purposes of our performance audit.

3. Reconciliation

KPMG obtained the audited 2016 and 2017 financial statements and reconciled to the G/L, from the G/L we reconciled to the Part 64 cost allocation inputs and then to the applicable HCP Forms. We also reconciled the trial balances for the twelve-month periods ended March 31, 2017, June 30, 2017 and September 30, 2017 to the respective Part 64 cost allocation study inputs and then to the 2017-2, 2017-3 and 2017-4 HCL Forms, respectively. We obtained explanations for any reconciling differences.

4. Assets

KPMG utilized a monetary unit sampling methodology to select asset samples from material accounts identified in the relevant HCP Forms. Asset selections were made from CPR details, and material accounts included COE, C&WF and certain general support asset accounts. We assessed whether asset balances were properly supported by underlying documentation such as work orders, third-party vendor invoices, and time and payroll documentation for labor-related costs; agreed dollar amounts charged to the third-party invoices and verified proper Part 32 categorization; and validated the physical existence of selected assets.

KPMG utilized the C&WF CPR details from January 1, 2014 onwards to make our sample selections. The Beneficiary did not maintain complete CPR details for C&WF assets prior to January 1, 2014 CPR details (including the limited period for C&WF assets) covered approximately 77% of the gross book value and 95% of the net book value of the material asset account balances as of September 30, 2017.

5. Expenses

KPMG utilized a monetary unit sampling methodology to select expense samples including payroll from material operating expense accounts identified in the relevant HCP Forms. Expense amounts were agreed to the supporting documentation such as invoices and were reviewed for proper Part 32 account coding and categorization by expense type and nature of the costs incurred (regulated versus non-regulated activities). We also obtained and examined monthly depreciation expense and accumulated depreciation schedules to assess whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation.

6. **HCP Eligibility Forms**

   For the relevant HCP Forms (HCL, ICLS/CAF BLS, and CAF ICC) completeness of reported accounts were assessed via reconciliations to the audited financial statements via the 'Reconciliation' process described above. Reconciling items were discussed with the Beneficiary.

7. **COE Categorization**

   KPMG reviewed the methodology established by the Beneficiary for COE categorization including the process for updating the network map and COE cost studies as well as performing a physical inspection. We assessed whether COE amounts reconciled to studies including reviewing power and common allocations, Part 36 inputs and whether amounts agreed to the HCL form data.

8. **C&WF Categorization**

   KPMG reviewed the methodology established by the Beneficiary for C&WF categorization including the process for updating the network map and C&WF cost studies. We assessed whether C&WF amounts reconciled to studies and whether amounts agreed to the HCL form data and also performed a route distance inspection.

9. **Overhead**

   KPMG performed a walkthrough of the overhead allocation and clearing process related to work orders and payroll for 2016 and 2017. Additionally, we reviewed overhead clearing reports for the entire year and reviewed the overhead clearance process for compliance with Part 32 requirements.

10. **Taxes**

    KPMG assessed the tax filing status for the Beneficiary as a tax-exempt cooperative based on its Federal Income Tax Form 990, "Return of Organization Exempt From Income Tax". We obtained and reviewed the form, and noted the Beneficiary is not required to pay federal or state income taxes on patronage activities.

11. **Part 64 Cost Allocations**

    KPMG reviewed the Beneficiary's cost apportionment methodology and performed procedures to evaluate the apportionment factors which included performing a walkthrough with the Beneficiary and evaluating the reasonableness of the cost pool and regulated/non-regulated apportionment factors as compared to regulated and non-regulated activities performed by the Beneficiary, assessing the reasonableness of the allocation methods and corresponding data inputs used to calculate the material factors and recalculating each of the material factors.

12. **Affiliate Transactions**

    KPMG performed procedures to assess the reasonableness of affiliate transactions via a management and operation agreement among other things that occurred during January 1, 2016 to September 30, 2017. These procedures included determining the population of affiliate transactions by reviewing the audited financial statements, trial balance, and intercompany accounts, and through inquiry, and utilizing attribute sampling to select a sample of the different types of affiliate transactions for testing. For the sample selected, we reviewed the business purpose of each transaction and determined if the transactions were recorded in accordance with 47 C.F.R. Section 32.27 and 47 C.F.R. Section 36.2 and categorized in the appropriate Part 32 accounts.

13. Revenues, Subscriber Listings and Billing Records

KPMG examined revenue G/L accounts, invoices and other related documentation to verify the accuracy and existence of revenue account balances. KPMG analyzed subscriber listings and billing records to assess that the number and type of lines reported in the HCP filings agreed to underlying support documentation that subscriber listings did not include duplicate lines, invalid data, or non-revenue producing or non-working loops, and that lines were properly classified as residential/single-line business or multi-line business.

14. Revenue Requirement

KPMG reviewed the calculation of the Beneficiary's revenue requirement, including assessing the reasonableness and application of Part 64 cost allocation, Part 36 and Part 69 separations and other cost study adjustments utilized in the calculation of the common line revenue requirement. KPMG obtained the projected data reported on FCC Forms 508 and compared against associated FCC Form 509 representing actual data, as applicable. KPMG inquired of the Beneficiary regarding the process related to determination of projections related to ICLS and BLS funding mechanisms.

RESULTS

KPMG's performance audit results include a listing of findings, recommendations and Beneficiary responses, with respect to the Beneficiary's compliance with FCC requirements, and an estimate of the monetary impact of such findings relative to 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69, applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018. USAC Management is responsible for any decisions and actions resulting from the findings or recommendations noted.

FINDINGS, RECOMMENDATIONS AND BENEFICIARY RESPONSES

KPMG's performance audit procedures identified five findings. The findings, including the condition, cause, effect, recommendation and Beneficiary response are as follows:

Finding #1 HC2019BE012-F01: 47 C.F.R. Section 64.901(a) – Improper Inclusion of Non-Regulated Amounts (Operating Expenses)

CONDITION

KPMG obtained and examined a sample of 46 operating expenses totaling $593,933 to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. The Beneficiary did not accurately and appropriately allocate the following six operating expenses ($315,942) between regulated and non-regulated activities, and between affiliates for the period from January 1, 2016 to September 30, 2017:

i. An expense related to leftover cable after provisioning for a project ($106,740) was recorded to C&WF regulated expense account (Account 6420 – C&WF Expense) in its entirety instead of being transferred to construction and/or plant specific operations expenses based on allocation of direct labor hours incurred on the special project.

ii. A COE asset transferred from an affiliate ($83,137) was inappropriately recorded as COE expense (Account 6230 – COE Transmission) to the regulated entity. Additionally, the transfer was recorded, as an expense, at the gross book value of the asset instead of net book value. The affiliate records held the asset for one full year prior to the transfer to the regulated entity.

iii. A C&WF expense (Account 6420 – C&WF Expense) related to 2015 annual physical inventory adjustment ($62,204) was recorded as an expense in 2016.

iv. Four General Support expenses (Account 6120 – General Support Expense) related to software license renewals ($41,261) were not allocated between regulated and nonregulated entities/activities. Amounts recalculated resulted in expenses overstated by $413.

v. A corporate operations expense (Account 6710 – Executive and Planning[4]) related to legal and planning services ($11,600) was not allocated between regulated and non-regulated entities/activities. Amounts recalculated resulted in expenses overstated by $1,044.

[4] For periods corresponding to HCL Forms 2017-1, 2017-02, 2017-3 and 2017-4, the Beneficiary exceeded the allowable Corporate Operations Expense Caps by $24,383, $68,408, $71 and $24,500, respectively.

vi. A planning expense (Account 6710 – Executive and Planning[5]) for services ($11,000) performed outside the cost study area was inappropriately expensed to the regulated entity in its entirety.

Additionally, KPMG analyzed transactions recorded to the Corporate Operations Expense[5] accounts for potential expenses unrelated to the provision of regulated services. KPMG reviewed the general ledger details, of these accounts (for the period of January 1, 2016 to September 30, 2017) for transactions that do not support provision, maintenance, and upgrading of facilities and services. Based on the analysis, KPMG identified 377 ineligible expense transactions ($90,493) recorded as regulated Corporate Operations expenses. The Beneficiary recorded these transactions in the following expense categories within regulated Corporate Operations Expense accounts:

Expense Type	# of Transactions	Amount
Entertainment	91	$29,078
Sponsorships	78	$20,751
Scholarships	24	$20,146
Gifts	62	$7,425
Memberships	19	$5,225
Donations	94	$4,951
Family Travel	2	$2,593
Penalty	3	$277
Food	4	$47
Total	**377**	**$90,493**

CAUSE

The Beneficiary's preparation, review and approvals related to the Part 64 common cost allocation process did not detect the use of inappropriate cost allocation methodologies or miscalculations in the determination of certain regulated expenses. Additionally, the Beneficiary's preparation, review and approvals related to the recording of regulated costs did not detect the improper inclusion of ineligible expenses in regulated expense accounts.[6]

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $136,581 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	$108,031
ICLS	$28,550
CAF BLS	N/A
CAF ICC	N/A
Total	**$136,581**

RECOMMENDATION

[5] For periods corresponding to HCL Forms 2017-1, 2017-02, 2017-3 and 2017-4, the Beneficiary exceeded the allowable Corporate Operations Expense Caps by $24,383, $68,408, $71 and $24,500, respectively.
[6] *FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821, 11822 (2015).

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

KPMG recommends that the Beneficiary enhance controls and procedures related to preparation, review and approvals related to the calculation, recording and reporting of regulated expenses. Specifically, the Beneficiary must update its procedures to ensure that expenses are allocated between regulated and non-regulated using an updated cost causative allocation factor and to ensure that only expenses used for the provision, maintenance, an upgrading of facilities are reported for High Cost Program purposes. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website

at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Wabash Telephone Cooperative agrees with a majority of the findings listed above.

However, we disagree with the application of the third bullet point regarding the costs of the 2015 physical inventory. The company does not dispute the timing of recognition due to an inadvertent accounting error, the expense for the 2015 inventory process was booked to a prepaid account and expensed in 2016. That said, both parties agree that the costs of the inventory are regulated, and includable in USF filings, so we feel there should be no financial impact related to this finding. To remove cost and "penalize" company for a simple error which would result in a total elimination of this expense would be unfair to company and its subscribers. The company position is that by removing the expense from the 2016 data filings, Wabash would be unable to recover on this eligible expense unless USAC agreed to allow it to update the 2015 data and submit for additional recovery. We feel that while the finding is accurate due to the timing of audit, to impose financial penalty for what is a simple timing error and not providing company opportunity to recover legitimate costs for this specific finding would be arbitrary and not in spirit of the overall program.

We agree with the findings related to bullet points 1,2,4,5,6 as well as the non-regulated expenses listed in the table.

We have updated our accounting procedures to correct the findings to comply with the issues listed in the finding in future USF filings.

KPMG RESPONSE

KPMG reviewed the Beneficiary's response and understand their viewpoint. However, we are auditing the time period of January 1, 2016 through September 30, 2017. As noted in the Condition for item #3 – Inventory Adjustment, the regulated costs recorded to Account 6420 – C&WF Expense in 2016 relate to 2015 inventory physical count adjustment and should not be reported on applicable 2016 USF filings. The expense was not recorded in regulated accounts for the correct accounting period in 2015, pursuant to applicable Rules as listed in the Criteria section of this report. We suggest the Beneficiary update its filings when significant changes arise that it would like to be reimbursed for within the 24-month Part 36 revision window.

Finding #2 HC2019BE012-F02: 47 C.F.R. Section 32.2(a)(b) – Improper

Distribution of Overhead Amounts

CONDITION

KPMG obtained and examined the overhead clearing reports for each month from January 1, 2016 to September 30, 2017 to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. The Beneficiary inappropriately cleared specific overhead expense amounts (Account 6112 – Motor Vehicle Expense and Account 6534 – Plant Operations Administrative Expense) for the period from January 1, 2016 to September 30, 2017 to ineligible and/or inaccurate expense accounts. Additionally, the Beneficiary also utilized two Corporate Operations Expense accounts (Account 6723 – Human Resource Expense and Account 6728 – Other General and Administrative Expense*) as overhead expense accounts and cleared to certain plant specific, nonspecific and corporate operations expense accounts. The Beneficiary's G/L system is configured to clear all overhead expenses based on direct labor payroll cost; as such Account 6512 – Provisioning Expense was not cleared appropriately using cost of materials. Summary of inappropriately cleared overhead expenses are as follows:

Account 6112 – Motor Vehicle Expense

Overhead Expense Account	Original Allocated Amount	Revised Allocated Amount	21 Month Period Variance (a)	Annualized Variance (b)
2003 – TPUC	$147,337	$191,263	$43,926	$25,101
6110 – Network Support Expense	($10,193)	($13,206)	($3,013)	($1,722)
6120 – General Support Expense	$8,177	$10,657	$2,480	$1,417
6210 – COE Switching Expense	$977	$1,476	$499	$285
6230 – COE Transmission Expense	$61,418	$79,576	$18,158	$10,376
6410 – Cable & Wire Expense	$460	$2,541	$2,081	$1,189
6420 – Cable & Wire Expense	$87,565	$113,453	$25,888	$14,793
6510 – Provisioning Expense	$20,801	$0	($20,801)	($11,886)
6530 – Network Admin Expense	$43,807	$0	($43,807)	($25,033)
6610 – Marketing Expense	$169	$0	($169)	($97)
6620 – Customer Services Expense	$141	$0	($141)	($81)
6710 – Executive and Planning Expense	$16,279	$0	($16,279)	($9,302)
6720 – General and Administrative Expense	$23,095	$0	($23,095)	($13,197)
Non-Regulated Accounts/Activities	$47,585	$61,858	$14,273	$8,157
Total	**$447,618**	**$447,618**	**$0**	**$0**

Note: (a) A positive variance represents under allocation and a negative variance represents over allocation for the 21-month period ended September 30, 2017 (b) Annualized variance was determined based on average monthly variance.

Account 6534 – Plant Operations Administration Expense

Overhead Expense Account	Original Allocated Amount	Revised Allocated Amount	21 Month Period Variance (a)	Annualized Variance (b)
2003 – TPUC	$16,847	$41,371	$24,524	$14,013
6120 – General Support Expense	$762	$0	($762)	($435)
6210 – COE Switching Expense	$132	$0	($132)	($75)
6230 – COE Transmission Expense	$40,364	$0	($40,364)	($23,065)
6420 – Cable & Wire Expense	$38,565	$0	($ 38,565)	($22,037)
6530 – Network Admin Expense	$0	$960	$960	$549

Non-Regulated Accounts	$37,331	$91,670	$54,339	$31,050
Total	**$134,001**	**$134,001**	**$0**	**$0**

Note: (a) A positive variance represents under allocation and a negative variance represents over allocation for the 21-month period ended September 30, 2017 (b) Annualized variance was determined based on average monthly variance.

Account 6720 – General & Administrative Expense (Accounts 6723 and 6728) (*)

Overhead Expense Account	Original Allocated Amount	Revised Allocated Amount	21 Month Period Variance (a)	Annualized Variance (b)
2003 – TPUC	$6,388	$0	($6,388)	($3,650)
6120 – General Support Expense	$317	$0	($317)	($181)
6210 – COE Switching Expense	$37	$0	($37)	($21)
6230 – COE Transmission Expense	$2,737	$0	($2,737)	($1,564)
6420 – Cable & Wire Expense	$4,162	$0	($4,162)	($2,378)
6530 – Network Admin Expense	$3,004	$0	($3,004)	($1,717)
6610 – Marketing Expense	$43	$0	($43)	($25)
6620 – Customer Services Expense	$1,114	$0	($1,114)	($636)
6710 - Executive and Planning Expense	$1,774	$0	($1,774)	($1,014)
6720 – General and Administrative Expense	$5,248	$0	($5,248)	($2,999)
Non-Regulated Accounts	$2,352	$27,176	$24,824	$14,185
Total	**$27,176**	**$27,176**	**$0**	**$0**

Note: (a) A positive variance represents under allocation and a negative variance represents over allocation for the 21-month period ended September 30, 2017 (b) Annualized variance was determined based on average monthly variance.

*For periods corresponding to HCL Forms 2017-1, 2017-02, 2017-3 and 2017-4, the Beneficiary has exceeded allowable Corporate Operations Expense Caps by $24,383, $68,408, $71 and $24,500, respectively.

CAUSE

The preparation, review and approval processes governing the clearing of benefits and overhead amounts did not detect the allocation of amounts to incorrect Part 32 accounts.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $28,927 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	$20,377
ICLS	$8,550
CAF BLS	N/A
CAF ICC	N/A
Total	**$28,927**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

KPMG recommends that the Beneficiary evaluate and update the methodology used for clearing overhead to the appropriate Part 32 expense accounts. In addition, the Beneficiary should enhance the preparation, review and approval processes governing the clearing of overhead related amounts. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY

Wabash Telephone Cooperative agrees with the listed condition. We have already made updates to our clearing processes to comply with the finding in future USF filings.

Finding #3 HC2019BE012-F03: 47 C.F.R. Section 64.901(a) – Improper Inclusion of Non-Regulated Amounts (Payroll Expenses)

CONDITION

KPMG obtained and examined a sample of 17 payroll expenses totaling $143,931, including time recorded to regulated activities by certain management employees in its entirety without appropriate allocation to non-regulated activities and/or affiliates. For the period between January 1, 2016 through September 30, 2017, the Beneficiary did not accurately and appropriately allocate certain payroll expenses (totaling $719,324 related to four management employees) between regulated and non-regulated activities, and between affiliates for certain management employees using cost causative factors. The recalculated payroll expenses for these management employees resulted in an overstatement of $64,739 in regulated balances. Payroll expenses associated with these specific management employees were –

- For the period between January 1, 2016 and December 31, 2016 - $349,044
- For the period between January 1, 2017 and September 30, 2017 - $370,280

CAUSE

The preparation, review and approvals related to the Part 64 common cost allocation process did not detect inappropriate allocation of certain management employees' payroll expenses to regulated entities/activities.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $5,025 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	$4,135
ICLS	$890
CAF BLS	N/A
CAF ICC	N/A
Total	**$5,025**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the

Effect section above.

KPMG recommends that the Beneficiary enhance controls and procedures related to recording regulated payroll expenses using cost causative allocation factors in accordance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Wabash Telephone Cooperative agrees with the listed condition. We have already made updates to our payroll processes to comply with the finding in future USF filings.

Finding #4 HC2019BE012-F04: 47 § 64.901(a) – Improper Allocation Methodology

CONDITION

KPMG obtained and examined the general ledger and cost study factors to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. The Beneficiary did not allocate property taxes related to certain General Support Facility (GSF) assets between regulated and non-regulated activities. For the year ended December 31, 2016, the Beneficiary allocated GSF assets totaling $513,309 out of a total balance of $2,371,296 to non-regulated activities. Associated plant specific operating expenses, depreciation and accumulated depreciation amounts were appropriately allocated to non-regulated activities; however, the Beneficiary did not allocate corresponding property taxes in the amount of $5,112 to non-regulated activities.

CAUSE

The preparation, review and approvals related to the Part 64 common cost allocation process were not complete to include all relevant associated GSF asset costs, including property taxes.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an over-disbursement of $4,327 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	$3,064
ICLS	$1,263
CAF BLS	N/A
CAF ICC	N/A
Total	**$4,327**

RECOMMENDATION

KPMG recommends that USAC Management seek recovery of the amounts identified in the Effect section above.

KPMG recommends that the Beneficiary enhance its preparation, review and approval processes governing the derivation and reporting of Part 64 cost allocation data to ensure that all costs related to GSF assets are appropriately allocated to non-regulated activities in compliance with FCC Rules and Orders. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Wabash Telephone Cooperative agrees with the listed condition. We will make an entry to remove the non-regulated portion of property taxes in future USF filings.

Finding #5 HC2019BE012-F05: 47 C.F.R. Section 32.2000(g)(2)(i) – Inaccurate Depreciation Calculation

CONDITION

KPMG obtained and examined the general ledger and depreciation schedules to determine whether the Beneficiary reported its cost study balances accurately for High Cost Program purposes. The Beneficiary used month end balances instead of average monthly balances to compute depreciation expense as prescribed by FCC Rules for the period of January 1, 2016 through September 30, 2017.

The differences noted in the Accumulated Depreciation and Depreciation Expense balances for the twelve-month period ended December 31, 2016, impacting the 2017-1 HCL Form and 2017 Form 509, and corresponding periods ended March 31, June 30, and September 30, 2017, impacting the 2017-2, 2017-3, and 2017-4 HCL Forms, are as follows:

Account Description	For the 12 months ended Dec. 31, 2016 Variance	For the 12 months ended Mar. 31, 2017 Variance	For the 12 months ended June 30, 2017 Variance	For the 12 months ended Sept. 30, 2017 Variance
Account 3100 (2110): Accumulated Depreciation -Land and General Support Assets	($55,587)	($20,552)	($70,104)	$70,109
Account 3100 (2210): Accumulated Depreciation – Central Office Switching	$0	$1,500	$0	$0
Account 3100 (2230): Accumulated Depreciation – Central Office Transmission Equipment	$48,290	$45,897	$36,701	$7,222
Account 3100 (2410): Accumulated Depreciation - Cable and Wire Facilities	$81,690	$80,354	$71,838	$30,644
Account 6560: Depreciation and Amortization - Expense	$74,393	$107,198	$38,435	$107,975

Note: Negative amounts noted above represent an overrstatement of the regulated account balances.

CAUSE

The preparation, review and approval processes governing the calculation of accumulated depreciation and depreciation expense did not detect inappropriate depreciation methodology used by the Beneficiary which was not in accordance with FCC Rules.

EFFECT

The monetary impact of this finding relative to disbursements made from the HCP for the twelve-month period ended December 31, 2018 is an under-disbursement of $57,470 and is summarized as follows:

Support Type	Monetary Effect & Recommended Recovery
HCL	($44,274)
ICLS	($13,196)
CAF BLS	N/A
CAF ICC	N/A
Total	**($57,470)**

RECOMMENDATION

KPMG recommends that the Beneficiary enhance its preparation, review and approval processes governing the calculation of depreciation to ensure compliance with FCC Rules and Orders. Specifically, the Beneficiary must update its processes to ensure that depreciation is calculated using average monthly asset balances. In addition, the Beneficiary may learn more about the reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

Wabash Telephone Cooperative agrees with the listed condition. We have already made updates to our monthly depreciation procedures to use average monthly investment balances.

CRITERIA

Finding	Criteria	Description
#1	47 C.F.R. Section 32.12(b) (2016)	"The company's financial records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission."
#1	47 C.F.R. § 54.7(a) (2016)	"A carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."
#1	*FCC Reminds ETCs of High-Cost Support Requirements*, WC Docket No. 10-90, Public Notice, FCC 15-133, 30 FCC Rcd 11821, 11822 (2015).	"The Commission reminds all eligible telecommunications carriers (ETCs) that receive support from the Universal Service Fund's high-cost mechanisms (whether legacy high-cost program support or Connect America Fund support) of their obligations to use such support only for its intended purposes of maintaining and extending communications service to rural, high-cost areas of the nation. ….. The following is a non-exhaustive list of expenditures that are not necessary to the provision of supported services and therefore may not be recovered through universal service support: • Personal travel; • Entertainment; • Alcohol; • Food, including but not limited to meals to celebrate personal events, such as weddings, births, or retirements; • Political contributions; • Charitable donations; • Scholarships; • Penalties or fines for statutory or regulatory violations; • Penalties or fees for any late payments on debt, loans or other payments • Membership fees and dues in clubs and organizations; • Sponsorships of conferences or community events; • Gifts to employees; and Personal expenses of employees, board members, family members of employees and board members, contractors, or any other individuals affiliated with the ETC, including but not limited to personal expenses for housing, such as rent or mortgages."
#1,3,4	47 C.F.R. Section 64.901(a) (2016)	"Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose."
#1,3	47 C.F.R. Section 32.14(c) (2016)	"In the application of detailed accounting requirements contained in this part, when a regulated activity involves the common or joint use of assets and resources in the provision of regulated and nonregulated products and services, companies shall account for these activities within the accounts prescribed in this system for telephone company operations. Assets and expenses shall be

Finding	Criteria	Description
		subdivided in subsidiary records among amounts solely assignable to nonregulated activities, amounts solely assignable to regulated activities, and amounts related to assets used and expenses incurred jointly or in common, which will be allocated between regulated and nonregulated activities. Companies shall submit reports identifying regulated and nonregulated amounts in the manner and at the times prescribed by this Commission. Nonregulated revenue items not qualifying for incidental treatment, as provided in [47 C.F.R.] § 32.4999(l), shall be recorded in Account 5280, Nonregulated operating revenue."
#2	47 C.F.R. Section 32.2 (2016)	"(a) The financial accounts of a company are used to record, in monetary terms, the basic transactions which occur. Certain natural groupings of these transactions are called (in different contexts) transaction cycles, business processes, functions or activities. The concept, however, is the same in each case; i.e., the natural groupings represent what happens within the company on a consistent and continuing basis. This repetitive nature of the natural groupings, over long periods of time, lends an element of stability to the financial account structure. (b) Within the telecommunications industry companies, certain recurring functions (natural groupings) do take place in the course of providing products and services to customers. These accounts reflect, to the extent feasible, those functions. For example, the primary bases of the accounts containing the investment in telecommunications plant are the functions performed by the assets. In addition, because of the anticipated effects of future innovations, the telecommunications plant accounts are intended to permit technological distinctions. Similarly, the primary bases of plant operations, customer operations and corporate operations expense accounts are the functions performed by individuals. The revenue accounts, on the other hand, reflect a market perspective of natural groupings based primarily upon the products and services purchased by customers."
#2	47 C.F.R. Section 32.6112(b) (2016)	"Credits shall be made to this account for amounts transferred to Construction and/or to other Plant Specific Operations Expense accounts. These amounts shall be computed on the basis of direct labor hours."
#2	47 C.F.R. § 32.6534(b) (2016)	"Credits shall be made to this account for amounts transferred to construction accounts. These amounts shall be computed on the basis of direct labor hours."
#5	47 C.F.R. Section 32.2000(g)(2)(iii) (2016)	"Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one- twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The average monthly balance shall be computed using the balance as of the first and last days of the current month."

CONCLUSION

KPMG's evaluation of the Beneficiary's compliance with the applicable requirements of 47 C.F.R. Parts 32, 36, 51, 54, 64 and 69 applicable to the disbursements made from the HCP during the twelve-month period ended December 31, 2018 identified, improper inclusion of expense and payroll non-regulated amounts, improper distribution of overhead amounts findings, improper allocation methodology for property taxes and inaccurate depreciation calculation. Detailed information relative to the findings is described in the Findings, Recommendations and Beneficiary Responses section above.

The combined estimated monetary impact of these findings is as follows:

Fund Type	Monetary Impact Overpayment (Underpayment)
HCL	$ 91,333
ICLS	$ 26,057
Total Impact	**$ 117,390**

KPMG recommends that the Beneficiary enhance the preparation, review and approval processes related to allocating Part 64 common costs, recording allowable expenses, clearing overheads, and calculating depreciation in accordance with FCC Rules and Orders.

ATTACHMENT L

HC2017LR012

Available For Public Use

Universal Service
Administrative Co.

Waitsfield-Fayston Telephone Co., Inc.

Limited Review Performance Audit on Compliance with the Federal Universal Service Fund High Cost Support Mechanism Rules
USAC Audit No. HC2017LR012

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EXECUTIVE SUMMARY

November 18, 2020

Roger Nishi
Vice President – Industry Relations
Waitsfield-Fayston Telephone Co., Inc.
3898 Main Street
P.O. Box 9
Waitsfield, VT 05673-0009

Dear Roger Nishi:

The Universal Service Administrative Company (USAC) Audit and Assurance Division (AAD) audited the compliance of Waitsfield-Fayston Telephone Co., Inc. (Beneficiary), study area code 140069 disbursements for the year ending December 31, 2016, using the regulations and orders governing the federal Universal Service High Cost Support Mechanism, set forth in 47 C.F.R. Parts 32, 36, 51, 54, 64, and 69, as well as other program requirements (collectively, the Rules). Compliance with the Rules is the responsibility of the Beneficiary's management. AAD's responsibility is to make a determination regarding the Beneficiary's compliance with the Rules based on our limited review performance audit.

AAD conducted the audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2011 Revision, as amended). Those standards require that AAD plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for its findings and conclusions based on the audit objectives. The audit included examining, on a test basis, evidence supporting the data used to calculate support, as well as performing other procedures we considered necessary to form a conclusion. The evidence obtained provides a reasonable basis for AAD's findings and conclusions based on the audit objectives.

Based on the test work performed, our examination disclosed ten detailed audit findings (Findings), as discussed in the Audit Results and Recovery Action section. For the purpose of this report, a Finding is a condition that shows evidence of non-compliance with the Rules that were in effect during the audit period.

Certain information may have been omitted from this report concerning communications with USAC Management or other officials and/or details about internal operating processes or investigations. This report is intended solely for the use of USAC, the Beneficiary, and the Federal Communication Commission (FCC) and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of those procedures for their purposes. This report is not confidential and may be released to a requesting third party.

We appreciate the cooperation and assistance extended by your staff during the audit.

Sincerely,

Teleshia Delmar
Teleshia Delmar
USAC Vice President, Audit and Assurance Division

cc: Radha Sekar, USAC Chief Executive Officer
Vic Gaither, USAC Vice President, High Cost Division

AUDIT RESULTS AND RECOVERY ACTION

Audit Results	Monetary Effect & Recommended Recovery[1]
Finding #1: 47 C.F.R. § 54.320(b) – Lack of Documentation: Expenses. The Beneficiary was unable to provide documentation to substantiate the value of one expense sample reported for High Cost Program purposes.	$12,320
Finding #2: 47 C.F.R. § 54.320(b) - Inadequate Documentation: Cost Study Adjustments. The Beneficiary's supporting documentation was insufficient and improper to substantiate certain cost study adjustments.	$8,546
Finding #3: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support. The Beneficiary included transactions that were not used for the provision, maintenance, and upgrading of facilities and services for which the support was intended for High Cost Program purposes.	$5,677
Finding #4: 47 C.F.R. § 54.320(b) – Inadequate Documentation: Assets. The Beneficiary did not provide adequate supporting documentation to substantiate a portion of value for certain the assets reported for High Cost Program purposes.	$4,053
Finding #5: 47 C.F.R. § 54.903(a)(1) – Misclassified Access Lines. The Beneficiary did not correctly classify some of its access lines reported for High Cost Program purposes.	$1,388
Finding #6: 47 C.F.R. § 32.2000(e)(1)(i),(e)7(i)(A-B), (f)(2)(iii), f(5) – Inadequate Continuing Property Records. The Beneficiary's continuing property records for Cable and Wire Facilities lacked sufficient detail for High Cost Program purposes.	$0
Finding #7: 47 C.F.R. § 32.2000(e)7(i)(B), (f)(2)(iii), f(5) – Improper Continuing Property Records. The Beneficiary's Central Office Equipment property records lacked sufficient detail, specifically a physical location or address, for the auditors to verify the property by physical examination of the assets recorded.	(1,226)
Finding #8: 47 C.F.R. § 64.901(b) – Improper Inclusion of Non-Regulated Asset. The Beneficiary did not provide sufficient evidence that certain non-regulated assets were properly recorded as non-regulated assets and reported for High Cost Program purposes.	($1,637)
Finding #9: 47 C.F.R. § 54.903(a)(4) – Inaccurate Subscriber Line Charge Revenue. The Beneficiary's end user Subscriber Line Charge revenues reported for High Cost purposes did not agree to the Beneficiary's supporting documentation.	($1,993)
Finding #10: 47 C.F.R. § 32.2000(g)(2) – Inaccurate Depreciation Expense and Accumulated Depreciation Calculation. The Beneficiary incorrectly calculated its depreciation expense for High Cost Program purposes.	($45,437)
Total	**$(18,309)**

[1] The recovery amount noted in the table is not reflective of prior period or cap adjustments. The actual recovery amount for this final audit report will not exceed the proposed recovery amount.

USAC MANAGEMENT RESPONSE

USAC Management concurs with the audit results and will seek recovery of the High Cost Program support from the Beneficiary for SAC 140069 in the amount noted in the table below.

The Beneficiary must implement policies and procedures necessary to comply with the Rules. USAC recommends that the Beneficiary implement internal controls to ensure correct application of its procedures to ensure compliance with FCC Rules and Orders.

Regarding Finding #1, USAC Management requires the Beneficiary to be placed on a corrective action plan (C.A.P.) to address the Lack of Documentation: Expenses. As part of the C.A.P., the Beneficiary must report to High Cost Management, within 60 days of the date of the Recovery Letter to be issued by High Cost Program, how it plans to improve its documentation processes.

	ICLS (A)	CAF ICC (B)	USAC Recovery Action (A) + (B)[2]	Rationale for Difference (if any) from Auditor Recommended Recovery
Finding #1	$12,320	$0	$12,320	
Finding #2	$8,546	$0	$8,546	
Finding #3	$5,677	$0	$5,677	
Finding #4	$4,053	$0	$4,053	
Finding #5	$1,388	$0	$1,388	
Finding #6	$0	$0	$0	
Finding #7	($1,226)	$0	($1,226)	
Finding #8	($1,637)	$0	($1,637)	
Finding #9	($1,993)	$0	($1,993)	
Finding #10	($45,437)	$0	($45,437)	
Mechanism Total	**$(18,309)**	**$0**	**$0**[3]	

As the above findings represent a net underpayment, the total recommended recovery (and thus the recommended recovery for each individual finding) is zero as USAC policy is not to issue support in the case of a net underpayment. Thus, USAC recovery action is $0.

[2] *Id.*
[3] As the findings represent a net underpayment, the total USAC Recovery Action is $0.

PURPOSE, SCOPE AND PROCEDURES

PURPOSE
The purpose of our audit was to determine whether the Beneficiary complied with the Rules.

SCOPE
In the following chart, AAD summarizes the High Cost Program support that was included in the scope of this audit:

High Cost Support	Data Period	Disbursement Period	Disbursements Audited
Connect America Fund (CAF) Intercarrier Compensation (ICC)	2014-2015	2016	$2,356,932
Interstate Common Line Support (ICLS)	2014	2016	$2,535,057
Total			**$4,891,989**

BACKGROUND
The Beneficiary is a cost-based eligible telecommunications carrier (ETC) that operates in Vermont.

PROCEDURES
AAD performed the following procedures:

A. High Cost Program Support Amount
AAD recalculated the support that the Beneficiary received for each High Cost component and determined that there were no more than nominal differences between the amounts received and those recorded in the High Cost system.

B. High Cost Program Process
AAD obtained an understanding of the Beneficiary's processes related to the High Cost Program to determine whether the Beneficiary complied with the Rules. AAD also obtained and examined documentation to determine whether the Beneficiary reported the information in its High Cost data filings consistent with based on the dates established by the Rules (*i.e.,* month or year-end, as appropriate).

C. Subscriber Listing and Billing Records
AAD obtained and examined the Beneficiary's subscriber listings and billing records. AAD used computer-assisted auditing techniques to analyze the data files and to determine whether:

- The number and type of lines in the data files agreed to the number and type of lines reported on the Beneficiary's High Cost data filings;
- The data files contained duplicate lines;

- The data files contained blank or invalid data;
- The data files contained non-revenue producing or non-working loops; and
- The lines in the data files were identified with the proper residential/single line business (Res/SLB) or multi-line business (MLB) classification.

D. Fixed Assets

AAD obtained and examined the Beneficiary's continuing property records (CPRs) and related documentation to determine whether the Beneficiary reported accurate central office switching equipment balances as well as cable and wire facility equipment balances. AAD also examined documentation and conducted a physical inventory to determine whether the Beneficiary categorized fixed assets to the proper accounts.

E. Operating Expenses

AAD obtained and examined tax reports, accrual schedules, and related documentation to determine whether the Beneficiary reported accurate tax expenses and deferred tax liabilities. AAD obtained and examined monthly depreciation and plant accumulated depreciation schedules to determine whether the Beneficiary reported accurate depreciation expenses and accumulated depreciation. AAD obtained and examined the allocation method and summary schedules to determine whether the Beneficiary reported accurate benefit and rent expenses. AAD obtained and examined general ledger details for select expenses and examined invoices to support the existence of the general support, corporate operations, plant specific, and plant non-specific expenses.

F. Revenues

AAD obtained and examined the general ledger, invoices, and other related documentation to determine whether the Beneficiary reported accurate common line and other revenue balances.

G. Form 481

AAD obtained and examined the Beneficiary's FCC Form 481 (Form 481) for accuracy by comparing select reported to the Beneficiary's data files.

DETAILED AUDIT FINDINGS

Finding #1: 47 C.F.R. § 54.320(b) – Lack of Documentation: Expenses

CONDITION

AAD requested documentation for a non-statistical sample of 10 expenses totaling $402,171 to determine whether the Beneficiary reported the correct amounts for High Cost Program purposes. The Beneficiary was unable to provide documentation to substantiate the value of one expense sample, a reclassification transaction totaling $141,580 from Account 6210 – Central Office Switching to Account 6230 – Central Office Transmission. Because the Beneficiary did not maintain and provide supporting documentation to validate the accuracy of the reclassification, AAD concludes that the Beneficiary improperly recorded one expense transaction totaling $141,580.

CAUSE

The Beneficiary did not have adequate documentation or data retention procedures to report the correct amount for High Cost Program purposes. The Beneficiary informed AAD that central office (CO) technicians were not charging the appropriate time to circuit equipment. The Beneficiary stated that it made an adjusting entry to correct time reporting for January 1, 2014 to September 30, 2014.[4]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the unsupported amount reported by the Beneficiary in its respective account in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$12,320

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. The Beneficiary must implement policies and procedures to create and maintain supporting documentation, which will strengthen internal controls surrounding the process of reporting amounts for High Cost Program purposes. The Beneficiary should provide training to technicians on how to record their time to the proper amount. In addition, the Beneficiary can learn more about documentation and

[4] Beneficiary responses to audit inquiries, received Jan. 3, 2020.

reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #2: 47 C.F.R. § 54.320(b) – Inadequate Documentation: Cost Study Adjustments

CONDITION

AAD obtained and examined documentation for all cost study adjustments (69 adjustments in total) to determine whether the Beneficiary reported the correct amounts for High Cost Program purposes. The AAD noted that the Beneficiary's supporting documentation was insufficient and improper to substantiate the accuracy of 25 out of 69 total cost study adjustments. For 14 out of 25 cost study adjustments, the Beneficiary provided cost study adjustment entries reclassifying expenses maintenance, storm damage work and retirements of assets related to carry-forward balances. For the remaining 11 out of 25 cost study adjustments, the Beneficiary provided cost study adjustment entries reclassifying customer sales expenses and assets categories. The Beneficiary supported these 25 cost study adjustments with a brief description and a calculation; however, no invoice or underlying data was provided to validate the rationale or allocation methodology for why the adjustment was needed. Further, the cost study adjustments related to assets appeared to be recorded to compensate for continued property records (CPR) not properly maintained (i.e., to adjust for retirements of carry-forward assets).[5] The table below summarizes the amounts not substantiated:

Account Description	Amount
Central Office – Switching (Acct. 2210)	$551,353
Central Office – Transmission (Acct. 2230)	($725,807)
Central Office – Switching (Accumulated Depreciation)	($194,593)
Central Office – Transmission (Accumulated Depreciation)	$402
Marketing Expense (Acct. 6610)	$116,287
Customer Service Expense (Acct. 6620)	($135,007)
General and Administrative Expense (Acct. 6720)	$18,720

Because the Beneficiary did not provide adequate documentation, AAD concludes that the Beneficiary did not properly record 25 cost study adjustments reported for High Cost Program purposes.

[5] *See* Finding #7 for further details.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to report the correct amount for High Cost Program purposes. The Beneficiary informed AAD that it classified some assets as non-regulated and later identified them as regulated. The Beneficiary also had some adjustments that reclassified expenses to capital accounts. The Beneficiary did not make these entries on the books or CPR so the entries were carried forward amounts in the cost study balances.[6]

EFFECT

AAD calculated the monetary effect for this finding by subtracting or adding the recorded value of the overstatement from or understatement to the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$8,546

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. The Beneficiary must implement an adequate system to properly report the correct amounts for High Cost Program purposes. The Beneficiary must implement a process and/or system enhancements that retains supporting information related to cost study adjustments and records the adjustments in the general ledger or CPR. Further, the Beneficiary must implement policies and procedures, which will strengthen internal controls surrounding the process of reporting amounts for High Cost Program purposes, including ensuring all cost study adjustments are accurate, and properly supported by documentation. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #3: 47 C.F.R. § 54.7(a), FCC 15-133 and FCC 18-29 – Support Not Used for Intended Purpose of Federal Universal Service Support

CONDITION

[6] Beneficiary responses to audit inquiries, received Jan. 3, 2020.

AAD obtained and examined the Beneficiary's general ledger, Continuing Property Records (CPR) and cost study adjustments documentation to determine whether High Cost Program support was only used for the provision, maintenance, and upgrading of facilities and services for which the support is intended.

As summarized below, the Beneficiary did not exclude 197 transactions, totaling $34,274, from all general ledger transactions and reported in various expense accounts related to food, charitable donations, membership fees and dues in clubs and organizations, sponsorships of conferences or community events, scholarships, and gifts to employees that were not necessary for the provision, maintenance, and upgrading of facilities.

Account Description	Amount
6120 – General Support Expenses	$6,735
6210 - Central Office Switching Expenses	$917
6410 – Cable and Wire Facilities Expenses	$656
6530 – Network Operations Expenses	$1,301
7300 – Non-operating Income and Expenses	$24,665
Total	**$34,274**

AAD clarifies that while FCC 15-33 and FCC 18-29 were released after the audit period, the FCC rule that was effective during the audit period states that "a carrier that received federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."[7] The Beneficiary should have removed these unallowable transactions during its cost study process.

Because the Beneficiary's reported balances included 197 unallowable transactions, AAD concludes that the Beneficiary's High Cost Program support was not used for the provision, maintenance, and upgrading of facilities and services for which the support is intended.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to properly exclude unallowable expenses from the amounts reported for High Cost Program purposes. The Beneficiary informed AAD that these expenses were not deemed excludable until the 2015 FCC Public Notice 15-133 was released in 2015.[8]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the value of the unallowable expenses from the total amount reported by the Beneficiary in its respective accounts in its High Cost filing. We summarize the results below:

[7] *See FCC Reminds ETCS of High-Cost Support Requirements* Public Notice, 30 FCC Rcd 11821 (released Oct. 19, 2015). *See also* 47 U.S.C. § 254(e).
[8] Beneficiary responses to audit results summary, received Jan. 6, 2020.

Support Type	Monetary Effect and Recommended Recovery
ICLS	$5,677

RECOMMENDATION
AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. The Beneficiary must ensure it has an adequate system to exclude unallowable costs and report accurate data for High Cost Program purposes and maintain documentation to demonstrate compliance with the FCC Rules. Further, the Beneficiary must implement policies and procedures, which will strengthen internal controls surrounding the process of excluding unallowable costs when reporting amounts for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE
The Commission's October 2015 Public Notice on allowable expenses (FCC 15-133) discusses several different expenses, many of which were already excluded from interstate rates and universal service support by FCC rule. However, prohibitions on other items addressed by the Public Notice, such as the charitable contributions, membership fees, kitchen items, and meals now in question, were not explicitly put into FCC rules until the FCC's March 23, 2018 Order that addressed eligible expenses for interstate rates and USF support on a prospective basis. (FCC 18-29 ¶ 10).

While the FCC's 2018 Order appears to affirm the 2015 Public Notice findings related to these type of expense, there remain serious procedural questions regarding the ability of a public notice to institute new rules, especially when previous FCC decisions and rules seem to support the inclusion of these expenses for recovery though USF and interstate rates.

Notwithstanding the above, the 2014 data in question was related to months prior to the 2015 Public Notice. At that time, Waitsfield's expense data complied with existing FCC rules and reasonably conformed with industry standards with regards to the expenses in question.

AAD RESPONSE
AAD clarifies that the Beneficiary should not have recorded the expenses in regulated accounts pursuant to the FCC's Public Notice in WC Docket Nos. FCC 15-133 and FCC 18-29 which clarified existing FCC Rules and Regulations. The FCC did not make new rules but provided additional clarity on existing rules, such as:

"The Commission reminds all eligible telecommunications carriers (ETCs) that receive support from the Universal Service Fund's high-cost mechanisms (whether legacy high-cost program support or Connect America Fund support) of their obligations to use such support only for its intended purposes of maintaining and extending communications service to rural, high-cost areas of the nation…"

"Just as carriers must not use USF funds for inappropriate expenses, we remind rate-of-return carriers that section 65.450 of our rules prohibits them from including expenses in their revenue requirements unless such expenses are "recognized by the Commission as necessary to the provision" of interstate telecommunications services."

Finding #4: 47 C.F.R. § 54.320(b) – Inadequate Documentation: Assets

CONDITION

AAD obtained and examined the general ledger, Continuing Property Record (CPR), and cost study balances to determine whether the Beneficiary reported accurate asset balances, including a non-statistical sample of 48 assets totaling $1,252,529 for High Cost Program purposes. AAD examined the supporting documentation and noted nine asset samples did not have adequate documentation to substantiate a portion of the assets' value. Therefore, the Beneficiary overstated its Cable and Wire assets amount by $84,162. In addition, AAD calculated the effect of these nine exceptions[9] to its associated depreciation expense and accumulated depreciation accounts, as summarized below:

Account	No of Samples with Exception	Value of Samples with Exception	Unsupported Portion of Samples with Exception	Overstated Accumulated Depreciation	Overstated Depreciation Expense
Cable and Wire Facilities (CWF) (Acct. 2410)	9	$314,031	$84,162	$6,132	3,366

Copies of invoices, detailed allocation schedules, and other relevant documentation are required to substantiate that the Beneficiary recorded its assets in the proper amount and to the proper general ledger account. Because the Beneficiary did not provide adequate documentation to substantiate a portion of nine assets, AAD concludes that the Beneficiary did not report accurate balances.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to ensure the proper retention of records to demonstrate that it recorded assets in the proper amount and to the proper General Ledger accounts. The Beneficiary informed AAD that this issue occurred because some of the assets identified related to jobs lasting longer than a year due to our short construction season in Vermont.[10]

[9] In this report, AAD identifies an "exception" when, based on a review of the Beneficiary-provided evidence/documentation, it identifies a discrepancy or deviation from the norm resulting in audit testing. An exception results in a finding based on the materiality of the exception.

[10] Beneficiary responses to audit inquiries, received Jan. 3, 2020.

EFFECT

AAD calculated the monetary effect for this finding by subtracting the unsupported amount of the transactions in the general ledger for the year from the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect and Recommended Recovery
ICLS	$4,053

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount noted in the Effect section above. The Beneficiary must implement policies and procedures to ensure it has an adequate system, strengthening internal controls surrounding the process of reporting accurate data for High Cost Program purposes and maintaining documentation to demonstrate compliance with FCC Rules. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #5: 47 C.F.R. § 54.903(a)(1) – Misclassified Access Lines

CONDITION

AAD obtained and examined the Beneficiary's subscriber listing to determine whether the Beneficiary accurately reported its access line counts and properly classified its access lines as Residential/Single-Line Business (Res/SLB) or Multi-Line Business (MLB) as of December 31, 2014. AAD identified the following differences between the Beneficiary's subscribers listing and the access line amount and classification it reported:

Description	Residential/Single Line Business	Multi-Line Business
Access Line Counts Reported	14,617	1,806
Access Line Counts Per Subscriber Listing	14,570	1,853
Difference: Over/(Under) Reported	**47**	**(47)**

Because the Beneficiary's supporting documentation did not agree to what was reported for High Cost purposes, AAD concludes that the Beneficiary did not report accurate access line revenues.[11]

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, or monitoring data to report the correct number and classification of subscriber access lines for High Cost Program purposes. The Beneficiary indicated that some customers had multiple accounts that were missed by the Beneficiary's customer service representative as being business multiline and were entered as business single line.[12]

EFFECT

AAD calculated the monetary effect for this finding by multiplying the difference between the Res\SLB rate and the MLB rate by the number of months the affected subscribers had service as of December 31, 2014.

Support Type	Monetary Effect & Recommended Recovery
ICLS	$1,388

RECOMMENDATION

AAD recommends that USAC management seek recovery of the recommended recovery amount identified in the Effect section above. The Beneficiary must ensure it has an adequate system to properly classify its lines and assess the appropriate subscriber line charge for High Cost Program purposes. Further, the Beneficiary must implement policies and procedures, strengthening internal controls surrounding the process of access line classification for High Cost Program purposes. The Beneficiary's system must include providing training to customer service representatives and other key personnel on how to properly classify and record access lines. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

[11] 47 C.F.R. 69.104(h).
[12] Beneficiary responses to audit inquiries, received Dec. 20, 2018.

Finding #6: 47 C.F.R. §32.2000(e)(1)(i),(e)7(i)(A-B), (f)(2)(iii), f(5) – Inadequate Continuing Property Records

CONDITION

AAD obtained and examined the Continuing Property Records (CPRs) to determine whether the Beneficiary maintained its property records with the sufficient detail required by FCC rules.[13] The Beneficiary's Cable and Wire Facility (CWF) property records did not contain the assets' location, totaled $48,950,082. The inadequacy of the property records does not allow for an accurate assessment of the Telephone Plant in Service (TPIS) at the time of the audit. This lack of detail will not allow for the accurate accounting of future CWF plant additions or retirements. Because the Beneficiary did not include sufficient detail required by FCC rules, AAD concludes that the CPRs were inadequate.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring the level of detail to include the CPR as required by FCC rules. The Beneficiary informed AAD that this issue occurred because the Beneficiary's Cable and Wire Facility CPR program was only able to produce a summary of size and gauge by vintage year, even though, the Beneficiary asserts that it has all supporting documentation for Cable and Wire Facilities by exchange.[14]

EFFECT

Because the Beneficiary maintained the detail, albeit separately, to properly account for each asset, AAD will not calculate a monetary effect from this finding. AAD was able to perform alternative procedures using the CPR to select assets for testing to validate the assets were in service and that proper plant amounts were included in the 2014 cost study and reviewed work orders detail to verify asset location and existence. However, detailed property records are an essential component of acquiring and retiring assets when removed from service, or transferring assets among locations. While there is no monetary impact of this finding, AAD notes that the failure to maintain property records that can be physically verified with sufficient detail to accurately account for retirements increases the probability for errors in future High Cost filings.

RECOMMENDATION

AAD recommends that the Beneficiary maintain its CPRs in compliance with FCC Rules. The Beneficiary must implement an adequate system to maintain property records with the level of detail compliant with the FCC's Part 32 rules. The Beneficiary must implement policies and procedures, which will strengthen internal controls surrounding the process of reconciliation and actualization of its continuing property records by utilizing information available to recreate historical records for the assets, and where applicable, use estimates and maintain documentation of such estimates, for assets that are missing from the CPR. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website

[13] *See* Finding #7 for further details.

[14] Beneficiary responses to audit inquiries, received Oct. 12, 2018.

at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #7: 47 C.F.R. §32.2000(e)7(i)(B), (f)(2)(iii), f(5) – Improper Continuing Property Records

CONDITION

AAD obtained and examined the Beneficiary's Continuing Property Records (CPR) and selected a non-statistical sample of five Central Office Equipment (COE) assets to determine whether the Beneficiary properly recorded and reported its assets for High Cost Program purposes. AAD noted that one sampled COE asset, totaling $10,479, consisted of miscellaneous labor and overhead charges with no associated property. AAD expanded the scope of work to include a review of other COE assets in the Beneficiary's CPR and noted 73 additional COE asset line items without a property component. AAD identified the value of these 74 assets transactions, including its associated depreciation expense and accumulated depreciation accounts, as summarized below.

Account Description	Value of Assets Without Property Component	Overstated Accumulated Depreciation	Overstated Depreciation Expense
COE – Switching (Acct. 2210)	$87,675	$41,102	$41,102
COE – Transmission (Acct. 2230)	$12,725	$9,659	$9,659
Total	**$100,400**	**$50,761**	**$50,761**

AAD determined that the Beneficiary's COE property records lacked sufficient detail, specifically a physical location or address, for the auditors to verify the property by physical examination of the assets recorded. Additionally, this lack of detail will not allow for the accurate accounting of future COE retirements. Because the Beneficiary's CPR lacked sufficient detail, AAD concludes that the Beneficiary did not properly maintain CPR for COE and the Beneficiary did not properly record and report accurate COE balances.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring the level of data to include in the CPR as required by FCC Rules. The Beneficiary informed AAD that it should have added these amounts to the asset line for the material, even though, the Beneficiary asserts that the total amount in both the general ledger and the CPR's is correct.[15]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the assets without a property component as reported by the Beneficiary in its respective account in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
ICLS	($1,226)

RECOMMENDATION

The Beneficiary must implement an adequate system to maintain property records with the level of detail required by FCC rules. The Beneficiary's system to maintain property records must include updated policies and procedures, strengthening internal controls surrounding the process of CPR assets recording, and a training program that addresses assigning miscellaneous labor and overhead costs to the related asset line in the CPR records. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> The Company points out that monetary effect is in favor of the Company. The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #8: 47 C.F.R. § 64.901(b) – Improper Inclusion of Non-Regulated Asset

CONDITION

AAD obtained and examined the general ledger, Continuing Property Records (CPRs), and cost study balances to determine whether the Beneficiary reported accurate asset balances, including a non-statistical sample of 48 assets totaling $1,252,528, for High Cost Program purposes. AAD examined the supporting documentation and noted that the Beneficiary had not removed from the Central Office Equipment (COE) asset balance one asset, totaling $69,611, was for non-regulated equipment (voicemail).[16] AAD expanded its examination of the

[15] Beneficiary responses to audit inquiries, received Jan. 3, 2020.
[16] 32 V.S.A. § 9701 (19)(H),(42) (2016).

Beneficiary's CPRs and found additional voicemail equipment for the same amount. The total value of the non-regulated equipment in the CPRs was $139,222. AAD identified the value of this type of equipment including its associated depreciation expense and accumulated depreciation accounts, as summarized below.

Account Description	Non-Regulated Asset Value	Overstated Accumulated Depreciation	Overstated Depreciation Expense
Central Office – Switching (Acct. 2210)	$139,222	$15,454	$103,024

When AAD inquired of the Beneficiary as to why this Finding occurred, the Beneficiary stated that the transactions were a mistake that were later corrected. However, AAD re-examined the general ledger, Part 64 Cost Study adjustments, and the Power and Common Allocation in 2014 and could not identify the correcting journal entries or any adjustments that were related to the two voicemail equipment assets. The journal entries that the Beneficiary provided to AAD were dated in 2008 and, therefore, were not related to this Finding. Thus, because the Beneficiary did not provide evidence that the two non-regulated assets were properly recorded as non-regulated assets, AAD concludes that the Beneficiary did not report accurate asset balances.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to ensure that non-regulated costs are excluded from the account balances before those balances are reported for High Cost Program purposes. The Beneficiary informed AAD that this issue occurred because the Beneficiary erroneously booked the voicemail investment to the regulated asset, the mistake was caught in the same year, and a journal entry was made to correct the mistake to allocate it to a non-regulated account. The Beneficiary provided information to AAD on January 22, 2019 to demonstrate that the amount removed the amount for the voicemail from the general ledger but the journal entry was from 2008.[17]

EFFECT

AAD calculated the monetary effect for this finding by subtracting the recorded value of the asset in the general ledger for the year from the total amount reported by the Beneficiary in its respective accounts on the High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
ICLS	($1,637)

RECOMMENDATION

The Beneficiary must implement policies and procedures to ensure it has an adequate system, strengthening internal controls surrounding the process of reporting accurate data for High Cost Program purposes and

[17] Beneficiary responses to audit inquiries, received Jan. 3, 2020.

maintaining documentation to demonstrate compliance with FCC Rules. The Beneficiary must also update its policies and procedures to include the proper treatment of correcting journal entries that are included within the general ledger. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

The Company points out that monetary effect is in favor of the Company. The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #9: 47 C.F.R. § 54.903(a)(4) – Inaccurate Subscriber Line Charge Revenue

CONDITION

AAD obtained and examined the Beneficiary's general ledger to determine whether the Beneficiary reported accurate Subscriber Line Charge (SLC) Revenues for High Cost Program purposes. The end-user SLC Revenues the Beneficiary reported on its FCC Form 509 did not agree to the Beneficiary's general ledger. The Beneficiary overstated its Residential/Single Line Business (Res/SLB) Revenues and understated its Multi-Line Business Line revenue, as detailed below.

Revenues	As Reported	Per General Leger	Difference
Res/SLB SLC Revenues	$1,155,356	$1,153,234	($2,122)
MLB SLC Revenues	$211,476	$211,564	$88
Total	**$1,366,832**	**$1,364,798**	**($2,034)**

Because the Beneficiary did not provide supporting documentation that agrees to what it reported, AAD concludes that the Beneficiary did not report accurate Subscriber Line Charge (SLC) Revenues.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to report accurate revenues. The Beneficiary informed AAD that this issue occurred because some adjustments such as write-offs and write-off payments were posted multiple times at the end of the month, after the revenues were reported to NECA. These adjustments were missed in the true-up process.[18]

[18] Beneficiary responses to audit inquiries, received Oct. 12, 2018.

EFFECT

AAD calculated the monetary effect for this finding by adding the net understated value of the end-user SLC Revenue to the total amount reported by the Beneficiary in the respective accounts in its High Cost filing. AAD summarized the results below:

Support Type	Monetary Effect
ICLS	($1,993)

RECOMMENDATION

The Beneficiary must implement an adequate system to collect and report accurate end-user revenues and maintain documentation to demonstrate compliance with FCC Rules. Further, the Beneficiary must implement policies and procedures, which will strengthen internal controls surrounding the process of reporting end-user revenue amounts for High Cost Program purposes. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/.

BENEFICIARY RESPONSE

> The Company points out that monetary effect is in favor of the Company. The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

Finding #10: 47 C.F.R. § 32.2000(g)(2) – Inaccurate Depreciation Expense and Accumulated Depreciation Calculation

CONDITION

AAD obtained and examined the Beneficiary's depreciation, accumulated depreciation and related expense schedules to determine whether the Beneficiary properly calculated depreciation expense (DE) and accumulated depreciation (AD). The Beneficiary did not calculate its depreciation using the average monthly asset balance as required by FCC Rules. The Beneficiary made manual adjustments to its calculation to reduce the depreciable balances for items that were determined to be fully depreciated but were not retired. As a result, monthly depreciation was not calculated using the average of the monthly beginning and ending asset balances. AAD recalculated the Beneficiary's depreciation using the average of the beginning and ending balance of each month. The Beneficiary understated its depreciation expense and accumulated depreciation in its High Cost Program (HCP) filings by a total of $741,166, as detailed below.

Depreciation Expense (DE)

Account Description	Part 64 Cost Study As Reported (A)	Part 64 Cost Study Recalculated (B)	Variance Overstated/ (Understated) (A – B)
6560 (2110) – DE (General Support)	$340,316	$624,727	($284,411)
6560 (2210) – DE (COE Switching)	$154,118	$600,275	($446,157)
6560 (2230) – DE (COE Transmission)	$1,149,834	$1,155,273	($5,439)
6560 (2410) – DE (CWF)	$2,141,658	$2,146,817	($5,159)
Total	**$3,785,926**	**$4,527,092**	**($741,166)**

Accumulated Depreciation (AD)

Account Description	Part 64 Cost Study As Reported (A)	Part 64 Cost Study Recalculated (B)	Variance Overstated/(Understated) (A – B)
3100 (2110) – AD (General Support)	$5,513,499	$5,797,910	($284,411)
3100 (2210) – AD (COE Switching)	$4,887,975	$5,334,132	($466,157)
3100 (2230) – AD (COE Transmission)	$9,326,916	$9,332,355	($5,439)
3100 (2410) – AD (CWF)	$35,349,886	$35,355,045	($5,159)
Total	**$55,078,276**	**$55,819,442**	**($741,166)**

Because the Beneficiary did not calculate depreciation using the average monthly asset balance, AAD concludes that the Beneficiary did not properly calculate DE and the associated AD.

CAUSE

The Beneficiary did not have an adequate system in place for collecting, reporting, and monitoring data to correctly calculate depreciation and accumulated depreciation. The Beneficiary informed AAD that this issue occurred because it utilized some sub-accounts as being completely depreciated to prevent additions from being fully depreciated in the same year that it was acquired.[19]

EFFECT

AAD calculated the monetary effect for this finding by adding the understated value of the depreciation expense and accumulated depreciation to the total amount reported by the Beneficiary in the respective accounts it its High Cost filing. AAD summarized the results below:

[19] Beneficiary responses to audit inquiries, received Jan. 3, 2020.

Support Type	Monetary Effect
ICLS	($45,437)

RECOMMENDATION

The Beneficiary must implement an adequate system to properly calculate depreciation expense and accumulated depreciation reported for High Cost Program purposes. The Beneficiary must update its system to ensure the proper calculation of depreciation expense as required by FCC rules. Further, the Beneficiary must implement policies and procedures, strengthening internal controls surrounding the process of calculating and reporting depreciation expense and accumulated depreciation amounts for High Cost Program purposes, including ensuring all cost study adjustments are accurate, and properly supported by documentation. In addition, the Beneficiary can learn more about documentation and reporting requirements on USAC's website at http://www.usac.org/about/about/program-integrity/findings/common-audit-hc.aspx.

BENEFICIARY RESPONSE

The Company points out that monetary effect is in favor of the Company. The Company elects to pass on the opportunity to provide a detailed response or to verify the calculation of the monetary effects. In doing so, the Company does not express judgement on the validity of the finding. Recommendations for the Company have been noted and implemented.

CRITERIA

Finding	Criteria	Description
#1, 2, 4	47 C.F.R. § 54.320(b) (2014)	"All eligible telecommunications carriers shall retain all records required to demonstrate to auditors that the support received was consistent with the universal service high-cost program rules. This documentation must be maintained for at least ten years from the receipt of funding. All such documents shall be made available upon request to the Commission and any of its Bureaus or Offices, the Administrator, and their respective auditors."

Finding	Criteria	Description
#3	47 C.F.R. § 54.7(a) (2014).	"A carrier that receives federal universal service support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."
#3	47 U.S.C.§ 254 (e)(2014).	"After the date on which Commission regulations implementing this section take effect, only an eligible telecommunications carrier designated under section 214(e) of this title shall be eligible to receive specific Federal universal service support. A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Any such support should be explicit and sufficient to achieve the purposes of this section."
#3	*FCC Reminds ETCS of High-Cost Support Requirements* Public Notice, 30 FCC Rcd 11821 (15) (released Oct. 19, 2015)	"Under federal law, high-cost support provided to an ETC must be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. The following is a non-exhaustive list of expenditures that are not necessary to the provision of supported services and therefore may not be recovered through universal service support: • Personal travel; • Entertainment; • Alcohol; • Food, including but not limited to meals to celebrate personal events, such as weddings, births, or retirements; • Political contributions; • Charitable donations; • Scholarships; • Penalties or fines for statutory or regulatory violations; • Penalties or fees for any late payments on debt, loans or other payments • Membership fees and dues in clubs and organizations; • Sponsorships of conferences or community events; • Gifts to employees; and • Personal expenses of employees, board members, family members of employees and board members, contractors, or any other individuals affiliated with the ETC, including but not limited to personal expenses for housing, such as rent or mortgages."
#3	FCC 18-29 Report and Order, Third Order on Reconsideration, and Notice of Proposed Rulemaking	"In this Report and Order, we adopt reforms to ensure that high-cost universal service support provided to eligible telecommunications carriers (ETCs) is used only for the provision, maintenance, and upgrading of facilities and services for which the high-cost support is intended pursuant to section 254(e) of the Act. We also adopt reforms to ensure that the investments and expenses that rate-of-return carriers recover through interstate rates are reasonable pursuant to section 201(b) of the Act. Our findings here do not prevent rate-of-return carriers from incurring any particular investment or expense, but simply clarify the extent to which investments and expenses may be recovered through federal high-cost support and interstate rates.

Finding	Criteria	Description
		The rules we adopt are prospective but the underlying obligations are preexisting and many of the rules we adopt today codify existing precedent. Our rules and the used and useful standard have long governed ETCs and rate-of-return carriers' behavior. Nothing we do in this Report and Order is intended to undermine our precedent."
#5	47 C.F.R. § 54.903 (a) (1) (2014).	"Each rate-of-return carrier shall submit to the Administrator on March 31 of each year the number of lines it served as of the prior December 31, within each rate-of-return carrier study area showing residential and single-line business line counts, multi-line business line counts, and consumer broadband-only line counts separately. For purposes of this report, and for purposes of computing support under this subpart, the residential and single-line business class lines reported include lines assessed the residential and single-line business End User Common Line charge pursuant to § 69.104 of this chapter, the multi-line business class lines reported include lines assessed the multi-line business End User Common Line charge pursuant to § 69.104 of this chapter, and consumer broadband-only lines reported include lines assessed the Consumer Broadband-only Loop rate charged pursuant to § 69.132 of this chapter or provided on a detariffed basis. For purposes of this report, and for purposes of computing support under this subpart, lines served using resale of the rate-of-return local exchange carrier's service pursuant to section 251(c)(4) of the Communications Act of 1934, as amended, shall be considered lines served by the rate-of-return carrier only and must be reported accordingly."
#5	47 C.F.R. § 69.104(h) (2014).	"(h) A line shall be deemed to be a single line business line if the subscriber pays a rate that is not described as a residential rate in the local exchange service tariff and does not obtain more than one such line from a particular telephone company."
#6, 7	47 C.F.R. § 32.2000(e)(1)(i),(e)7(i)(A-B), (f)(2)(iii), f(5)(2014).	"(e) *Basic property records.* (1) The basic property records are that portion of the total property accounting system which preserves the following detailed information: (i) The identity, vintage, location and original cost of units of property…….. (7)(i) The continuing property records shall be compiled on the basis of original cost (or other book cost consistent with this system of accounts). The continuing property records shall be maintained as prescribed in §32.2000(f)(2)(iii) of this subpart in such manner as will meet the following basic objectives: (A) Provide for the verification of property record units by physical examination. (B) Provide for accurate accounting for retirements……. (f) *Standard practices for establishing and maintaining continuing property records*—

Finding	Criteria	Description
		(2) *Property record units.* (iii) The continuing property record shall reveal the description, location, date of placement, the essential details of construction, and the original cost (note also paragraph (f)(3) of this section) of the property record units. The continuing property records shall be compiled on the basis of original cost (or other book cost consistent with this system of accounts) and maintained in such manner as will provide for the verification of property record units by physical examination. The continuing property record and other underlying records of construction costs shall be so maintained that, upon retirement of one or more retirement units or of minor items without replacement when not included in the costs of retirement units, the actual cost or a reasonably accurate estimate of the cost of the plant retired can be determined……. (5) *Identification of property record units.* There shall be shown in the continuing property record or in record supplements thereof, a complete description of the property records units in such detail as to identify such units. The description shall include the identification of the work order under which constructed, the year of installation (unless not determinable per §32.2000(f)(4) of this subpart, specific location of the property within each accounting area in such manner that it can be readily spot-checked for proof of physical existence, the accounting company's number or designation, and any other description used in connection with the determination of the original cost.”
#8	47 C.F.R. § 64.901(a), (b) (2014).	“(a) Carriers required to separate their regulated costs from nonregulated costs shall use the attributable cost method of cost allocation for such purpose. (b) In assigning or allocating costs to regulated and nonregulated activities, carriers shall follow the principles described herein. (1)Tariffed services provided to a nonregulated activity will be charged to the nonregulated activity at the tariffed rates and credited to the regulated revenue account for that service. Nontariffed services, offered pursuant to a section 252(e) agreement, provided to a nonregulated activity will be charged to the nonregulated activity at the amount set forth in the applicable interconnection agreement approved by a state commission pursuant to section 252(e) and credited to the regulated revenue account for that service. (2) Costs shall be directly assigned to either regulated or nonregulated activities whenever possible…..”
#8	32 V.S.A. § 9701 (19)(H),(42) (2014).	“(19) “Telecommunications service" means the electronic transmission, conveyance, or routing of voice, data, audio, video, or any other information or signals to a point, or between or among points. The term "telecommunications service" includes such transmission, conveyance, or routing in which computer processing

Finding	Criteria	Description
		applications are used to act on the form, code, or protocol of the content for purposes of transmission, conveyance, or routing without regard to whether such service is referred to as voice-over internet protocol services or is classified by the Federal Communications Commission as enhanced or value added. Telecommunications service does not include: (H) Ancillary services. (42) "Ancillary services" means services that are associated with or incidental to the provision of telecommunications services, including detailed telecommunications billing, directory assistance, vertical service, and voice mail services."
#9	47 C.F.R. § 54.903(a)(4) (2014).	" a) To be eligible for Interstate Common Line Support, each rate-of return carrier shall make the following filings with the Administrator… (4) Each rate-of-return carrier shall submit to the Administrator on December 31st of each year the data necessary to calculate a carrier's Interstate Common Line Support, including common line cost and revenue data, for the prior calendar year. Such data shall be used by the Administrator to make adjustments to monthly per-line Interstate Common Line Support amounts in the final two quarters of the following calendar year to the extent of any differences between the carrier's ICLS received based on projected common line cost and revenue data and the ICLS for which the carrier is ultimately eligible based on its actual common line cost and revenue data during the relevant period. The data shall be accompanied by a certification that the cost data is compliant with the Commission's cost allocation rules and does not reflect duplicative assignment of costs to the consumer broadband-only loop and special access categories."
#10	47 C.F.R. § 32.2000(g)(2) (2014).	(g) *Depreciation accounting* (2) *Depreciation charges.* (i) A separate annual percentage rate for each depreciation category of telecommunications plant shall be used in computing depreciation charges. (ii) Companies, upon receiving prior approval from this Commission, or, upon prescription by this Commission, shall apply such depreciation rate, except where provisions of paragraph (g)(2)(iv) of this section apply, as will ratably distribute on a straight line basis the difference between the net book cost of a class or subclass of plant and its estimated net salvage during the known or estimated remaining service life of the plant. (iii) Charges for currently accruing depreciation shall be made monthly to the appropriate depreciation accounts, and corresponding credits shall be made to the appropriate depreciation reserve accounts. Current monthly charges shall normally be computed by the application of one-twelfth of the annual depreciation rate to the monthly average balance of the associated category of plant. The

Finding	Criteria	Description
		average monthly balance shall be computed using the balance as of the first and last days of the current month. (iv) In certain circumstances and upon prior approval of this Commission, monthly charges may be determined in total or in part through the use of other methods whereby selected plant balances or portions thereof are ratably distributed over periods prescribed by this Commission. Such circumstances could include but not be limited to factors such as the existence of reserve deficiencies or surpluses, types of plant that will be completely retired in the near future, and changes in the accounting for plant. Where alternative methods have been used in accordance with this subparagraph, such amounts shall be applied separately or in combination with rates determined in accordance with paragraph (g)(2)(ii) of this section.”

This concludes the report.