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ORIGINAL

EX PARTE OR LATE FILED

R. William (Bill) Johnston
Executive Director - Markets
Federal Regulatory Strategy

USWEST

July 30, 1999

EX PARTE

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 - 12th Street, SW, TW-A325
Washington, DC 20554

RECEIVED
JUL 30 1999
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

RE: **CC Docket No. 99-253**
Comprehensive Review of the Accounting Requirements and
ARMIS Reporting Requirements for Incumbent Local Exchange
Carriers: Phase I

Dear Ms. Salas:

Today, representatives from Ameritech (Tony Alessi); GTE (Scott Randolph); Alltel (Carolyn Hill); U S WEST (Bill Johnston) and Carl Geppert of Arthur Andersen, met with the following Accounting and Safeguards Division representatives: Mark Gerner, John Hays, Mark Stone, Brett Kissel, Andy Skadin, Mark Stephens, Alicia Dunnigan, Tim Peterson, Robert Hood, Hugh Boyle, Joe Watts and Ellen Becker to discuss the above-referenced proceeding. The attached material was distributed at the meeting and served as the basis of the discussion.

In accordance with Section 1.1206(a)(2) of the Commission's rules, an original and one copy of this letter and the attachment are being filed with your office for inclusion in the public record.

Acknowledgment and date of receipt of this submission are requested.

Sincerely,



Attachment

| | | |
|---------------------|---------------|-----------------|
| Copy w/ Attachment: | Mark Gerner | Alicia Dunnigan |
| | John Hays | Tim Peterson |
| | Mark Stone | Robert Hood |
| | Brett Kissel | Hugh Boyle |
| | Andy Skadin | Joe Watts |
| | Mark Stephens | Ellen Becker |

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Federal Communications Commission

Cost Allocation Manual (CAM) Audits

Audits Branch Meeting

July 30, 1999

ARTHUR
ANDERSEN

CAM Audit Overview

- CAM Audit Background
- Relationship of CAM and Financial Statement Audits
- Changes in CAM Audit Requirements
- Impact on Audit Procedures
- Other Impacts
- Impact on Audit Fees

CAM Audit Background

- Prior to 1991, annual attestation engagements were performed in accordance with AICPA Attestation Standards (expressed an opinion as to compliance with the CAM)
- From 1991 to the present, audits are being performed annually in accordance with SAS No. 58 (audits express a positive opinion as to the fair presentation of Report 43-03)

CAM Audit Background (Cont.)

● Audit Requirements

» Part 64, Section 64.904

- Audits are performed annually
- Opinion that 43-03 “presents fairly”
- Follow GAAS, except as directed by the Chief, Common Carrier Bureau
- Report filed with 43-03 (by April 1)

● Other Reporting Requirements

» CAM Audit Review Package (CAM Spreadsheets)

- Summary of LEC Cost Allocation Results, Audit Procedures & Results
- Filed by May 1

● Audit and Reporting Guidelines

» Audit Guidance Letters (10/16/91, 4/20/92)

» CAM Spreadsheet Letters

» CAM Audit Review Letters (to individual companies)

**ARTHUR
ANDERSEN**

Relationship of CAM and Financial Statement Audits

- Financial Statement Audits --

- » Focus is on fair presentation of financial statements taken as a whole
- » Scope & approach is determined on that basis
- » Provides the primary basis for Part 32 testing (in support of Column (b) of Report 43-03)
- » Testing of significant financial systems and processes performed/ relied on in Part 64

- Part 64 Audits --

- » Focus is on fair presentation of Report 43-03
- » Incremental Part 32 testing performed, specifically focused on Part 32 account distributions
- » Testing of specific Part 64 audit risk areas and related systems & processes

Changes in CAM Audit Requirements

● Mid-Size LECs

- » Report and Order in CC Docket No. 98-81, Order on Reconsideration in CC Docket No 96-150, released June 30, 1999
- » Prescribes Attestation Engagement to be performed every two years
 - Covers 2-year period
 - CAM based on Class B Account Structure

● Large LECs

- » NPRM in CC Docket No. 99-253, released July 14, 1999
- » Proposes Attestation Engagement to be performed every two years
 - Covers 2-year period
 - CAM based on Class A Account Structure

Changes in CAM Audit Requirements (Cont.)

● New Report of Independent Public Accountants

- » Issued pursuant to AICPA Attestation Standards - opinion regarding the “fair presentation” of Management’s Assertion Statement
- » Examination expected to include the following procedures (taken from pre-1991 attestation opinion) -
 - Obtain understanding of the Company’s CAM
 - Review Company policies and procedures for implementation of the CAM
 - Determine consistency of cost allocation methods with the CAM
 - Evaluate materiality and criticality of data sources utilized
 - Evaluate reasonableness of data sources utilized in providing costing information for selected cost allocation methodologies
 - Obtain understanding of Company policies and procedures relating to incidental activities and affiliate transactions & determine that such transactions were accounted for in conformity with the CAM
 - Determine that data reported in columns (b) through (j) of the Company’s Report 43-03 agrees with information produced by the cost allocation system

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Impact on Audit Procedures

- Overall Shift of Audit Focus:

- » **FROM** Report on Cost Allocation Results presented in ARMIS 43-03
TO Report on Management Assertion (Statement of Cost Allocation System Compliance)

- Change in Audit Period:

- » **FROM** Annual Audit Period **TO** Two-Year Audit Period

- Overall Impacts:

- » Audit Procedures to Focus on Cost Allocation System and Supporting Methods and Procedures (Compliance with CAM & FCC Rules)
- » Audit Procedures to be Performed Throughout Two-Year Period
- » Emphasis on Compliance Testing, Reduced Emphasis on Substantive Testing

Impact on Audit Procedures (Cont.)

- Impact on Major Audit Areas:
 - » Part 32 Testing
 - » Time Reporting
 - » Affiliate Transactions
 - » Cost Apportionment Studies (Special Studies)
 - » Part 64 System
 - » Incidental Activities
 - » Report 43-03 Testing
- Impact on Audit Reporting Requirements
- Impact on CAM Audit Review Package (CAM Spreadsheets)

Other Impacts

- Clarification of New Section 64.904 Requirements
 - » Effective date of New Mid-Sized LEC Audit Standards
 - » Interpretation of Section 64.901(b) language:
 - “...expresses an opinion that the results reported pursuant to 43.21(e)(2) of this chapter are an **accurate application** of the Commission’s Joint Cost Orders...”
- Application of Existing FCC Audit Guidance
 - » October 16, 1991 Letter
 - » April 20, 1992 Letter
 - » CAM Spreadsheet Letters
 - » FCC CAM Audit Review Letters
- Other

Impact on Audit Fees

- Major Drivers of Audit Cost Reductions:
 - » Change from annual audit period
 - » Focus on compliance testing of methods & procedures
 - » Elimination of incremental Part 32 and detailed Report 43-03 testing
- Minimal Impacts Expected From the Following Changes:
 - » Class B Level CAM for Mid-Sized LECs
 - » \$250,000 proposed threshold for fair market value studies
- Audit Fees Should Decrease by a Minimum of 50%
 - » Extent of decrease will depend on specific changes adopted -
 - Management assertion and required procedures
 - Application of audit guidelines
 - CAM Spreadsheet requirements