EX PARTE COMMUNICATION

May 30, 2017

The Honorable Ajit Pai
Chairman
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Dear Chairman Pai,

We greatly appreciate the time you took to meet with the Small Company Coalition (SCC) on April 11 to discuss our views regarding a variety of matters important to small rural telecom providers. As you'll recall, in addition to the absolute necessity of raising the Universal Service Fund (USF) cap, we also discussed ways to streamline and improve the regulatory process.

As we related at that time, one of our primary concerns is management at the Universal Service Administrative Company (USAC). While we fully support the need to keep close watch on the utilization of USF funds, as entities who have been through USAC audits, our experiences left us convinced that this process was fundamentally flawed both in the targeting and execution of the audits. In addition, our review of USAC's financial statements and Universal Service Fund contribution processes revealed that the Commission and other stakeholders would be well-served by a fresh, detailed review in a formal setting.

We were greatly encouraged, therefore, to see that both you and Commissioner O'Rielly informed USAC that improvement was necessary. As it so happens, at the time of your warnings to USAC, the SCC was in the midst of investigating what we believe to be possible problems in USAC's administration of the USF program.

As you may know, the SCC was formed to work cooperatively with the FCC, providing an on-the-ground, practical perspective to federal regulators. Though we are a small group, the SCC member companies live in the communities we serve, and take our responsibilities to these communities very seriously. Consequently, the SCC expended substantial time and effort in conducting our own review of particular aspects of USAC's administration of federal universal service programs, including, *inter alia*: 1) carryover of unexpended USF monies, now constituting a substantial reserve; and 2) audit expenditures, findings of malfeasance, and associated recoveries.

Based on our analysis, we have identified several areas of concern, including:

1) <u>Reserve fund carryover</u>
   - Significant funds are collected each year from service providers, yet not disbursed. According to USAC's own reports, this reserve now exceeds $8 billion in the form of Assets Held for the USF and CAF Reserves (now the High Cost Account).

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- We believe that this overage could be put to better use by increasing payments to providers, and/or in reduced collections from end-user/customers.

2) Size of USF shortfall
   - Past estimates of the annual shortfall in the USF program have varied, but have generally been within the $200-$400 million range.

   - The SCC's careful analysis places this annual shortfall startlingly closer to $1.5 billion per annum.

3) Unfocused and wasteful audits
   - According to their own numbers, the FCC and USAC have spent close to $250 million on the first three rounds of USAC audits of the High Cost Program alone, but in fiscal year 2016, recovered only $8 million.

   - Such a startlingly low recovery rate clearly demonstrates that USAC should dramatically revise their audit targeting, utilizing—at a minimum—the materiality threshold in accordance with generally accepted auditing standards.

Within the next two weeks, the SCC will be releasing a white paper elucidating these findings in greater detail. We would very much appreciate an opportunity to sit down with you at that time to discuss our findings, with an eye toward further enhancing the FCC's role as a responsible and accountable regulator.

Similarly, pursuant to our earlier conversation, we'd like to formally extend to you an invitation to come visit our operations in Southwestern Pennsylvania. It's only a short distance from Washington, D.C., and would be illuminating with respect to how small rural telecoms operate, and the unique challenges we face in providing quality services to remote communities.

As always, we are grateful for your leadership, and very much appreciate your time and consideration. We'll be in contact with your office shortly to arrange a time to meet.

Sincerely,

James J. Kail
Executive Committee Member

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