

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)
)
Comprehensive Review of the Universal Service) WC Docket No. 05-195
Fund Management, Administration, and Oversight)

COMMENTS OF VERIZON AND VERIZON WIRELESS

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I. INTRODUCTION AND SUMMARY.

This proceeding affords the Commission an important opportunity to improve oversight and management of the Universal Service Fund (“USF” or “Fund”) while ensuring that it operates in an efficient and effective manner.² The Commission should adopt Verizon’s specific recommendations regarding universal service audits, reseller procedures, carrier “red light” status, USF contribution guidance to the industry, document retention, Universal Service Administrative Company (“USAC”) procurements and administrative processes, and rural healthcare funding recovery.

Although carrier audits are an important tool in safeguarding the USF from waste, fraud, and abuse, the audits, as currently administered, can sometimes contribute toward the ineffective use of program funds. Some of the audit challenges are understandable because comprehensive auditing is a relatively recent addition to USF administration. Such challenges include USF audits that are not always appropriately focused. USF audits should be better targeted, and audit

¹ In addition to Verizon Wireless, the Verizon companies participating in this filing are the regulated, wholly owned subsidiaries of Verizon Communications Inc. (collectively “Verizon”).

² *Comprehensive Review of the Universal Service Fund Management, Administration, and Oversight*, Notice of Inquiry, WC Dkt. No 05-195, FCC 08-189 (rel. Sep. 12, 2008) (“*NOI*”).

procedures should be better defined, so that auditors and carriers have consistent expectations, which will help make the fund more efficient.

The Commission should also adopt other changes to the administration of the fund to give parties appropriate incentives and to ensure consistent USF contributions from all providers. Among other things, the Commission should end the practice of requiring wholesalers to police and guarantee the universal service payments of reseller customers. The Commission should also provide contributors with more advance warning regarding an entity's "red light" status to allow USF contributors to respond to and correct any issues prior to being denied funding. In addition, the current system does not afford contributors a readily available means to obtain consistent and reliable guidance from the Commission on important issues that affect the competitive market. To address this shortcoming, the Commission should institute a more formal process for USF contributors to seek guidance from the Wireline Competition Bureau.

At the same time, the Commission should refrain from adopting requirements that would only burden the program without providing any corresponding benefits. There is no need for the Commission to establish additional rules extending document retention periods. The existing document retention rules that the Commission adopted just last year for each USF program strike an appropriate balance between the need to preserve important information and the inherent cost of maintaining such records for specified periods of time. Similarly, the Commission should not require additional, unnecessary Federal Acquisition Regulation compliance from USAC nor seek to move administration of the Fund to a government contract relationship. Doing so would only add unnecessary costs and would eliminate any efficiencies inherent in having a third-party rather than the government administer the USF.

Finally, the Commission should clarify that the E-rate rule requiring USAC to seek

recovery of improperly acquired funds from the party at fault applies equally to the rural healthcare program.

II. THE COMMISSION SHOULD STREAMLINE THE USF AUDIT PROCESS.

Verizon understands the important role that the audit process plays in ensuring the sustainability and sufficiency of the Fund. But the audit process can and should be improved. Comprehensive USF auditing, in place now for more than two years, should become more efficient. There are few standards that govern USF audits, and there is insufficient consistency among audits. Several parties have raised concerns about the current audit process, including members of Congress.³

To address these and other related concerns, the Commission should take the following steps: (1) establish a materiality threshold for audit findings; (2) eliminate duplicative audits and encourage the increased use of data sampling; (3) give carriers that are subject to an audit timely notice when the audit fieldwork and findings are complete and notice of audit results within one month from submission of findings; (4) ensure that audits are appropriately focused from their inception, including providing the entity being audited with sufficient information about the purpose of the audit; (5) establish a standardized framework for USF audits that appropriately recognizes differences in the size of the companies being audited; and (6) adopt a comprehensive training program for all auditors employed and retained by USAC.

A. Materiality.

The Commission should establish a standard materiality threshold for audit findings to differentiate meaningful issues from insignificant matters. The most recent round of high cost program audits, for example, resulted in many audit findings regarding small line count

³ See, e.g., Letter from Senator Enzi, Senator Barrasso and Rep. Cubin to Kevin J. Martin, Chairman, FCC (Sept. 29, 2008) (“*Enzi Letter*”); Letter from Reps, Stupak, Terry, and 44 other members of Congress to Kevin J. Martin, Chairman, FCC (Oct. 6, 2008) (“*Stupak Letter*”).

inconsistencies that were not material under any standard. Line counts are dynamic. As a result, very often these small variances are not the product of anything nefarious, or even an error, but rather for large study areas reflect the inherent difficulty of reaching back in time to exactly recreate counts of millions of lines through database queries. The current lack of a materiality threshold is difficult for auditors, USAC, and companies alike. Indeed, it can lead to recommendations that are out of proportion to the actual discrepancies. Thus, even though a discrepancy may be so inconsequential that no recovery results from the auditor's findings, these non-material issues can result in unwarranted conclusions about "controls" failures and recommendations for unnecessary, expensive process changes.

B. Duplication.

The Commission should streamline the audit process to eliminate duplicative USF audits. In particular, the Commission's Office of Inspector General ("OIG") and USAC⁴ should eliminate multiple audits that involve the same holding company using the same systems but operating in different study areas. The OIG and USAC also should not "re-audit" a carrier in the same study area in successive audit cycles unless there is a change in circumstances. In addition, the OIG and USAC should encourage high cost auditors evaluating large companies to use samples of line count data rather review millions of actual subscriber records. These minor modifications alone could significantly reduce the number and complexity of high cost audits without affecting the quality or nature of the audit findings.

Auditing multiple, individual study areas of the same company is not a good use of resources. Very often, large companies such as Verizon use centralized billing systems and other databases to support multiple study areas. And many, if not all, of the same carrier personnel

⁴ The Commission's OIG oversees the USF audits, which are carried out by auditors retained by USAC.

perform accounting functions across multiple study areas. As a result, separate audits examining the same procedures of the same company, albeit in different study areas, are unnecessarily duplicative. The same is true of audits of the same carrier study area in successive audit cycles. Nothing is gained by simply “re-doing” an audit for a different time period unless there is a change in circumstances. This is particularly true when the timing of a subsequent audit is such that the company could not have implemented any changes as a result of the findings in the earlier audit that would affect the new audit period.

To further streamline the process, the Commission should encourage auditors to sample subscriber line data during high cost audits rather than looking at all line count data. Currently, auditors very often request literally tens of millions of records to verify line counts in large study areas. Reasonable sampling is much more efficient and is still reliable.

C. Notice.

USF audits should be concluded in a timely and consistent manner. Currently, carriers are given little guidance as to what constitutes a final decision of an auditor and/or USAC, and it is often unclear when an audit is actually “closed.” This results in uncertainty for the company and confusion over the timeframe to exercise any appeal rights. *Stupak Letter* at 2 (noting that there has been a failure by auditors to “complete, issue, and share final audits with individual companies on a timely basis”). The uncertainty created by open audits can also create the incorrect impression that there are control deficiencies, which can be harmful in other contexts such as litigation or new audits. To address this concern the OIG and USAC should: (i) specify at the outset of the audit the nature of the final deliverable that an auditor must produce at the conclusion of the audit; and (ii) provide the audited company with a copy of the final audit report that includes USAC’s response to the audit within one month from submission of findings to USAC.

D. Focus.

The Commission should ensure that USF audits are appropriately focused. A company currently subject to a USF audit is essentially required to attest that it has complied with all applicable USF rules, even though the purpose of the audit is not and should not be to confirm compliance with every USF rule. For example, USF audits conducted pursuant to the Improper Payments Information Act (“IPIA”), which appears to govern the vast majority of USF audits conducted to date, are intended to ensure that the Commission identifies areas that “are vulnerable to making erroneous payments” and reports on steps it has taken “to reduce these vulnerabilities.” 31 U.S.C. § 3321 (2006). Consequently, an audit conducted pursuant to the IPIA should be focused on identifying potential erroneous USF payments, not ensuring compliance with every requirement of every USF program.

Similarly, the scope of an audit necessarily depends upon the particular USF program at issue. Different high cost programs like Interstate Common Line Support, Interstate Access Support, and Local Loop and Switching Support involve different support schedules and different funding structures. An IAS audit, for example, should focus on the accuracy of line counts, not consideration of the original calculations undertaken pursuant to the *CALLS Order*, which were not calculated and published by audited companies.⁵ However, under the current audit regime, auditors have sometimes used generic document and data requests that are over-inclusive, which necessitates lengthy discussions with the auditors to determine what documents are necessary and relevant to the particular program being evaluated.

⁵ See 47 C.F.R. § 54.800 *et seq.*; *Access Charge Reform*, Sixth Report and Order, CC Dkt. Nos. 96-262 and 94-1, Report and Order, CC Dkt. No. 99-249, Eleventh Report and Order, CC Dkt. No 96-45, 15 FCC Rcd 12962 (2000) (subsequent history omitted) (“*CALLS Order*”).

The OIG and USAC can readily address these problems by: (i) providing auditors with a specific description of the scope of the audit to be conducted, including the particular USF program(s) at issue; and (ii) mandating that all information, documents, and data requested by the auditor be consistent with the scope of the audit as defined by the OIG and USAC. These measures would make the audit process considerably more cost effective and efficient.

E. Standard Framework.

Audit plans employed by USF auditors vary widely, and different auditors conducting the same type of audit very often request and base their opinions on different information. Such variations can add unnecessary cost and complexity to the audit process. The Commission should establish a standardized framework for the audit process that includes streamlined information requests from all similarly situated companies audited under the same USF program while still allowing auditors flexibility to modify the requests as circumstances warrant.⁶ This standardized framework should take into account the size of the entity being audited. For example, for large companies it is simply not practical or even useful to require that their senior-level corporate officers meet with auditors or sign representation and assertion letters. Rather, the corporate managers most directly responsible for the audit subject matter are in the best

⁶ That USF audits may be conducted as “compliance attestation” engagements in accordance with Generally Accepted Government Auditor Standards (“GAGAS”) and the American Institute of Certified Public Accountant (“AICPA”) standards does not preclude the Commission from establishing a model framework to govern such audits. *See, e.g.*, GAGAS at § 3.7 (providing that “exercising professional judgment in determining the sufficiency and appropriateness of evidence to be used to support the findings and conclusions based on the audit objectives and any recommendations reported is an integral part of the audit process”); AICPA Standards, Compliance Attestation § AT 601.48 (for attestation engagements, the auditor “should apply procedures to provide reasonable assurance of detecting material noncompliance. Determining these procedures and evaluating the sufficiency of the evidence are matters of professional judgment”). The establishment of a basic standardized format for audits in order to impose more structure on the audit process would not prevent an auditor from exercising his or her professional judgment in conducting the audit.

position to assist auditors and attest to compliance. In addition, certain information requests that might be reasonable for a small company often result in time-consuming and expensive undertakings by a large company and ultimately produce nothing more than an unwieldy and useless “data dump.”

F. Auditor Training.

Auditors need better training about the USF programs that they are auditing. While the OIG and USAC have an auditor training program and many auditors have subject matter expertise, additional knowledge of the communications industry generally and of specific USF programs would be useful to all parties. *See Enzi Letter* (noting that “many of the Contracted USAC auditors have no knowledge of the telecommunications industry and the USF program”). An understanding of the programs subject to audit and the accounting practices of the entities being audited is essential to ensuring that audits are complete and accurate.⁷ Lack of knowledge can prolong an audit and lead to inaccurate conclusions, which benefit no one. Additional education and a baseline level of understanding of the USF programs and communications industry accounting practices should be a prerequisite for any auditor working on behalf of the OIG and USAC.

III. THE COMMISSION SHOULD ADOPT OTHER PROPOSALS TO BETTER ALIGN CARRIER INCENTIVES WITH USF OBJECTIVES.

In addition to reforming the audit process, the Commission should adopt certain proposals suggested in the past to make the administration of the fund more efficient. At a

⁷ *See* GAGAS § 3.36 (requiring that “professional judgment is important in determining the required level of understanding of the audit subject matter and related circumstances” and noting that “staff assigned to conduct an audit or attestation engagement under GAGAS must collectively possess the technical knowledge, skills, and experience necessary to be competent for the type of work being performed before beginning work on that assignment”); AICPA Standards § AT 601.40 (noting that auditors “should obtain an understanding of the specified compliance requirements” that are being considered in the audit).

minimum, the Commission should eliminate the requirement for wholesalers to police the USF contributions of their reseller customers; give contributors an opportunity to respond to and correct any “red light” issues that arise before applying the rule; and should formalize a process for contributors to seek and receive real-time, consistent, and reliable guidance from the Wireline Competition Bureau.

The Commission should not continue to require that underlying carriers monitor and verify the USF contributions of their reseller customers. Over time, the Wireline Competition Bureau and USAC have adopted changes to the Form 499 Worksheet Instructions that effectively ask wholesale carriers to guarantee reseller contributions to the Fund. Today, wholesalers are subject to onerous requirements to collect a Form 499 filer ID and other information from their resellers, annually obtain a signed statement from resellers regarding their contributions, and to more generally monitor reseller contributions because “[f]ilers that do not comply with the above procedures will be responsible for any additional universal service assessments that result if its customers must be reclassified as end users.” *See* Telecommunications Reporting Worksheet, Form 499-A, Instructions at 19 (February 2008).

Such requirements do not strike the right policy balance. These policing functions are more appropriately carried out by USAC or Enforcement Bureau personnel who, unlike wholesaler carriers, have the ability to force resellers to comply with program rules. Moreover, requiring wholesale carriers to guarantee reseller contributions to the fund does not give resellers themselves incentive to ensure that all required contributions are properly made. These requirements also create a competitive imbalance because they disadvantage wholesale providers relative to their pure retail competitors. The Commission should eliminate these requirements so that wholesalers are no longer required to underwrite the contributions of resellers.

Reflexive application of the Commission’s red light rule also results in the wrong incentives. The red light rule ensures that companies will not receive the benefits of universal service payments if their non-tax debts are unpaid. In practice, companies can also be suspended from receiving USF support because of an erroneous red light notices caused by administrative error. For example, Verizon once received a red light notification that occurred because of a clerical error from typing a Form 499 filer ID number. Under current practice, if a company has a red light issue, it frequently will only obtain notice when funding has already been suspended and will be given thirty days to remedy any deficiencies.⁸ Instead of notifying companies of red light issues only when funding has been suspended, however, the Commission should adopt a process that provides carriers with a 30-day grace period, or “yellow light” period, during which they would be given a warning and an opportunity to remedy any issues *before* funding is suspended for pending disbursements. This would benefit all parties by giving carriers incentive to fix issues quickly while there is still time to do so before the “red light.”

At the same time, the Commission should establish a more formal and efficient process for participants to obtain guidance from the Wireline Competition Bureau regarding USF contributions. The Commission is correct that certain rules do not lend themselves to straightforward interpretation in all circumstances. *NOI*, ¶ 30. Contributors should not be required to wait for an audit or investigation to determine the Commission’s interpretation of its USF rules, at which point it may be too late to avoid fines or penalties. The absence of real-time contribution guidance also creates competitive disparities when providers interpret the contribution rules differently. If parties had access to a more formal process with specific timelines to obtain guidance from the Bureau, the Commission could address misunderstandings before they evolve into larger problems and result in audits and investigations.

⁸ 47 C.F.R. §1.1910.

The exact form of such a process need not be elaborate or burdensome on the Bureau. The Commission should establish a reasonable timeframe by which the Bureau would be required to respond to inquiries regarding the interpretation of contribution rules within the Bureau's delegated authority or the establishment of a more formal pleading process for such inquiries. A process by which the Bureau would commit to respond to parties through a timely exchange of letters would work for this purpose. The subsequent fulfillment of that commitment would likely save USAC, the Bureau, and affected parties a great deal of time and resources.

IV. THE COMMISSION SHOULD NOT ADOPT BURDENSOME REQUIREMENTS THAT HAVE NO CORRESPONDING BENEFITS TO THE FUND.

The Commission should refrain from adopting requirements that would only burden the Fund without providing any corresponding benefit. For example, there is no need for the Commission to establish additional rules extending document retention periods. *NOI*, ¶ 21. The existing document retention rules that the Commission adopted just last year for each USF program strike an appropriate balance between the need to preserve important information and the inherent cost of maintaining such records for specified periods of time. Likewise, there is no need for the Commission to establish additional restrictions on USAC procurements or to more generally require that USAC operate under a government contracting relationship instead of as a third-party administrator.

The Commission's current rules generally require that records pertaining to USF programs (except for the low income program) be retained for five years. *Id.* The five-year document retention period is comparable to the document retention requirements of other federal programs. *See, e.g.*, 42 C.F.R. § 482.24 (requiring hospitals that participate in Medicare to retain inpatient and outpatient medical records for five years); Federal Acquisition Regulation § 4.703 (requiring federal contractors to retain most records for three years with some categories of

records required to be retained for up to four years and others only required to be retained for two). Extending this five-year document retention requirement would subject program participants to additional, unnecessary costs ultimately paid for by consumers.

Nor should the Commission require that USAC comply with all aspects of the Federal Acquisition Regulation (“FAR”), the extensive rules that regulate many aspects of the federal government acquisition process, or to more generally operate under a government contracting relationship. *NOI*, ¶ 33. At the outset, it is not clear that the Commission’s requirement that USAC conduct its procurements consistent with FAR has improved the efficacy or results of USAC’s procurement process or USAC’s performance as an administrator. With respect to whether USAC should be required to comply with the “socio-economic goals incorporated into FAR,” such goals, no matter how laudable, are not consistent with the purposes for which Congress established the Fund. *Id.*

Requiring that USAC comply with additional requirements of FAR or other government contracting requirements would only increase the costs of administration of the Fund to the detriment of participants and consumers alike. Moreover, the reason for third-party administration of the fund is to realize efficiencies that could not be obtained if the USF were administered by the Commission – a benefit that would be lost if the Commission required USAC to comply with the same restrictions that would apply if the Commission itself administered the Fund.

V. THE COMMISSION SHOULD REQUIRE USAC TO RECOVER RURAL HEALTH CARE PROGRAM FUNDS FROM THE PARTY THAT COMMITS THE RULE VIOLATION.

The Commission should clarify that its E-rate rules requiring USAC to recover contributions from the party that commits a rule violation, rather than from the service provider

only, applies equally to the rural healthcare program.⁹ In the E-Rate context, the Commission has recognized that “directing recovery actions towards beneficiaries in those situations where the beneficiary bears responsibility for the rule or statutory violation will promote greater accountability and care on the part of such beneficiaries.” *Id.* at 15256 (¶ 13). This is also the case in the rural healthcare context. The Commission should clarify that USAC should seek recovery from healthcare providers where they, and not the service provider, are at fault.

⁹ *Federal State Joint Board on Universal Service, Changes to the Board of Directors for the National Exchange Carrier Association, Inc., Schools and Libraries Universal Support Mechanism, Order on Reconsideration and Fourth Report and Order, 19 FCC Rcd 15252 (2004).*

VI. CONCLUSION

The Commission should adopt the universal service administrative reforms suggested by Verizon.

Respectfully submitted,

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