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August 17, 1999

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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

Re: Comprehensive Review of Accounting Requirements – CC Dkt. 99-253

Dear Ms. Salas,

On August 17, representatives from BellSouth, Bell Atlantic, and PriceWaterhouseCoopers LLP met with members of the Accounting Safeguards Division, at their request, to discuss issues regarding audits of Cost Allocation Manuals and the potential impact of allowing carriers to obtain an attestation, instead of an annual financial audit. Topics addressed included an overview of attestation engagement standards, previous attestation engagements performed, and issues associated with moving to attestation engagements. All materials distributed during the meeting are attached.

Participating in the meeting from each organization: ASD - Hugh Boyle, Mark Stephens, Joe Watts, Brett Kissel, Andrew Skadin, Alex Chan, and Diane Lee; PriceWaterhouseCoopers - T.J. Mangold, Terry Bowling, Martin Kehoe, and Sharon Luckshire; Bell Atlantic - Gerald Asch, Sandy Anderson, and Joann Barron; and, BellSouth -Lyn Rogers-Haney, Mary Henze, and Kathie Levitz.

This notice is being filed pursuant to Sec. 1.1206(b)(2) of the Commission's rules. If you have any questions concerning this filing, please do not hesitate to contact me.

Sincerely,



Mary L. Henze

cc: H. Boyle A. Skadin
M. Stephens A. Chan
J. Watts D. Lee
B. Kissel

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Federal Communications Commission

Attestation Engagement Presentation

to Audits Branch

August 17, 1999

Overview

- Currently the ARMIS 43-03 report is subject to a full-scope financial statement audit. This presentation will discuss an alternative to an audit, an attestation engagement, as mentioned in the NPRM.
- Points for Discussion:
 - Overview of Attestation Engagements
 - Previous Attestation Engagement Performed
 - Issues in Moving to Attestation Engagement

Compliance Attestation

- AT Section 500 of the Statements on Standards for Attestation Engagements provides guidance for engagements related to management's written assertion about either:
 - An entity's compliance with requirements of specified laws, regulations, rules, contracts, or grants; or
 - The effectiveness of an entity's internal control structure over compliance with specified requirements
- This presentation will discuss compliance attestation as it relates to requirements of specified laws and regulations

Objectives of the Engagement

- The objective of the examination procedures applied to management's assertions about an entity's compliance is to express an opinion about whether management's assertion is fairly stated in all material respects based on established criteria.
- To do this, the practitioner should limit attestation risk to an acceptably low level by accumulating sufficient evidence in support of management's assertion regarding compliance.
- This includes designing the examination to detect both intentional and unintentional non-compliance which is material to the assertion.

Conditions for Attestation Engagement Performance

This type of engagement may be performed only if the following conditions are met:

- Management accepts responsibility for the entity's compliance with the specified requirements
- Management evaluates the entity's compliance with the specified requirements
- Management makes an assertion about the entity's compliance with specified requirements
 - Assertion may take various forms but should be specific enough that users having competence in and using similar measurement and disclosure criteria ordinarily would arrive at materially similar conclusions
- Management's assertion is capable of evaluation against reasonable criteria that either have been established by a recognized body or are sufficiently clear and comprehensive, and the assertion is capable of reasonably consistent estimation or measurement using such criteria.
- Sufficient evidential matter exists (or could be developed) to support management's evaluation.

Management's Responsibilities

- Management is responsible for ensuring that the entity complies with the requirements applicable to its activities.
- This responsibility encompasses:
 - Identifying applicable compliance requirements
 - Establishing and maintaining internal control structure policies and procedures to provide reasonable assurance that the entity complies with those requirements
 - Evaluating and monitoring the entity's compliance
 - Specifying reports that satisfy legal, regulatory, or contractual requirements

Materiality

- Consideration of materiality differs from that of an audit of financial statements in accordance with GAAS
- The consideration is affected by:
 - Nature of management's assertion and the compliance requirements
 - These may not be quantifiable in monetary terms
 - Nature and frequency of noncompliance identified (with appropriate consideration of sampling risk)
 - Qualitative considerations, such as needs and expectations of the report's users
 - The engagement may provide for a supplemental report of all or certain noncompliance discovered. Such a requirement should not change the practitioner's judgments about materiality in planning, performing or reporting on the engagement

Performing the Engagement

The following should be performed:

- Obtain an understanding of the specified compliance requirements
- Plan the engagement
- Consider relevant portions of the entity's internal control structure over compliance
- Obtain sufficient evidence including testing compliance with specified requirements
- Consider subsequent events
- Form an opinion about whether management's assertion regarding compliance with specified requirements is fairly stated in all material respects, considering
 - Nature and frequency of noncompliance identified
 - Materiality of noncompliance relative to the compliance requirements

Sample Report from AT 500.55

We have examined management's assertion about [name of entity]'s compliance with [list specified compliance requirements] during the [period] ended [date] included in the accompanying [title of management's report]. Management is responsible for [name of entity]'s compliance with those requirements. Our responsibility is to express an opinion on management's assertion about the Company's compliance based on our examination.

Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence about [name of entity]'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on [name of entity]'s compliance with specified requirements.

In our opinion, management's assertion [identify management's assertion] is fairly stated, in all material respects.

Other Reporting Considerations

- Evaluating compliance may require interpretation of the laws, regulations, rules, contracts, or grants. If so, the practitioner should consider whether they have been provided with reasonable criteria to evaluate the assertion.

- If the interpretations are significant, a descriptive paragraph stating the description and source of interpretation made by management may be added, following the scope paragraph.

Previous Attestation Engagement

- Prior to the current requirements for a financial statement audit of the 43-03, the FCC required an attestation engagement (late 1980s).
- Assertion made by management was that the cost allocation system conformed to the criteria in the CAM, and the 43-03 was prepared in accordance with those criteria (see Appendix 1 for an example).
- Specific procedures performed by the independent auditors included (see Appendix 2 for an example):
 - Obtaining an understanding of the CAM
 - Reviewing Company policies and procedures for implementing the CAM
 - Reviewing the cost allocation methods for consistency with the CAM
 - Evaluating the materiality and reasonableness of data sources used
 - Obtaining an understanding of incidental activities and affiliated transactions to determine conformity with the CAM
 - Determining if 43-03 columns (c) to (j) agreed to cost allocation system

Summary of Engagement Alternatives

	<u>Financial Audit</u>	<u>Compliance Attestation</u>
Source of Standards	AU Sections of the AICPA Professional Standards	AT Section 500 of the AICPA Professional Standards
Scope of Procedures	Auditor's Judgment	Auditor's Judgment
Responsibility for Procedures	Auditor's Judgment	Auditor's Judgment

Summary of Engagement Alternatives

	<u>Financial Audit</u>	<u>Compliance Attestation</u>
FCC Input as to steps performed	Can request, but not mandate	Can request, but not mandate
Opinion	Yes, regarding financial statements taken as a whole	Yes, regarding the assertion pertaining to internal controls or compliance taken as a whole
Report	Fairly stated and free of material misstatement	Fairly stated in compliance with management's written assertion

Summary of Engagement Alternatives

	<u>Financial Audit</u>	<u>Compliance Attestation</u>
Report of Findings	<ul style="list-style-type: none"> • Based solely on auditor judgment • In a separate letter to management 	<ul style="list-style-type: none"> • Based solely on auditor judgment • In a separate letter to management
Concept of Materiality	Yes	Yes
Impairment of Independence	None if auditor determines scope and develops program	None if auditor determines scope and develops program

Other Issues for Discussion

- Nature of Assertions
- Timing Issues (Single year/Two year)
- Impact on Spreadsheets
- Other Alternatives



South Central Bell

B.V. Walton
Vice President and Comptroller

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Birmingham, Alabama 35201
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SOUTH CENTRAL BELL TELEPHONE COMPANY
STATEMENT OF COST ALLOCATION SYSTEM COMPLIANCE
FOR THE YEAR ENDED DECEMBER 31, 1988

Our Cost Allocation Manual as amended through September 30, 1988 (the "Manual") has been filed with the Federal Communications Commission. The Manual provides criteria against which the Company's cost allocation system can be evaluated. The system is supported by cost allocation methods which are consistent with the Manual and utilized methods which permit preparation of the attached FCC Report 43-03 in accordance with the Manual. The actual cost allocation methods and procedures implemented and performed conform with the objectives, approach and procedures described in the Manual.

We believe that, for the year ended December 31, 1988, the cost allocation system, as implemented, conforms with the criteria set forth in the Manual and the report referred to above has been prepared in accordance with these criteria.

Date March 27, 1989

Name B.V. Walton

Title Vice President and Comptroller

**Coopers
& Lybrand**

certified public accountants

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**Mr. Boyd V. Walton
Vice President and Comptroller
South Central Bell Telephone Company**

We have examined the accompanying South Central Bell Telephone Company Statement of Cost Allocation System Compliance for the year ended December 31, 1988. Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary in the circumstances.

Our examination included the following procedures. We:

- Obtained an understanding of the Company's Cost Allocation Manual as amended through September 30, 1988 ("the Manual");
- Reviewed Company policies and procedures for implementation of the Manual;
- Determined the consistency of the cost allocation methods with the Manual;
- Evaluated the materiality and criticality of data sources utilized;
- Evaluated the reasonableness of data sources utilized in providing costing information for selected cost allocation methodologies;
- Obtained an understanding of the Company policies and procedures relating to incidental activities and transactions with affiliates and determined that such transactions were accounted for in conformity with the Manual, and
- Determined that the data in columns (c) to (j) in the attached FCC Report 43-03 agrees with the information produced by the Cost Allocation System.

In our opinion, the accompanying Statement of Cost Allocation System Compliance of South Central Bell Telephone Company presents, in all material respects, the operation of the Cost Allocation System for the year ended December 31, 1988, in conformity with the criteria set forth in the Manual.

This report is intended for the information of the Company and the Federal Communications Commission, which established the criteria under which the Statement of Cost Allocation System Compliance was evaluated. Accordingly, the report should not be used by those who did not participate in establishing the criteria.

Coopers & Lybrand

Atlanta, Georgia
March 27, 1989