



By Courier

April 30, 2013

High Cost and Low Income Committee
Universal Service Administrative Company
2000 L St., N.W., Suite 200
Washington, D.C. 20036

Re: Appeal of the FCC Office of Inspector General USF Audit Program Audits of High Cost Program Beneficiaries: Nemont Telephone Cooperative, Inc. and Project Telephone Company (SAC 482247 and 482250), Audit HC-2009-001

Gentlemen,

Pursuant to 47 C.F.R. 54.719(a) and 54.720(b) Nemont Telephone Cooperative, Inc. and Project Telephone Company ("Nemont") hereby appeal the decision of the Administrator of March 1, 2013 with respect to the above captioned audit (a copy of which is attached).¹ In its decision the Administrator determined to recover \$256,852 of previously disbursed High Cost Program support. Nemont asserts that the Administrator's decision is in error in that the proper resolution of the two accounting issues identified in the audit, and referenced below, should not have been total elimination of the support amounts.

First, the Administrator determined to recover \$155,507 of previously paid support because it concluded that Nemont had not properly documented the allocation of materials and supplies among the affiliated companies in the approved manner and rejected the alternative documentation provided. This decision effectively reached the conclusion that no amount of materials and supplies were properly included in the costs of providing the supported services despite the obvious fact that such materials and supplies were demonstrably so used. Because Nemont could not produce the documentation requested by the auditors, we believe that the proper, and completely acceptable under Generally Accepted Government Accounting Standards (GAGAS), response would have been to utilize alternative audit procedures. For example, the auditors could have utilized the relative plant under construction or the relative amount of plant closed into service of the four affiliated companies to determine if the allocations were reasonable or to determine a more reasonable allocation.

¹ Section 54.719 establishes a right to seek review from the appropriate Board Committee by persons aggrieved by "a division of the Administrator." The March 1 letter was signed only "Universal Service Administrative Company" and carried the heading "Administrator's Decision on High Cost Program Beneficiary Appeal." Nemont is proceeding on the assumption that the right to seek review of a division decision includes the right to seek review of a decision labeled "Administrator."

In its findings letter dated September 12, 2011 titled *Independent Auditor's Report on Nemont Telephone Cooperative, Inc. and Project Telephone Company's Compliance with High Cost Support Mechanism Rules (USAC Audit No. HC2009BE001) (Findings Letter)*, USAC stated the following:

1. "We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States (2007 Revision, as amended), with the exception of the scope limitation identified in Audit Finding #8."²
2. "USAC is required to conduct audits in accordance with GAGAS, which specifies that auditors obtain sufficient, appropriate evidence to substantiate audit findings and conclusions."³

What was not mentioned in the Findings Letter is the fact that alternative audit procedures are allowed under GAGAS^{4/5} and may be used by auditors to achieve the intent of the audit requirement. Alternative audit procedures have previously been utilized by USAC and/or independent audit firms in the context of audits of high cost beneficiaries that could not produce continuing property records to support their investment in plant. In these cases, where the auditors had disclaimed the entire amount due to lack of documentation, it is our understanding that in the past, the FCC has directed USAC to require the independent auditors involved in these audits to implement alternative audit procedures to express an opinion on the reasonableness of the investment in plant. Doing so ensured that at least a portion of the investment in plant was included in the calculation of support when it could reasonably be determined that the investment had been made. USAC's extensive experience with rural telephone companies should have provided the auditors with the expertise to exercise reasonable judgment as to whether the companies' allocation or some other allocation was proper, and that the allocation could not be zero.

Second, the Administrator decided to recover \$8,897 because Nemont recorded some expenses in years other than those in which they were incurred. Pole rental expenses for 2005 were recorded in 2006 while pole rental expenses for 2006 were recorded in 2007. The variance between the 2005 and 2006 expenses were nominal, as communicated by Nemont

² See Findings Letter dated September 12, 2011, Page 1.

³ See Findings Letter dated September 12, 2011, Page 23.

⁴ *Government Auditing Standards*, GAO-07-162, Section 2.16 (2007 revision, as amended), "In rare circumstances, auditors and audit organizations may determine it necessary to depart from a relevant presumptively mandatory requirement. In such rare circumstances, auditors should perform alternative procedures to achieve the intent of that requirement. The need for the auditors to depart from a relevant presumptively mandatory requirement is expected to arise only when the requirement is for a specific procedure to be performed and, in the specific circumstances of the audit, that procedure would be ineffective in achieving the intent of the requirement."

⁵ *Government Auditing Standards*, GAO-07-162, Section 7.40 (2007 revision, as amended), "If auditors believe that it is likely that sufficient, appropriate evidence will not be available, they may revise the audit objectives or modify the scope and methodology and determine alternative procedures to obtain additional evidence or other forms of evidence to address the current audit objectives."

in its response to the audit findings. As a result, the amount recorded as expense in 2006 was very similar to the amount actually associated with 2006. The Administrator elected to eliminate the entire expense, rather than to adjust the expense to the amount associated with 2006 pole rental expense. Nemont acknowledges these errors but contends that they are not material to the financial statements of the company. If these types of errors were discovered in the context of an audit by an independent audit firm, they likely would not be deemed material or result in revisions to the financial statements. Even if revisions were made to the financial statements, the adjustment would be for the variance between actual 2005 and 2006 pole rental expense; it would not result in a complete elimination of the expense.

Nemont fully accepts its responsibility to correctly record its expenses and investments and understands USAC's responsibility to ensure that support payments are made only where such investments and expenses were actually incurred in providing supported services. Nemont has revised its practices to ensure that the errors noted in the audit do not occur in the future.

However in those cases where there are recording errors, but the actual expenses and investments can be readily ascertained by an auditor, the remedy most consistent with the objectives of Section 254 of the Communications Act is to adjust the recorded information to the correct levels and locations, rather than assume that the costs were not actually incurred.

In consideration of the foregoing, Nemont respectfully requests that the Administrator be directed not to recover the full amount of previously disbursed funds, but to limit such recovery only to those amounts uncontested.

Sincerely,



Remi Sun
Chief Financial Officer

Attachment

Verification

I, Remi Sun, declare under penalty of perjury that I have read the foregoing Appeal of Nemont Telephone Cooperative, et al., that I have personal knowledge of the facts set forth therein and I believe them to be true and correct.



Remi Sun
Chief Financial Officer
April 30, 2013



Administrator's Decision on High Cost Program Beneficiary Appeal

Via Email and Certified Mail

March 1, 2013

Aimee Dietrich
Controller
Nemont Telephone Cooperative, Inc.
61 Hwy 13 S
PO Box 600
Scobey, MT 59263-0600

Re: Appeal of the FCC Office of Inspector General USF Audit Program Audits of High Cost Program Beneficiaries: Nemont Telephone Cooperative, Inc. and Project Telephone Company (SAC 482247 and 482250), Audit HC-2009-001

Dear Ms. Dietrich:

The Universal Service Administrative Company (USAC) has reviewed the appeal you filed on behalf of Nemont Telephone Cooperative, Inc. ("Nemont") and Project Telephone Company ("Project"), dated January 20, 2012, concerning USAC's decision to recover \$256,892 in High Cost Program support disbursed for the 2008 program year. The amount to be recovered was determined by audits of Nemont and Project conducted under the FCC Office of Inspector General (OIG) Universal Service Fund (USF) Audit Program. Nemont appealed USAC's determination that cost study adjustments lacked adequate documentation, engineering charges were booked in the wrong account, and expense amounts were recorded in the wrong year.¹

Decision on Appeal: Denied. USAC has determined that \$226,205 of previously disbursed High Cost Program support should be recovered.

Background and Discussion

HC2009BE001-F01 – Lack of Documentation

Nemont appeals the finding HC2009BE001-F01 stating that due to poor communication with USAC Internal Audit Division (IAD) staff at the time of the audit Nemont was unable to provide an explanation of the different warehouse storage and inventory

¹ Letter from Aimee Dietrich, Controller, Nemont, Telephone Cooperative, Inc. and Project Telephone Company to the High Cost and Low Income Division of the Universal Service Administrative Company, dated Jan. 20, 2012, page 1 (*January 20 Letter*).

methods used in its reconciliation.² In the appeal letter, Nemont included supplementary records to reconcile the inventory to the general ledger. The documentation provided by the carrier approximates the amounts recorded for the time period audited. While the amounts provided are close to the original, the carrier has not explained the original calculations that established the inventory levels for both the Nemont and Project companies for the time period audited.³ Essentially, the original calculations cannot be justified because the company did not maintain adequate documentation to ensure the allocation methodology was compliant with 47 C.F.R. § 32.12.⁴ USAC hereby denies this appeal of the finding and will recover \$155,707 of previously paid support.

HC2009BE001-F02 – Improper Charges to Telecommunications Plant in Service

Nemont's accounting procedures charged engineering costs to account 2423. FCC regulations state that account 2423 should contain only the costs of buried cable and material associated with the construction of such plant as stated in 47 C.F.R. § 32.2423.⁵ In its appeal, Nemont reiterates its stance outlined in the beneficiary's response included in the audit report.⁶ In that response, Nemont agrees that the engineering expense was improperly recorded, however the amount of support it would have received would be approximately the same over the life of the asset.⁷ In the appeal letter, Nemont does not provide any new documentation or supporting arguments, therefore USAC maintains the audit finding's recommendation, and hereby denies the appeal of the finding and will recover \$61,601.⁸

² January 20 Letter, page 2.

³ January 20 Letter, page 2.

⁴ 47 C.F.R. § 32.12 (“(a) The company's financial records shall be kept in accordance with generally accepted accounting principles to the extent permitted by this system of accounts.(b) The company's financial records shall be kept with sufficient particularity to show fully the facts pertaining to all entries in these accounts. The detail records shall be filed in such manner as to be readily accessible for examination by representatives of this Commission.(c) The Commission shall require a company to maintain financial and other subsidiary records in such a manner that specific information, of a type not warranting disclosure as an account or subaccount, will be readily available. When this occurs, or where the full information is not otherwise recorded in the general books, the subsidiary records shall be maintained in sufficient detail to facilitate the reporting of the required specific information. The subsidiary records, in which the full details are shown, shall be sufficiently referenced to permit ready identification and examination by representatives of this Commission.”).

⁵47 C.F.R. § 32.2423 (“Buried cable. (a) This account shall include the original cost of buried cable as well as the cost of other material used in the construction of such plant. This account shall also include the cost of trenching for and burying cable run in conduit not classifiable to Account 2441, Conduit Systems. Subsidiary record categories, as defined below, are to be maintained for nonmetallic buried cable and metallic buried cable. (1) Nonmetallic cable. This subsidiary record category shall include the original cost of optical fiber cable and other associated material used in constructing a physical path for the transmission of telecommunications signals. (2) Metallic cable. This subsidiary record category shall include the original cost of single or paired conductor cable, wire and other associated material used in constructing a physical path for the transmission of telecommunications signals.(b) The cost of pumping water out of manholes and of cleaning manholes and ducts in connection with construction work and the cost of permits and privileges for the construction of cable and wire facilities shall be included in the account chargeable with such construction.”).

⁶ January 20 letter, page 9.

⁷ High Cost Beneficiary Report No. HC-2009-001 from USAC to Nemont Telephone Cooperative, Inc. and Project Telephone Company dated September 12, 2011, page 9 (*Nemont Audit Report*).

⁸ *Nemont Audit Report*, page 9.

HC2009BE001-F04 – Improper Expense Amounts

Nemont states that better communication with IAD staff would have clarified the company's accounting was consistent with its established expense accounting procedures. The carrier contends that the issue does not impact their financial records and is related to compliance to accrual accounting processes.⁹ Nemont supplemented their appeal with a copy of the 2007 payment for the expenses incurred in 2006 as well as the 2006 payment for the expenses incurred in 2005.¹⁰ As a result of comparing the two invoices, Nemont asserts its filings understated the expense by only \$1,554 and the recovery amount is inappropriate.¹¹ In order for USAC to audit the support received by the beneficiary, it is the responsibility of the beneficiary to accurately report the amounts in each account, as required by 47 C.F.R. § 54.301(b).¹² In this audit, the financial period under consideration was 2006. Nemont's inclusion of expenses occurring in years other than 2006 resulted in improper amounts being reported in the expense account. USAC hereby denies the appeal of this finding and will recover \$8,897.

USAC Action and Nemont Appeal Rights

USAC hereby denies Nemont's appeal and will recover \$256,852¹³ of previously disbursed High Cost Program support within 60 days of the receipt of this decision through the monthly disbursement process. If the recovery amount exceeds the current month's disbursement, USAC will continue to net the recovery amount against subsequent monthly disbursements. USAC may in its discretion and at anytime issue an invoice for all or a portion of the amount to be recovered. If any further errors are found in any of Nemont's reporting for the period under data validation herein, USAC reserves the right to recover the financial impact of those deviations.

If you wish to further appeal this decision, you may file an appeal pursuant to the requirements of 47 C.F.R. Part 54, Subpart I. Detailed instructions for filing appeals are available at:

<http://www.usac.org/hc/about/program-integrity/appeals.aspx>

//s// Universal Service Administrative Company

⁹ January 20 Letter, page 11.

¹⁰ January 20 Letter, 'Invoice Support' appendix.

¹¹ January 20 Letter, page 11.

¹² 47 C.F.R. § 54.301(b) ("Submission of data to the Administrator. Until October 1, 2011, each incumbent local exchange carrier that has been designated an eligible telecommunications carrier and that serves a study area with 50,000 or fewer access lines shall, for each study area, provide the Administrator with the projected total unseparated dollar amount assigned to each account listed below for the calendar year following each filing. This information must be provided to the Administrator no later than October 1 of each year. The Administrator shall use this information to calculate the projected annual unseparated local switching revenue requirement pursuant to paragraph (d) of this section.")

¹³ \$30,647 unappealed support + \$226,205 appealed support.