

APPENDIX

USAC February 28, 2008 Letter



February 28, 2008

VIA E-MAIL AND FIRST-CLASS MAIL

Anthony Dale
Managing Director
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: Suggested Additional Steps to Reduce or Prevent Improper USF Payments

Dear Mr. Dale:

This letter responds to your January 29, 2008, letter regarding the Federal Communications Commission (FCC or Commission) Office of Inspector General (OIG) Universal Service Fund (USF) audit program for 2006-2007. Your January 29 letter required the Universal Service Administrative Company (USAC) to furnish additional information regarding measures to mitigate improper USF payments as a follow-up to USAC's *Report on the Federal Communications Commission Office of Inspector General 2006-07 Universal Service Fund Audit Program*, submitted to the Commission at your direction on December 31, 2007 (USAC December 31 Report). Your January 29 letter directed USAC to "provide a specific list of proposed additional steps that USAC proposes to take to prevent or reduce potential improper payments and the additional resources needed to implement such measures."

USAC is pleased to submit this letter in fulfillment of the Commission's requirement for more information about proposed additional steps to mitigate improper payments. As emphasized in the USAC December 31 Report, USAC is committed to understanding the nature and causes of improper USF payments and implementing further measures to prevent or reduce them. The additional steps discussed below build on a firm foundation of processes, systems, procedures, and outreach activities that USAC has developed since its creation in 1997. The additional steps suggested herein to assist in prevention or reduction of improper payments, several of which were identified in the USAC December 31 Report, encompass all areas of USAC operations and USF program activity, including USF contributor payments, High Cost, Low Income, Rural Health Care, and Schools and Libraries.

The proposals in this letter are divided into four categories as suggested in your January 29 letter: additional oversight and managerial controls, strengthened audit or

investigative techniques, improved information technology tools, and more effective use of outreach resources. The descriptions below provide resource estimates to the extent and level of precision possible at this time. For several proposals discussed below, it is difficult to assess resource needs precisely without further development. In addition, implementation of certain suggestions depends on systems development efforts that have not yet been fully defined and on actions that may require approval for procurement of goods and services pursuant to the FCC-USAC Memorandum of Understanding. USAC anticipates that additional discussions with Commission staff as contemplated in your January 29 letter, as well as further input from the USAC Board of Directors, will clarify the suggestions that are deemed to have the most merit.

ADDITIONAL OVERSIGHT AND MANAGERIAL CONTROLS

USAC continually works to improve its oversight and management of the USF programs. The additional steps presented below represent enhancements and extensions to the scope and structure of USAC's existing portfolio of oversight and managerial controls designed to reduce or prevent improper payments.

Internal Controls

1. Assessment and Modification of USAC Internal Controls Program. To complement the annual audit of USAC's procedures required pursuant to 47 C.F.R. Part 54, and consistent with the FCC-USAC Memorandum of Understanding, USAC recently obtained approval to acquire services to assist USAC in assessing its existing extensive internal controls framework. This project is designed to bring USAC into full conformance with best practices consistent with the internal controls process defined in OMB Circular A-123. The contractor will identify all significant business processes and review controls over all transactions within these processes, including portions of the payment process currently performed by program support services contractors. The contractor will perform a risk analysis to identify significant risks in USAC's business processes, test all key controls, and complete a gap analysis, which will identify any necessary modifications of USAC's current internal controls system. This effort will be directed by the USAC Senior Manager of Internal Controls, a recently created position. The internal controls assessment will enable USAC to develop and implement corrective action plans for any identified internal control weaknesses to prevent or reduce improper payments. Based on further consultation with Commission staff and the USAC Board of Directors, this action plan may involve retaining consultants or other experts to assist in developing and/or documenting new or revised internal controls and/or to review other aspects of USAC's operations to ensure efficient and effective administration of the USF.

- Resource Estimate: \$1,300,000 in contractor services for first phase; TBD for corrective action phase

Data Gathering and Validation

1. Enhanced Data Gathering and Analysis. USAC proposes working with the Commission to gather data to add oversight and management capabilities that do not currently exist due to the unavailability of certain data. USAC respectfully suggests the Commission consider working with USAC to provide access to such data to the extent the Commission deems appropriate.

a. High Cost Program: USAC proposes working with the Commission to ensure that FCC Form 498 collects Study Area Code (SAC) information for High Cost Program beneficiaries. Obtaining SAC data would ensure that the proper Service Provider Identification Number and SAC mapping data are available for automated feed into USAC's information technology systems. This linkage would result in greater administrative efficiency and could assist in preventing improper payments to the wrong service provider. Modification of FCC Form 498 would be required to implement this proposal.

- Resource Estimate: No additional resources required

b. High Cost Program: USAC suggests the Commission consider authorizing USAC to receive cost study data and other documentation supporting annual filings and quarterly revisions filed by carriers with the National Exchange Carrier Association, Inc. (NECA) pursuant to 47 C.F.R. Part 36. USAC does not seek to assume Part 36 data collection or associated administrative responsibilities, but respectfully suggests that it be authorized to receive copies of underlying data submitted by carriers to NECA that is used in USF support calculations. USAC access to this information would enable data review and verification that cannot be performed today by USAC. For example, under current rules, NECA performs calculations on data submitted by carriers and transmits the results to USAC to be used as the basis for High Cost Loop support payments. USAC does not have access to the underlying cost study data collected by NECA. Access to this data could enable USAC to perform validation checks to better identify potential anomalies and prevent improper payments.

- Resource Estimate: 1 FTE; \$250,000 in IT development and deployment

c. Low Income Program: USAC suggests the Commission consider requiring Eligible Telecommunications Carriers (ETCs) to provide certain additional documentation in support of claims for Low Income Program support. Modification of FCC Form 497 would be required to implement this proposal. Such data could include the following:

- i. All ETCs claiming Lifeline, Link Up or Toll Limitation Service (TLS) support would submit subscriber listings to validate the number of

subscribers claimed for each type of support. For example, an ETC that claimed 1,284 Lifeline subscribers in a particular month would provide a list of 1,284 subscribers that received service in that month. Gathering this information would enable USAC to ensure it does not pay support for subscribers that did not receive discounts.

ii. Incumbent ETCs that resell Lifeline service to an ETC would provide a list of resold accounts. This would enable USAC to ensure that the incumbent ETC and the competitive ETC are not claiming support for the same consumers.

iii. All ETCs would be required to provide proof of the rates upon which support claims are based. For example, ETCs would be required to submit evidence of their End-User Common Line (EUCL) charge (or, in the case of competitive ETCs, the EUCL of the incumbent in the area served) so that USAC can validate Lifeline Tier 1 support claims. Gathering this information will further ensure that USAC pays the correct rate for Tier 1 support, thus preventing improper payments.

- Resource Estimate: 3 FTEs; \$100,000 in IT development and deployment

2. Children's Internet Protection Act Validation. USAC proposes gathering additional information as part of its review processes to assess compliance with the Children's Internet Protection Act (CIPA). Violations in this area identified in the 2006-07 FCC OIG audits largely resulted from beneficiaries failing to enunciate explicit Internet safety policies rather than the absence of installed filtering technologies. See USAC December 31 Report at 55. To date, USAC's review of CIPA compliance has focused on the primary CIPA requirements such as having filtering technology in place. To address the results of the 2006-07 FCC OIG audits, USAC proposes to strengthen review in this area by verifying that applicants are fully complying with Internet safety policy requirements. This change, coupled with outreach on these issues, should help reduce the number of CIPA violations that resulted in identification of improper payments.

- Resource Estimate: 1 FTE; \$100,000 in IT development and deployment

STRENGTHENED AUDIT OR INVESTIGATIVE TECHNIQUES

USAC has long recognized that audits serve a fundamental role in administering the USF with efficiency and integrity and are essential in identifying areas that may require further investigation. The additional steps presented below address audit techniques and augmentations to the current FCC OIG audit program and other audit activities conducted by USAC. In addition, the information technology activities described below will have a positive impact on audit and investigative activities.

1. Alternative Procedures and Performance Audits. Where warranted, USAC proposes to use alternative procedures and/or performance audits to reduce the number of disclaimed and qualified opinions and to provide specific amounts subject to recovery. Depending on the circumstances, USF beneficiary and contributor audits requiring expanded audit procedures could benefit from using a GAGAS-compliant performance audit methodology. This contingency could address, for example, instances in which auditors were unable to reach a conclusion or calculate improper payments to support a compliance attestation examination due to a lack of documentation or for other reasons.

- Resource Estimate: TBD based on number and complexity of audits requiring use of alternative procedures and/or performance audits. As audits requiring such work are identified, USAC will assess the resources required.

2. High Cost and Low Income Programs Follow-Up Audit Activities. At this time, beneficiary audits generally review support disbursed during a specific time period USAC proposes expanding audit activity to include follow-up audits when an initial audit suggests activity that may have occurred in time periods not subject to audit warrants examination.

- Resource Estimate: 2-4 FTEs

3. Enhanced Schools and Libraries Program Service Provider Audit Program. Several audit findings were based on weak internal controls on the part of service providers. See USAC December 31 Report at 51, 57. USAC recommends dedicating audit resources to performing targeted audits of Schools and Libraries Program service providers that would be triggered by appropriate risk-based criteria.

- Resource Estimate: 2 FTEs

DEPLOYING IMPROVED INFORMATION TECHNOLOGY TOOLS

Sophisticated, robust information technology (IT) tools play uniquely important, widely varied roles in efforts to reduce or prevent improper payments. USAC has developed a strategy to augment current IT capabilities directed at enhancing efficiency, ensuring program compliance, and preventing improper payments. Many of the proposed activities discussed elsewhere in this report will benefit from deployment of the enhanced IT tools discussed in this section.

1. Systems Modernization. A proposed sequence of systems modernization and data warehousing projects will enable USAC to identify areas of USF program participant activity that warrant targeted verification or review of documentation and transaction details as well as appropriate follow-up activity. Updated IT systems will provide a more

robust, flexible infrastructure to support all aspects of USAC operations. These enhancements will be accomplished through the ongoing High Cost and Low Income Programs systems enhancement effort, USAC's financial systems modernization (FSM) project, and the systems modernization component of the IT services contract for the Rural Health Care and Schools and Libraries Programs. Deployment of the High Cost and Low Income Program systems is scheduled to occur in early 2009. FSM activities will occur in 2009 and 2010, with deployment planned for late 2010. The Rural Health Care and Schools and Libraries Program systems modernization work will take place in 2009 and 2010, with deployment planned for 2011. These projects will help prevent or reduce improper payments by providing modernized systems and normalized data structures that will bring greater efficiency and consistency to application processing, invoice payment, recordkeeping, booking expenditures, data analysis, performance measurement, and reporting.

- Resource Estimate: 4 FTEs; \$3,700,000 for High Cost and Low Income, \$4,600,000 for FSM, TBD for Rural Health Care and Schools and Libraries

2. Enhanced Data Reporting and Analysis. The systems modernization efforts described above will allow USAC to expand its data analysis capabilities by enabling creation of a data warehouse. USAC plans to begin development of such a data warehouse populated with data from production systems which initially will serve as the basis for a robust reporting environment. As the universe of data is expanded, USAC proposes to "mine" this data with sophisticated analysis techniques. This capability would be similar to methods used by credit card companies and financial institutions to identify potentially problematic transactions. For example, with more sophisticated systems, instances of large fluctuations in reported revenues by USF contributors will be more readily susceptible to detection at a greater degree of granularity earlier in the process, thus better facilitating review and investigation where warranted. In addition, enhanced data reporting capability will improve USAC's ability to measure and analyze its performance. Pursuant to Commission order and the FCC-USAC Memorandum of Understanding,¹ USAC currently reports on program administration, providing more than 250 pages of performance data to the Commission on a quarterly basis. The systems enhancements described here and above will allow for more sophisticated enterprise-wide performance reporting.

- Resource Estimate: 2-3 FTEs; \$1,000,000 in IT development

3. Online Portals. USAC proposes expanding the use of secure online portals by participants in each of the USF programs as well as contributors. Such portals allow for

¹ See In the Matter of Comprehensive Review of the Universal Service Fund Management, Administration, and Oversight, WC Docket No. 05-195, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Schools and Libraries Universal Service Support Mechanism, CC Docket No. 02-6, Rural Health Care Support Mechanism, WC Docket No. 02-60, Lifeline and Link-Up, WC Docket No. 03-109, Changes to the Board of Directors for the National Exchange Carrier Association, Inc., CC Docket No. 97-21 ¶¶ 34-75 (rel. August 29, 2007); FCC-USAC Memorandum of Understanding, Attachment C.

documents to be uploaded electronically and stored for future review and retrieval and will also provide an enhanced platform for online certifications. Such portals will reduce errors in information submissions. An online document storage and retrieval capability will facilitate improved record retention practices, thus addressing a major cause of audit findings and improper payments.

- Resource Estimate: 3 FTEs

4. Consolidated Post-Audit Tracking System. USAC has initiated development of a consolidated post-audit tracking system to collect and aggregate audit information to provide USAC with enhanced tracking and reporting. This capability will provide greater transparency, facilitate cross-division tracking and response to audit issues, and help provide increased outreach support, thus assisting in prevention of improper payments.

- Resource Estimate: 2 contractor FTEs; \$400,000 in IT development

MORE EFFECTIVE USE OF OUTREACH RESOURCES

Because participant self-certification is one of the primary means mandated by the Commission to ensure USF program and contributor integrity, effective and comprehensive education and training are vital. USAC has developed a strong outreach and training program, but as stated in the USAC December 31 Report, recognizes the need for more activity in this area. To help beneficiaries change behavior to ensure compliance with the Commission's requirements and prevent improper payments, USAC will refine and expand training and outreach as described below. Enhancements will include not only providing more training and outreach opportunities for program participants, but also ensuring that the training reaches those who need it most and provides participants with the assistance they most need. USAC believes that effort and resources committed to outreach will result in fewer instances of improper payments, funding denials, administrative appeals, and the need to recover funds.

More In-Person Exchanges

1. Site Visit Program. USAC plans to continue enhancements to the site visit program with the objective of focusing more on front-end participant education, training, and outreach. The program will build on the current site visit program to provide substantive, targeted outreach to beneficiaries identified as needing direct support in understanding and complying with USF program rules. Although USAC anticipates continued contractor support in 2009, USAC staff members ultimately should conduct this outreach to ensure the reliability and integrity of the communication.

- Resource Estimate: 10 FTEs; \$1,500,000 in 2009 (contractor expense reduced from approximately \$5,000,000 in 2007); TBD thereafter

2. Training. USAC plans an expanded roster of training sessions for program participants. USAC is planning four joint High Cost and Low Income Program training activities in 2008 that would address best practices for audit compliance, rules compliance, and other program-related education. USAC expects such a training program to be an ongoing activity. In the Rural Health Care Program, USAC plans to implement regular health care provider and service provider training sessions. Building upon the success of the recent Rural Health Care Pilot Program training, these sessions will focus on helping participants understand program requirements. USAC is currently developing training and outreach programs for telecommunications industry stakeholders at industry events and in other exchanges with USF contributors. This training would include guidance on documentation requirements, the audit process, completing FCC Forms 498 and 499, and awareness of and compliance with program rules.

- Resource Estimate: 2 FTEs, \$200,000 per year

Increased Interactive Program Support and Expanded Access to Online Resources

1. Automated Program Instruction. USAC proposes to prepare interactive, self-guided, online "E-learning" modules that provide instruction and user-specific guidance regarding program requirements. The initial phase of the program would consist of developing one module providing general program guidance; broader roll-out would consist of 2-4 modules per program. Program-specific modules would address frequently-cited causes of non-compliance as identified in the 2006-2007 OIG USF audit program and elsewhere for USF contributors and beneficiaries of the High Cost, Low Income, Rural Health Care, and Schools and Libraries Programs.

- Resource Estimate: \$750,000 (15 modules at \$50,000/unit)

2. Increased Portfolio of Internet-based Materials. USAC proposes a series of webinars, interactive online demonstrations, frequently asked questions (FAQs), fact sheets, and training sessions, addressing specific areas of outreach and instruction in various aspects of program compliance. These materials would focus on specific compliance issues and offer participants opportunities to engage in question-and-answer sessions. One example is an interactive tool that prompts users with questions, answers, and actions needed to prepare for an audit. Such materials should focus on major issues discovered in the 2006-07 FCC OIG audits that led to improper payments.

- Resource Estimate: 1 FTE, \$50,000 in IT development
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Mr. Anthony Dale
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USAC recognizes that some proposals discussed above are in the nature of works in progress at this time and will require further development. USAC looks forward to continuing to work closely with the Commission to identify and implement appropriate, effective measures to further safeguard the USF from improper payments and to enhance the efficiency and effectiveness of all aspects USAC's administration of the USF.

Sincerely,

A handwritten signature in black ink, appearing to read 'D. Barash', with a long horizontal line extending to the right.

D. Scott Barash
Acting Chief Executive Officer

cc: Kent R. Nilsson, Inspector General
Dana Shaffer, Wireline Competition Bureau Chief
Mark Stephens, Chief Financial Officer
Mark Stone, Deputy Managing Director
Mindy Ginsburg, Deputy Managing Director
USAC Board of Directors
(all via e-mail only)