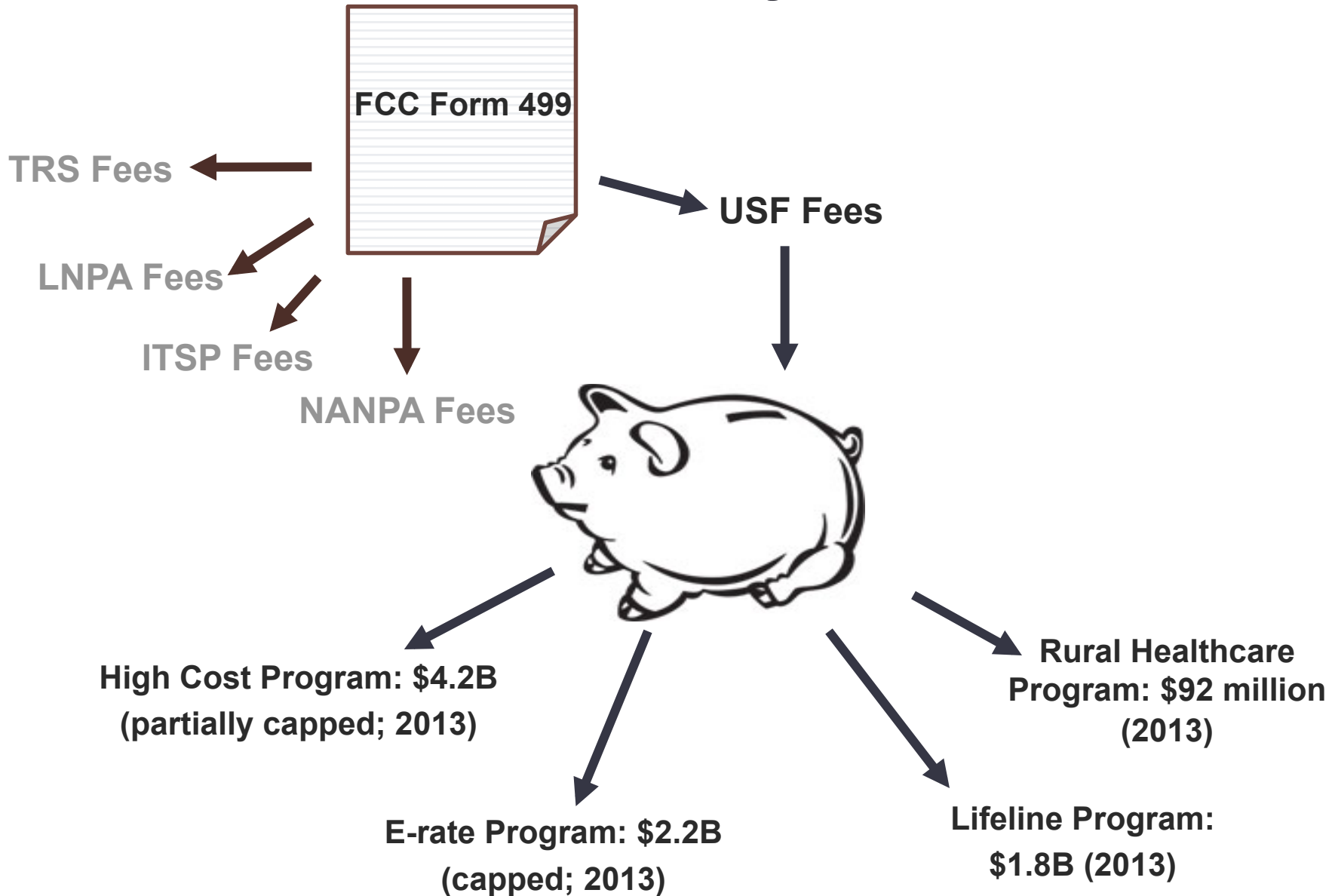


Federal Universal Service System



FCC Forms

- Forms:
 - **FCC Form 499A** (annual report)
 - **FCC Form 499Q** (quarterly report)
 - Forms are used to report revenues to the FCC
 - Reported revenues are the basis for a number of FCC fees:
 - Universal Service Fund (USF)
 - Telephone Relay Service (TRS)
 - Interstate Telecommunications Service Provider (ITSP)
 - North American Numbering Plan Administration (NANPA)
 - Local Number Portability Administration (LNPA)

USF Fee

- **Universal Service Fund**

- Administered by the Universal Service Administrative Company (USAC) (private contractor to FCC)
- Fee is revised quarterly. Current fee is 17.4% of assessable revenues
- Contribution factor is based on projected funds needed for:
 - Connect America Fund (f/k/a High Cost)(capped)
 - Lifeline program
 - E-rate (capped)
 - Healthcare Connect

Other Fees

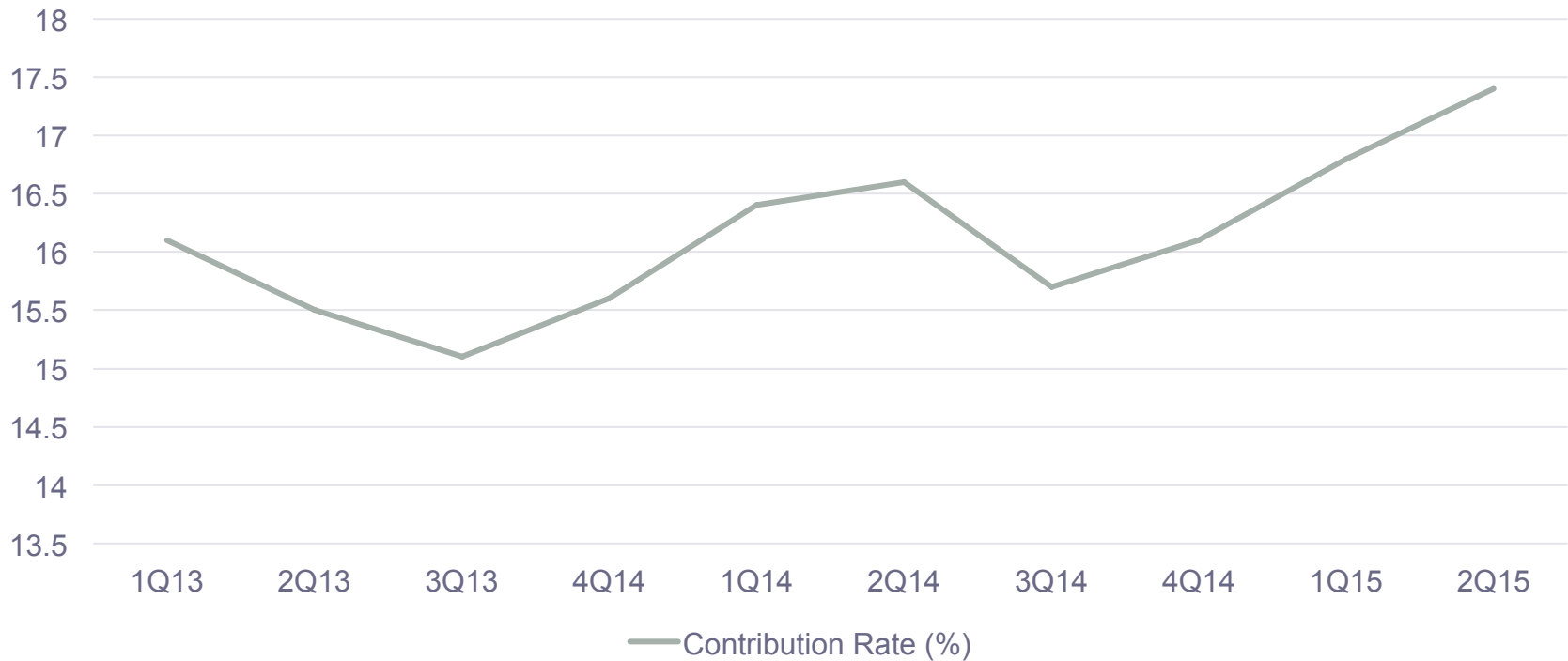
- **Telephone Relay Service (TRS)**
 - Administered by Rolka Loube Saltzer Associates
 - 1.484% of assessable revenues
- **Interstate Telecommunications Service Provider (ITSP)**
 - Administered by the FCC
 - Hovers between 0.346-.375% of assessable revenue
- **North American Numbering Plan Administration (NANPA)**
 - Administered by Welch LLP
 - 0.00302% of assessable revenues
- **Local Number Portability Administration (LNPA)**
 - Currently administered by Neustar; transitioning to Telcordia
 - Low fee (rate not public); minimum of \$100

USF Contribution Basics

- **“Contribution Factor” 2Q 2014:** 17.4% on interstate and international revenues
- **Contributor** = entity that cuts the check to gov’t
 - Paying a line item on your phone bill isn’t “contribution”
- **Contributions** = fees paid by contributor that it MAY choose to recover through line item on bill
- **NOT a tax.** Fee assessed on provider, not end user.
 - Tax jurisdictional rules don’t apply.
- **No mark up on bill:** factor x assessable revenues = max

USF Contribution Rate History

USF Contribution Rates
2012 - Current



USF Contribution Rate High/Low from 2010 through Current

High – 17.9% (1Q12) Low – 12.9% (4Q10)

Note that impact of additional E-Rate funding has not yet been taken into account

USAC Contributions...Changes Ahead?

- Current contribution rate of 17.4% may increase even further.
- Potential sources of increase include:
 - Increased cap on Schools & Libraries (E-rate) Program from \$2.5 Billion to \$3.9 Billion, with inflation escalations
 - Outcome of the FCC's Net Neutrality and USF Contribution Reform proceedings
 - For now, the FCC's position is that the reclassification of broadband service will not make it assessable under USF. However, this could change as a result of the USF contribution proceeding
 - If broadband were to be assessed, the number of services subject to USF fees would increase, but the overall contribution rate would decrease due to the larger pool of assessable revenue
 - Joint Board recommendations to the FCC imminent
 - Potential to change the types of services that are assessed and the way contributions are calculated

Dissecting the FCC Form 499

- “Block 4” (lines 401-423)
 - Default section
 - Jurisdictional breakdown
 - USF fees triggered for interstate/int’l revenues
 - Each line for different service
- “Block 3” (lines 301-315)
 - Reseller revenues go here (plus other types)
 - Fees not assessed, but need to justify with documents!

Assessable Revenues

- Interstate + int'l end user telecom, interconnected VoIP
 - Open Internet Order: no USF fees for now on broadband, but FCC may impose in separate proceeding
- Interconnected VoIP = VoIP services that:
 - enable real-time, two-way voice communications
 - require a broadband connection from the user's location;
 - require IP-compatible customer premises equipment; and
 - permit users to receive calls from and terminate calls to the PSTN (VoIP E911 Order)

Assessable Revenues

- Telecommunications not just voice
 - Point-to-point transport of data is a telecommunications service
- Self-provisioning, government self-provisioning
 - Does NOT mean that governmental customers are exempt—they're not!
 - Sales tax exemption certificates not applicable

USAC BCAP Program

- The Beneficiary and Contributor Audit Program is USAC's relatively new audit program for universal service beneficiaries and contributors.
- The BCAP Program includes the following types of audits
 - Contributor audits
 - High Cost Program audits
 - Lifeline Program audits
 - Rural Health Care Program audits
 - Schools and Libraries Program audits
- BCAP may use either USAC auditors or independent accounting firms.

USAC BCAP Program

- Key points for BCAP audits:
 - BCAP audits are conducted as *performance audits*
 - Audit scope and approach are driven by the organization's size, complexity, and overall revenue assessable for its USF contribution
 - Performance audits are performed in accordance with Generally Accepted Government Auditing Standards (GAGAS or Yellow Book)
 - The objective of GAGAS-conducted BCAP audit is to identify areas of non-compliance with program rules and to calculate how much is owed as a result of any violations

BCAP Program Contributor Audits

- Key points for USF Contributor Audits:
 - Based on revenues reported on Forms 499A and 499Q
 - Process takes around a year, and is very thorough
 - A contribution audit focuses on several topics, including:
 - Completeness of revenue
 - Block 3 reporting
 - Classification of products and services as assessable or non-assessable
 - Jurisdictional allocations
 - USF recovery charges and associated reporting
 - To prepare for an audit, the auditee should gather relevant documentation to provide to the auditors (see Audit Documentation Checklist)

Contributor Audit Checklist



Contributors
Documentation for Auditors Checklist

Completeness of Revenue

Documentation to support the completeness of revenue, such as:

- Audited Financial Statements
- Federal Tax Return

Block 3 Reporting

Documentation to support the accuracy of carrier's carrier revenue classification, such as:

- Listing of Reseller Customers – to include name, filer ID, contact information, revenue amount, reported Form 499-A Line and description of services
- Documentation to support reseller classification, such as, but not limited to, annual reseller certificates, FCC website printout, and/or other supporting documentation in accordance with the FCC Rules and Instructions
- Carrier Access Billing System report
- Universal Service Support Revenue – should include amounts received for the High Cost and Low Income mechanisms from the State and Federal programs

Classification of Products

Documentation to support the classification of products, such as:

- Detailed description of products
- Line classification of products
- Trial Balance
- G/L Detail
- Methodology of Good Faith Estimates, if applicable

Jurisdiction Allocation

Documentation to support the allocation of the jurisdiction, such as:

- Traffic Studies
- Billing System Reports
- Call Detail Records (CDRs)
- Methodology of Good Faith Estimates, if applicable

USF Recovery

Documentation to support the revenue recovered for USF, such as:

- Listing of USF Assessed Products
- Customer Listing
- Customer Invoices
- G/L Detail – to include where State and/or Federal USF is recorded

Other

- External Auditor's Report, including Sarbanes-Oxley Report
- Policies and Procedures regarding USF Recovery, Form 499-A preparation, and Carrier's Carrier Reporting
- Methodology for reporting bad debt
- Supporting documentation for the percentages reported in Lines 503 to 510

Additionally, you should have the following people available to answer questions:

- Person who prepares the Form 499-A
- Person knowledgeable about the billing system(s)
- Person knowledgeable about the products your company offers
- Person knowledgeable about assessing USF to end-users

Scope of USAC Audits

- Scope of information requested by USAC auditors is **broad** and includes:
 - General ledger
 - Services provided
 - Business processes
 - Billing systems
 - Tax systems
- Will review whether *all* revenues reported even if not assessable
- Will review jurisdictional allocation
 - Regulatory and jurisdictional classifications per FCC rules and decisions—not governed by tax law concepts such as **location of activity**.
- Will look for over-collection or under-collection of USF fees from customers
- Auditors request screen shots, examine bills, customer lists, copies of exemption certificates

Claimed Exemptions Will Be Audited

- Exemptions include:
 - Intrastate revenues
 - Revenues from resellers that directly contribute
 - Resellers may pay line item on bill from wholesaler but that doesn't count, it isn't direct contribution
 - LIRE exemption for international revenues
 - Formula

$$\text{If } \frac{\text{Interstate telecom/interconnected VoIP}}{\text{Interstate + international telecom/interconnected VoIP}} \leq 12\% \text{ or less}$$

Must take into account affiliates' revenues

Method of Allocating to Jurisdictional Categories Will Be Audited

Methods for determining interstate vs. intrastate:

- Determined by end-to-end analysis of the entire data stream (not just the portion your company provides, and not just where the facilities lie)
- Booked revenues
- Traffic studies
- Safe harbor
 - 37.1% of mobile telephony revenues
 - 64.9% of interconnected VoIP revenues
- 10% certificates from customers for “private lines,” special access, services whose jurisdictional nature can’t be determined by service provider

10% and Reseller Exemption Certificates

- 10% certificates
 - For services for which jurisdictional allocation cannot be determined by service provider need “10% certificate” from customer attesting that usage is 10% or less interstate
 - Obtain once unless service changes
- Reseller certificates (avoid double “taxation”)
 - Need 2 things:
 1. “reseller certificate” that is renewed each year that is service specific (for revenues Jan 1, 2014 or later)
 2. print out from FCC website showing the customer is a direct USF contributor

USAC Contributor Audit Process

- Contributor audits proceed according to the following framework:
- **Announcement letter**
 - Describes the purpose and scope of the audit, key audit firm personnel, and timing. Also includes an internal control questionnaire and data request
- **Entrance conference**
 - Initial meeting between the auditor and the auditee to discuss audit scope, timing, logistics, and milestones
- **Fieldwork**
 - Typically performed through a combination of offsite and onsite testing
- **Closing Meeting**
 - Auditor provides and overview preliminary audit results based on fieldwork
- **Reporting/Review Process**
 - Auditor conducts management review of its conclusions and USAC review processes
- **Exit Conference**
 - Auditor and auditee discuss formal audit results & report

USAC Contributor Audit Process

- Contribution auditors are responsible for producing two key documents:
 - Performance Audit Report - Narrative-based with findings (monetary effect)
 - Management Letter - Other matters (compliance findings with no or immaterial monetary impact)
- Common findings include:

Lack of documentation to support carrier's carrier (wholesale) revenue reported

Reseller certifications not received on a timely basis, or at all

Services are not reported on the correct lines of FCC Form 499-A

Telecommunications revenue incorrectly reported as non-telecommunications revenue on Line 418 of the FCC Form 499-A

Non-telecommunications revenue incorrectly reported as telecommunications revenue

Justification for unbundled revenue values not documented

Missing documentation to support private line jurisdiction (10% Certificates, Traffic Studies)

Estimates for services and jurisdiction are not properly maintained

Incorrect application of traffic study factors/safe harbor percentages

USF amounts recovered are not correctly reported on the FCC Form 499-A, Line 403

State USF recovery charges on FCC Form 499-A are not properly reported

USAC Contributor Audits – Auditee Guidance

- Best Practices to Minimize Findings

- Study Form 499-A reporting requirements and relevant FCC rules
- Retain appropriate and adequate documentation to support service and jurisdiction reporting
- Maintain documentation to support revenue classification
- Review data for accuracy prior to submission to USAC

- Best Practices to Facilitate a Successful Audit

- Provide requested documentation in a complete and timely manner
- Ask questions to ensure that you are providing adequate documentation
- Work *with* the auditors, not *against* them – explore alternatives where applicable
- Maintain documentation, for five years, for data submitted to USAC/auditor

Common USF Contributor “Red Flags”

- **Operating Environment:**

- New compliance or reporting requirements (especially new regulations).
- High number of disputes, regulatory audits, or inquiries.
- Entry into or exit out of a business or service.
- Recent acquisitions or divestitures, especially if regulatory approval was contingent on certain requirements, or if operating under a transition services agreement.
- Multiple billing systems/revenue cycle control environments

- **Regulatory Reporting Process:**

- Excessive manual adjustments required to complete regulatory reports, or inconsistent revenue reporting processes across affiliates and business units
- Failure to reconcile USF contributions and USF customer surcharges
- Complex large business customer contracts with multiple services provided and nonstandard terms
- Bundling of services and lack of revenue decomposition methodology

Common USF Contributor “Red Flags”

- *Systems and Technology:*

- Multiple/complex IT environments
- Failure to reconcile billing and ERP (general ledger) systems
- Inability to identify affiliate, reseller, and nonregulated revenues in billing and ERP systems
- Inability to measure network usage and traffic

- **Products and Services:**

- Bundled service offerings require unbundling to determine interstate regulated revenues subject to USF assessment
- New services or business models
 - IP-based services
 - Handset subsidies/financing

THANK YOU

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