



Audit Committee Meeting

Briefing Book

Monday, October 29, 2018

8:00 a.m. - 9:30 a.m. Eastern Times

Universal Service Administrative Company Offices

700 12th Street, NW, Suite 900

Washington, DC, 20005

**Universal Service Administrative Company
Audit Committee Quarterly Meeting
Agenda**

**Monday, October 29, 2018
8:00 a.m. – 9:45 a.m. Eastern Time
USAC Offices
700 12th Street, N.W., Suite 900
Washington, D.C. 20005**

<u>OPEN SESSION</u>		<i>Estimated Duration in Minutes</i>
Chair	a1. Consent Items (each available for discussion upon request): A. Approval of Audit Committee Meeting Minutes of July 23, 2018. B. Approval of moving all <i>Executive Session</i> items into <i>Executive Session</i> .	5
Teleshia	a2. Cadence of Annual Audit Committee Reports and 4 th Quarter 2018 Audit Committee Reports	20
Teleshia	A. Acceptance of the Annual Assessment of the Independence and Financial Literacy of USAC Audit Committee Members	
Chris	B. Annual Review of the Effectiveness of USAC’s Process to Assess and Minimize Significant Risks	
Charlie	C. USAC’s Financial Reporting Process	
Teleshia	i1. USAC Audit and Assurance Division Business Update	15

<u>EXECUTIVE SESSION</u>		
Confidential – Executive Session Recommended		
Pauline	i2. USAC Audit and Assurance Division Business Update (<i>Continued</i>)	10
Teleshia	a3. Annual Review of the Audit and Assurance Division Charter and Operations of the Audit and Assurance Division	15
Lisa	a4. Action on One Rural Health Care Office of Management and Budget (OMB) Circular A-123 Internal Controls Review Report	10
Teleshia	i3. Executive Session with USAC’s Vice President of Audit and Assurance	10
Chair	i4. Executive Session -- Audit Committee Only	20

Next Scheduled USAC Audit Committee Meeting

**Monday, January 28, 2019
8:00 a.m. – 9:30 a.m.
USAC Offices, Washington, D.C.**

**Universal Service Administrative Company
Audit Committee Meeting**

ACTION ITEM

Consent Items

Action Requested

The Audit Committee (Committee) is requested to approve the consent items listed below.

Discussion

The Committee is requested to approve the following items using the consent resolutions below:

- A. Approval of Committee meeting minutes of July 23, 2018 (*see Attachment A*).
- B. Approval for discussing in *Executive Session* agenda items:
 - (1) **i2** – USAC Audit and Assurance Division Business Update (*Continued*). USAC management recommends that this matter be discussed in Executive Session because this matter relates to *specific internal controls, and/or confidential company data* that would constitute a discussion of internal rules and procedures.
 - (2) **a3** – Annual Review of the Audit and Assurance Division Charter and Operations of the Audit and Assurance Division. USAC management recommends that this matter be discussed in *Executive Session* because this matter relates to *specific internal controls, and/or confidential company data* that would constitute a discussion of internal rules and procedures.
 - (3) **a4** – Action on One Rural Health Care Office of Management and Budget (OMB) Circular A-123 Internal Controls Review Report. USAC management recommends that this matter be discussed in Executive Session because this matter relates to *specific internal controls, and/or confidential company data* that would constitute a discussion of internal rules and procedures.
 - (4) **i3** – Audit Committee Executive Session with USAC’s Vice President of Audit and Assurance. USAC management recommends that this matter be discussed in *Executive Session* pursuant to the guidelines in the approved Audit Committee Charter.
 - (5) **i4** – Executive Session with Audit Committee (only). USAC management recommends that this matter be discussed in *Executive Session* pursuant to the guidelines in the approved Audit Committee Charter.

Upon request of a Committee member any one or more of the above items are available for discussion by the Committee.

Recommended USAC Audit Committee Action

APPROVAL OF THE FOLLOWING RESOLUTION:

RESOLVED, that the USAC Audit Committee hereby approves:
(1) the Committee meeting minutes of July 23, 2018; and (2) discussion in *Executive Session* of the items noted above.

**UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
700 12th Street, N.W., Suite 900
Washington, D.C. 20005**

**AUDIT COMMITTEE MEETING
Monday, July 23, 2018**

(DRAFT) MINUTES¹

The quarterly meeting of the Audit Committee (Committee) of the USAC Board of Directors (Board) was held at USAC’s offices in Washington, D.C. on Monday, July 23, 2018. Mr. Geoff Feiss, Committee Chair, called the meeting to order at 8:00 a.m. Eastern Time, with all five Committee members present:

Choroser, Beth	Tinic, Atilla – Vice Chair
Feiss, Geoff – Chair	Wibberly, Dr. Kathy
Gillan, Joe	

Other Board members and officers of the corporation present:

Beckford, Ernesto – Vice President, General Counsel and Assistant Secretary
Beyerhelm, Chris – Vice President of Enterprise Portfolio Management
Bocher, Bob – Member of the Board
Davis, Craig – Vice President of Procurement and Strategic Sourcing
Garber, Michelle – Vice President of Lifeline
Holstein, Bob – Vice President and Chief Information Officer
Kinser, Cynthia – Member of the Board – *by telephone*
Lubin, Joel – Member of the Board
Salvator, Charles – Vice President of Finance, Chief Financial Officer and Assistant Treasurer
Scott, Wayne – Vice President of Internal Audit
Sekar, Radha – Chief Executive Officer
Sweeney, Mark – Vice President of Rural Health Care
Wein, Olivia – Member of the Board

Others present:

<u>NAME</u>	<u>COMPANY</u>
Anderson, Jarnice	USAC
Anderson, Latoya	USAC
Ayer, Catriona	USAC
Carpenter, Nikki-Blair	USAC

¹ Draft resolutions were presented to the Committee prior to the Committee meeting. Where appropriate, non-substantive changes have been made to the resolutions set forth herein to clarify language where necessary or to correct grammatical or spelling errors.

<u>NAME</u>	<u>COMPANY</u>
Delmar, Teleshia	USAC
Francisco, Dale	USAC
Gelman, Sheryl	USAC
Goode, Vernell	USAC
Haus, Allen	Avitecture
Hawkins, Crystal	USAC
Huynh, Linh	USAC
King, Lauren	USAC
Leonard, Tom	PwC
Nuzzo, Patsy	USAC
Richardson, Rashonda	USAC
Smith, Chris	USAC
Smith, Porchia	USAC
Tawes, Pauline	USAC
Tomlin, Nicole	USAC
Tuistra, Jason	PwC

OPEN SESSION

All materials from Open Session can be found on the [USAC website](#).

a1. Consent Items. Mr. Feiss presented these items to the Committee and requested the addition of item i4 for discussion in *Executive Session* with only Board members present.

A. Approval of Committee meeting minutes of April 23, 2018.

B. Approval for discussing in *Executive Session* agenda items:

(1) **i2.** – USAC Internal Audit Division Business Update. (*Continued*)
USAC management recommends that this matter be discussed in Executive Session because this matter relates to USAC’s *internal personnel matters*.

(2) **a2** – Acceptance of USAC’s 2017 Annual Financial Audit and Agreed-Upon Procedures Review. USAC management recommends that this matter be discussed in *Executive Session* because the basis to support the changes relate to *specific internal controls, and/or confidential company data* that would constitute a discussion of internal rules and procedures.

(3) **a3** – Consideration of Contract Amendment for Procurement and Compensation Audits. USAC management recommends that this matter be discussed in Executive Session because this matter relates to USAC’s *procurement strategy and contract administration*.

- (4) **i3** – Audit Committee Executive Session with USAC’s Independent Audit Firm. USAC management recommends that this matter be discussed in *Executive Session* pursuant to the guidelines in the approved Audit Committee Charter.
- (5) **i4.** – Audit Committee and Board members in Executive Session. USAC management recommends that this matter be discussed in *Executive Session* pursuant to the guidelines in the approved Audit Committee Charter.

On a motion duly made and seconded and after discussion, the Committee adopted the following resolution:

RESOLVED, that the USAC Audit Committee hereby approves: (1) the Committee meeting minutes of April 23, 2018; and (2) discussion in *Executive Session* of the items noted above.

- i1. USAC Internal Audit Division Business Update.** Mr. Scott presented this item to the Committee for discussion. Mr. Scott provided an update on the Beneficiary and Contributor Audit Program (BCAP) and Payment Quality Assurance (PQA) audits, and reviewed the results of the post audit surveys.

At 8:48 a.m. Eastern Time, on a motion duly made and seconded, the Committee moved into *Executive Session* for the purpose of discussing the confidential items noted above.

EXECUTIVE SESSION

- i2. USAC Internal Audit Division Business Update (Continued).** Mr. Scott continued his report and provided an update on the division’s employee engagement activities.
- a2. Acceptance of USAC’s 2017 Annual Financial Audit and Agreed-Upon Procedures Review.** Mr. Scott introduced Mr. Leonard and Mr. Tuistra to present the results of the 2017 Annual Financial Audit and Agreed-Upon Procedures Review conducted by PwC.

On a motion duly made and seconded and after discussion, the Committee adopted the following resolution:

RESOLVED, that the USAC Audit Committee, having reviewed the USAC 2017 Financial Audit Report as submitted by PricewaterhouseCoopers LLP, hereby deems the report final; and

RESOLVED FURTHER, that the USAC Audit Committee, having reviewed the USAC 2017 Agreed-Upon Procedures Review Report as submitted by PricewaterhouseCoopers LLP, hereby deems such report final.

a3. Consideration of Contract Amendment for Procurement and Compensation Audits. Mr. Scott presented this item to the Committee for consideration.

On a motion duly made and seconded and after discussion, with Mr. Gillan voting no, the Committee adopted the following resolution:

RESOLVED, that the USAC Audit Committee, having reviewed the recommendation of USAC management, hereby authorizes management increase the award to Crowe Horwath LLP in the amount of \$5,700.

At 9:05 a.m. Eastern Time, the meeting continued in *Executive Session* with only members of the Board and PricewaterhouseCoopers, LLP present for the purpose of discussing item i2.

i3. Audit Committee Executive Session with USAC's Independent Audit Firm – PricewaterhouseCoopers LLP. Mr. Feiss and the Audit Committee discussed this item.

At 9:25 a.m. Eastern Time, on a motion duly made and seconded, the Committee continued in *Executive Session* with only members of the Committee and Board present to discuss item i4.

i4. Audit Committee Executive Session with Committee and Board members only. Mr. Feiss and the Audit Committee discussed this item.

At 9:48 a.m. Eastern Time, the Committee moved out of *Executive Session* and immediately reconvened in *Open Session*, at which time Mr. Feiss reported that, in *Executive Session*, the Committee took action on items a2 and a3 and discussed items i2, i3, and i4.

On a motion duly made and seconded, the Committee adjourned at 9:48 a.m. Eastern Time.

/s/ Ernesto Beckford
Assistant Secretary

Universal Service Administrative Company Audit Committee Meeting

ACTION ITEM – *Executive Session Option*

Action on the Cadence of Annual Audit Committee Reports and 4th Quarter 2018 Audit Committee Reports

Action Requested

The Audit Committee (Committee) of the USAC Board of Directors (Board) is requested to review and approve the cadence for annual Committee reports, as required by the Audit Committee Charter (Charter). The Committee is also requested to review and approve the 4th Quarter Committee reports that are listed in **Attachments A, B, and C** to this briefing paper.

Discussion

Cadence of Reports for Committee Approval. In accordance with the Charter, the Committee shall provide assistance to the Board in fulfilling the Board's oversight responsibilities relating to corporate accounting, financial reporting practices, internal control, Universal Service Fund program integrity, enterprise risk management, and all aspects of corporate compliance with applicable law. The table below outlines the cadence of when USAC Management will present specific reports to the Committee for approval to assist the Committee fulfill its oversight responsibilities:

Annual Cadence of Reports Presented to the Audit Committee	1 st Qtr.	2 nd Qtr.	3 rd Qtr.	4 th Qtr.
Corporate Assurance Audit Plan	✓			
FCC's Financial Statement Audit Report *	✓			
FCC's Report on Internal Controls *	✓			
FCC's Compliance with Laws and Regulations *	✓			
Audit Committee Charter		✓		
USAC's Process to Comply with Laws and Regulations		✓		
USAC's System of Internal Controls			✓	
USAC's Financial Reporting Process +			✓	
USAC's Financial Statement Audit and Agreed Upon Procedures Review and Executive Session with Audit Firm			✓	

* Agenda item will be included for informational purposes only (i.e., non-voting item).

+ Agenda item will be presented at this 4th Quarter 2018 Committee meeting, as it has not yet been presented to the Committee in 2018. Going forward, USAC will present this agenda item at the 3rd Quarter Committee meeting.

Annual Cadence of Reports Presented to the Audit Committee	1 st Qtr.	2 nd Qtr.	3 rd Qtr.	4 th Qtr.
Independence and Financial Literacy of Audit Committee Members				✓
Audit and Assurance Division Charter ++				✓
USAC’s Process for Assessing & Minimizing Risks				✓
Peer Review (every 3 years)				✓

Fourth Quarter Committee Reports. The Committee is also requested to review the 4th Quarter Committee reports as summarized below:

Independence and Financial Literacy of Audit Committee Members. In accordance with the Charter, the Committee is required to assess the independence and financial literacy of its members to ensure that the Committee can adequately fulfill its roles and responsibilities. The Acceptance of the Annual Assessment of the Independence and Financial Literacy of USAC Audit Committee Members is included as **Attachment A** to this briefing paper.

USAC’s Process for Assessing & Minimizing Risks. In accordance with the Charter, the Committee is required to review the effectiveness of USAC’s process for assessing significant risks and exposures (collectively, risks), and the steps management has taken to minimize such risks. The Annual Review of the Effectiveness of USAC’s Process to Assess and Minimize Significant Risks is included as **Attachment B** to this briefing paper.

USAC’s Financial Reporting Process. In accordance with the Charter, the Committee is required to review USAC’s financial reporting process. USAC’s Financial Reporting Process is included as **Attachment C** to this briefing paper.

++ The Audit and Assurance Division Charter is being presented at the 4th Quarter Committee Meeting as Item a3.

Recommended USAC Audit Committee Action

APPROVAL OF THE FOLLOWING RESOLUTIONS:

RESOLVED, that the USAC Audit Committee, having reviewed the cadence for annual Committee reports as required by the Committee Charter, accepts the recommendation of USAC management to present said reports to the Committee in accordance with the frequency noted in the table above.

RESOLVED FURTHER, that the USAC Audit Committee accepts the assessment and agrees that the Audit Committee consists of independent members and that there is a sufficient level of financial expertise; and

RESOLVED FURTHER, that the USAC Audit Committee accepts the effectiveness of USAC's financial reporting process.

Attachment A

Acceptance of the Annual Assessment of the Independence and Financial Literacy of USAC Audit Committee Members

Action Requested

In accordance with the Audit Committee Charter, the Committee is required to assess the independence and financial literacy of its members to ensure that the Committee can adequately fulfill its roles and responsibilities. This issue paper documents the assessment of the Committee made by the USAC Audit and Assurance Division (AAD).

Discussion

The Charter requires that the Committee assess the independence and financial literacy of its members at least annually to verify that the Committee is independent and has a sufficient level of financial expertise to perform its duties.

The following is a summary of the Charter’s independence and financial literacy requirements and an assessment of each Committee member’s compliance with specific sections:

Audit Committee Charter (Section II, A1c, 2a-c)	Joseph Gillan	Geoff Feiss	Beth Choroser	Atilla Tinic	Kathy Wibberly
[The member] is not and has not been employed in an executive capacity by the Company for at least five years prior to appointment to the Audit Committee.	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
[The member] is not an advisor or consultant to the Company, and does not have a personal services contract or other business relationship with the Company.*	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>

Audit Committee Charter (Section II, A1c, 2a-c)	Joseph Gillan	Geoff Feiss	Beth Choroser	Atilla Tinic	Kathy Wibberly
[The member] is not a spouse, parent, sibling, child, or in-law of any person described in the preceding two clauses of this paragraph or of any member of the management of the Company.	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
At least one member shall have a background in financial reporting, accounting, or auditing, or other financial expertise.	<i>Yes</i>	<i>No</i>	<i>Yes</i>	<i>Yes</i>	<i>No</i>
<i>*NOTE: None of the members of the Audit Committee have a consulting arrangement or contractual business relationship with USAC. Members may be employees of companies or entities that contribute to and/or receive funds from the Universal Service Fund (USF).</i>					

The financial proficiency shown by Mr. Joseph Gillan, Ms. Choroser, and Mr. Atilla Tinic is experience acquired during their professional careers.

- Mr. Gillan is an economist with extensive experience evaluating financial implications of technological change and regulatory policy in the telecommunications industry. Mr. Gillan has provided expert testimony in over 300 proceedings. Mr. Gillan was previously employed on the staff of the Illinois Commerce Commission as the Director of Market Structure, where he oversaw Commission policies that encouraged competition in the electric, gas and telecommunications industries.
- In addition to holding an MBA from Syracuse University, which included significant course work in accounting and finance, Ms. Choroser has significant experience in budgeting and establishing tariffs in the utility industry. Specifically, in the telecommunication industry, Ms. Choroser has experience with telecommunications tax and surcharge filings, including the preparation of the FCC Form 499-A.
- Mr. Tinic is Vice President of Information Technology (IT) for Level 3 Communications, Inc., where he is responsible for Business and Customer Support Systems (BCIlaSS). Mr. Tinic has worked in information and communication technology for over 20 years and has a long track record of deploying new and innovative solutions. Before assuming his current role, Mr. Tinic was Vice President of IT for tw telecom, inc. (tw telecom), where he lead all

functions around business support systems. Mr. Tinic was also responsible for revenue assurance and billing operations for 10 years while at tw telecom. In this role, he worked closely with the Controller and Chief Accounting Officer by managing internal controls that were subject to Sarbanes-Oxley (SOX) testing and reporting in conjunction with internal and external auditors. His significant experience in billing and financial systems provides a solid basis for understanding financial reporting and accounting controls.

The professional backgrounds noted above provide the Committee with adequate financial, telecommunications, and regulatory experience to sufficiently fulfill Committee roles and responsibilities. AAD has concluded that the members of the Committee as a whole fulfill the requirements for independence and financial literacy required by the Charter and recommends that the Committee accept this assessment.

Attachment B
Annual Review of the Effectiveness of USAC’s Process to Assess and Minimize Significant Risks

Background

In accordance with the Audit Committee Charter, USAC management must evaluate the effectiveness of its process for assessing significant risks and exposures (collectively, risks) and the steps management has taken to minimize such risks.¹ The purpose of this paper is to describe how the organization plans to pivot from an audit-driven approach to risk management to a more holistic and proactive approach to risk management, and to evaluate the effectiveness of USAC management’s risk assessment process.

Risk management is the process of identifying and analyzing risks that affect the achievement of company objectives, and having controls in place to identify and mitigate significant risks

Historically, risk portfolios have been managed within separate lines of business, creating silos of activity like business risk, financial risk, and operational risk. However, regulatory requirements, accounting rules changes, and an evolving economic environment are encouraging compliance, financial, and operational risk stakeholders to collaborate across organizations. Organizations are now integrating portfolio strategies with other lines of business that affect the overall risk of the organization in a discipline called Enterprise Risk Management (ERM).

ERM is a discipline embraced by the organization that identifies risks from a broad scope and as an interrelated portfolio. The USAC Enterprise Portfolio Management Office (EPMO) team manages the ERM governance mechanisms that provide all inputs, including a comprehensive audit component, required for USAC management to make informed decisions for proper governance and the benefit of key operational initiatives.

USAC has adopted an “enterprise view” of risk management, which is a top-down mindset that has been embraced by each member of the Leadership team and within each of USAC’s business units.

¹ See USAC Audit Committee Charter, Section III, F., revised January 2018.

Risk Management Framework

In 2016, USAC created a cross-divisional ERM team that is now led by EPMO and includes members across all USAC programs and divisions. A primary focus of the ERM team is to identify the high risks that impact USAC’s key objectives/initiatives, address what is being done to mitigate those risks, and determine whether USAC is pursuing the most effective risk mitigation strategy. The ERM team assesses risk likelihood and impact on a monthly basis via internal risk registers and, on a quarterly basis, significant risks are escalated to the Risk Management Council (RMC). Risk discussions and related efforts are ongoing, and USAC will continue to engage the Audit Committee and the Board of Directors, as appropriate.

In 2018, USAC has made significant progress with maintaining and modifying the ERM program. As summarized below, USAC has established a redesigned framework to protect the Universal Service Fund. As part of this redesigned framework, we felt it important to have shared responsibilities and, therefore, shared accountability for the management of risk at USAC. To that end, the responsibilities defined in Office of Management and Budget (OMB) Circular No. A-123, Appendix A have been shifted to the Finance Division; program integrity has been made a greater responsibility of the program Vice Presidents; USAC has placed greater emphasis on compliance with the Federal Information Security Management Act (FISMA); and overall management of risk has been moved to the EPMO. *See Exhibit 1 – ERM/GRC Governance and Framework.*

Roles and Responsibilities

Organization	ERM Framework	Roles/Responsibilities	Frequency	Outputs/ Outcomes	Comments
Finance Division	<ul style="list-style-type: none"> • OMB Circular A-123 Appendix A 	<ul style="list-style-type: none"> • Testing the design and effectiveness of financial internal controls and providing oversight into the evaluation risks of meeting objectives • Performing risk assessment activities around key controls 	Per annual audit plan	<ul style="list-style-type: none"> • Determination of the risk level that can be minimized versus what is acceptable 	<ul style="list-style-type: none"> • OMB Circular A-123 Appendix A
Audit and Assurance Division (AAD)	<ul style="list-style-type: none"> • FCC Orders • OMB Circular A-123 Appendix C 	<ul style="list-style-type: none"> • Conducting audits to assess whether beneficiaries & contributors are compliant with FCC Directives. • Assessing USF disbursements to assess whether improper payments occurred 	Per annual audit plan	<ul style="list-style-type: none"> • Audit reports that discuss testing methodology, scope and conclusion • Provide oversight of external auditor’s assessment of USAC and the USF’s procedures for effectiveness 	<ul style="list-style-type: none"> • OMB Circular A-123 Appendix C

Organization	ERM Framework	Roles/Responsibilities	Frequency	Outputs/ Outcomes	Comments
Divisions		<ul style="list-style-type: none"> Taking proactive program integrity efforts to safeguard the USF from waste, fraud, and abuse 	All times	<ul style="list-style-type: none"> Meet one of USAC's objectives to reduce waste, fraud, and abuse 	
Information System Owners	<ul style="list-style-type: none"> FISMA 	<ul style="list-style-type: none"> Accepting the risk to USAC operations after implementing agreed-upon security controls as required by the Federal Information Security Act 	All times	<ul style="list-style-type: none"> Reduced levels of risks from technologies 	<ul style="list-style-type: none"> FISMA
EPMO	<ul style="list-style-type: none"> OMB A-123 	<ul style="list-style-type: none"> Responsible for the implementation and management of policies and procedures to guide the response to a perceived loss of mission capability Managing governance meetings (Leadership Council Meetings, Investment Review Board & Exception Meetings) to discuss company operations Tracking and managing all USAC corrective action plans (CAPs) 	All times	<ul style="list-style-type: none"> Reduced levels of risks as a result of governance and oversight Lead the Risk Management Council (RMC) Track and help manage the CAPs to completion 	
FCC Office of Inspector General	<ul style="list-style-type: none"> Oversight 	<ul style="list-style-type: none"> Ensures USF contributors and beneficiaries are compliant with FCC Directives Assesses USAC's compliance with rules and regulations 	As needed	<ul style="list-style-type: none"> Audit reports that discuss testing methodology, scope and conclusion Determination of USAC's level of compliance 	
Government Accounting Office	<ul style="list-style-type: none"> Oversight 	<ul style="list-style-type: none"> Evaluates USAC's internal control systems and effectiveness of reducing waste, fraud and abuse 	As needed	<ul style="list-style-type: none"> Assessment of USAC's internal control system and recommendations for improvement 	

Summary

USAC no longer approaches ERM strictly as an audit activity. Consequently, USAC has determined it important to rearrange the risk identification activities within the organization and centralize the collection of these results and the oversight of the activities. To that end, the risk related activities have been reassigned within the USAC organization. The risk management processes used by USAC are designed to provide a framework in which risks are continually identified, evaluated, and managed. The ERM team and RMC has further leveraged USAC's ability to effectively manage risks. The implementation of various governance structures has furthered efforts to identify, detect, and protect the organization from damaging risks proactively. Accordingly, for the reasons described herein, USAC management has established and maintained an effective process for assessing significant risks and taking steps to minimize such risks.

Audit Committee Meeting

aAC02B Acceptance of USAC's Enterprise Risk Management Framework

Exhibit 1: ERM/GRC Governance and Framework

October 29, 2018



Universal Service
Administrative Co.

ERM/GRC: Risk Management Governance Mechanisms

USAC has established multiple governance bodies to review and provide guidance on key outputs

Enterprise Portfolio Management Office

Manages the governance framework and provides all inputs required for leadership to make decisions for Program/Division Governance.

Leadership Council

- Provide status and coordination of Program/Division initiatives
- Create solutions for Program/Division roadblocks, challenges and risks

FISMA

- Provide status and coordination in FISMA initiatives
- Manage the assessment of FISMA activities

Exceptions Meeting

- Analyze metrics-based, goals-based and corrective action plan exceptions
- Identify cross-enterprise challenges and gain cross-functional support

Corrective Action Plan Management

- Manage the completion of corrective actions in collaboration with OGC
- Reduce risk and repeat findings

Risk Management Council

- Discuss risk incidents/matters and various audit testing results
- Advise on remediation of deficiencies and vulnerabilities

ERM/GRC: USAC's Framework to Protect the Universal Service Fund (USF)

Enterprise Risk Management & Governance Risk and Compliance

Audit & Assurance¹

Finance ¹

Programs ¹

Chief Information Security Officer ²

	Audit & Assurance ¹		Finance ¹		Programs ¹	Chief Information Security Officer ²	
Activity	Beneficiary & Contributor Audit Program Assessment of Beneficiary's and Contributor's compliance with USF rules	Payment Quality Assurance Assessment of disbursement of USF funds	Agreed Upon Procedures Audit Assessment of USAC and USF's procedures effectiveness	Internal Controls Testing Assessment of design & effectiveness of internal controls	Entity Level Assessment Evaluation of Enterprise's risks of meeting objectives	Program Integrity Proactive efforts made by the Programs to safeguard the USF from waste fraud and abuse	FISMA Evaluation Assessment of USAC's compliance with the National Institute of Standards and Technology – Risk Management Framework
Source	USF Orders	Office of Management & Budget A-123 Appendix C ³	47 C.F.R. Section 54.717 (Audits of the Administrator)	Office of Management & Budget A-123 Appendix A ⁴		USF Orders, Program reviews, Knowledge Management	Federal Information Security Management Act (FISMA)

¹ In coordination with OGC

² In conjunction with the OGC Director of Privacy

³ OMB Circular A-123 Appendix C – Requirements for Payment Integrity Improvement (Improper Payments Eliminations and Recovery Act of 2010 and Improper Payments Elimination and Recovery Improvement Act of 2012).

⁴ OMB Circular A-123 Appendix A – Management's Responsibility for Enterprise Risk Management and Internal Control.

ATTACHMENT C

USAC'S FINANCIAL REPORTING PROCESS

Overview

The Universal Service Administrative Company (USAC) is responsible for recording and reporting the financial activity for the Universal Service Fund (USF), including the four Universal Service Support Mechanisms: High Cost (HC); Lifeline (LI); Schools and Libraries (SL); and Rural Health Care (RHC). In addition, USAC is responsible for the accurate reporting of expenses and capital assets related to USAC's administrative operations, including but not limited to, the operational activity related to billing contributors, collecting billed amounts, and disbursing funds to authorized beneficiaries.

External Resources

USAC relies on the following external resources to provide financial-related support services:

- (1) In the second quarter of 2018, USAC's cash operations were transitioned to the U.S. Department of Treasury (Treasury). Upon transfer of funds to Treasury, further investments have ceased. Existing investments with maturity dates subsequent to transfer of funds to Treasury will be liquidated upon maturity and transferred to USAC's cash account with Treasury.
- (2) J.P. Morgan Chase performs cash management related to USAC's administrative expenses.

Financial Transactions

Financial transactions for RHC, HC, and LI, including support amount calculations and payment authorizations, are processed by USAC. The same financial transactions for SL are processed by external vendor Solix, Inc. (Solix) and reviewed by USAC. Transactions for USAC's administrative costs are processed by the USAC Finance Division. Administrative costs are allocated to the various USF Support Mechanisms in accordance with the cost allocation methodology (CAM) approved by the USAC Board of Directors and filed with the FCC.

Accounting Systems

USF financial data is maintained in the Microsoft Dynamics Great Plains-based accounting system (GP). The GP system is operated and maintained by the USAC Finance Division. USAC and USF accounting management and staff have read/write access to GP depending on their role. The USF and USAC general ledgers (GLs) are independent of each other.

Throughout this paper, reference is made to accounting staff posting to the GL in GP. Finance staff may record transactions and general journal entries to the subsidiary ledger, but only Finance management personnel may post journal entries to the GL. In specific instances, data uploaded between GP and other database systems (integrations) may be posted through to the GL

without accounting management personnel performing the posting. Other authorized USAC Finance Division team members have read-only access to the GP GL.

USF billing activity is processed and recorded in the in-house custom-designed Billing System managed by the Finance Division Director of Financial Operations. The billings activity is updated monthly. The transaction detail is transferred from the Billing System into the GP system through a custom-designed automated integration process, and data is accepted into GP only after a thorough review and reconciliation process has occurred, as further described below. USF collections activity is processed and recorded in GP. USAC's Information Technology (IT) Division operates the Billing System for the USAC Finance Division.

Disbursement activity is processed in the GP system from file load to generation of payment files. The Billing System feeds detail level transaction activity to the USF GP for billings to contributors and receivables transactions. The collections activity is updated in USF GP daily. The disbursements activity is updated twice weekly for SL, bi-monthly for RHC, and monthly for HC and LI.

GP contains the USF billed accounts receivable subsidiary ledger, the USF disbursements subsidiary ledger for all programs, the subsidiary ledgers for USAC accounts payable and fixed assets. No other USF-related subsidiary ledgers are maintained in GP.

USF Billing and Collections

USAC issues monthly invoices to USF contributors based on FCC Form 499 revenue information reported to USAC by telecommunications providers. The invoices are issued as of the 15th of each month and indicate total amounts owed. Monthly, the USF Finance Division Billing team performs a 100 percent quality assurance test to verify the accuracy of the monthly invoice calculations by performing independent calculations outside of the system for comparison to system results. The Finance Division Manager of Financial Operations reviews and approves the quality assurance tests for the invoices at a total batch level, not by individual invoices. Billings are recorded in the Billing System and uploaded to the GL in USF GP monthly through an automated integration process between the systems. On or about the 3rd business day following the 15th day of the month, the Billing team prepares the Pre GP Integration Totals Report. The report lists the billing amounts entered into the Billing System that are to be loaded into GP. The IT team integrates the billings from the Billing System into the GP GL via batch. Upon completion of the billings load to GP, the Billing team verifies that the totals loaded agree to the Pre-GP Integration Totals Report. If the amounts agree, the journal entries are posted through to the USF GP by the Billing Manager and a batch summary is prepared for the USF Accounting Manager to approve for the transaction. If the amounts do not agree, the Billing team notifies USAC IT staff of the error. Once the billings are loaded into USF GP, a Billing Manager applies invoices to individual USF contributor balances by utilizing the mass apply function in the USF GP. This function automatically applies billings, adjustments, and credits to contributor accounts.

Payments are remitted to USAC via Credit Card or Automated Clearing House (ACH) electronic transfer through USAC's online system (E-File) and Treasury's online payment system (Pay.gov). On a daily basis, Treasury sends to USAC a cash receipt file with all the payments received from the previous day. Upon receipt, USAC automatically uploads the cash receipt file into its collection processing system, where the payment data is reviewed and uploaded into GP. Once the payment data is in GP, the USAC Manager of Financial Operations conducts a final review and posts the payments in GP. Payments received are applied to USF contributor balances by utilizing the mass apply function in the USF GP, which automatically applies payments received to contributor balances. Payments are applied in accordance with the FCC's USF Comprehensive Report and Order, such that payments are applied first to outstanding penalty and administrative cost charges, next to accrued interest, and third to the outstanding principal of the oldest outstanding debt.¹ Upon Completion of Collections posting, a Processing Analyst sends an email to BCD Production FSDIT, stating that "The late payment interest charges and cash application processes are complete."

USF contributors that receive HC, LI, SL, or RHC benefits can elect to have funds netted against USF contributions. Consistent with the FCC's Red Light Rule, disbursements across all four programs are force netted against delinquent contributor balances to recover outstanding delinquent contribution amounts due.²

Cash and Investments

Per FCC instruction, USAC moved all Universal Service Funds to the U.S. Department of Treasury (Treasury) beginning in the second quarter of 2018. Upon transfer of funds to Treasury, USAC ceased new investments. Existing investments with maturity dates subsequent to transfer of funds to Treasury will be liquidated upon maturity and transferred to USAC's cash account with Treasury.

Interest earned on securities is applied to each program based on an investment allocation factor in place during that period. The investment allocation is based on the average amount of cash/investments attributed to the program during the period. A USF Accountant prepares investment schedules to identify the interest earned and changes in accrued amortization of accrued discounts/premiums. The investment schedules are utilized by a USF Accountant to prepare the monthly summary investment journal entries. These entries are entered manually into the USF GP and are reviewed and posted by the USF Accounting Manager.

The bank sends monthly statements of cash and investment activity to USAC. A USF Accountant prepares a reconciliation of bank transactions against the cash and investment activity reported by the USF. The reconciliation is reviewed and approved by the USF Accounting Manager. This process is also performed for USAC's administrative cash

¹ See *Comprehensive Review of the Universal Service Fund Management Administration, and Oversight et al.*, WC Docket Nos. 05-195 *et al.*, CC Docket Nos. 96-45 *et al.*, Report and Order, 22 FCC Rcd 16372, 16381, para. 16 (2007).

² See 47 C.F.R. § 1.1912(c).

transactions that are posted to the USAC GL. The reconciliation is reviewed and approved by the USAC Accounting Manager. If adjusting journal entries are needed, the USAC and USF Accountants prepare journal entries and the USF Accounting Manager reviews and approves the adjustments.

A USF Financial Analyst calculates the allowance for accounts that may be uncollectible based on the USF policies for the allowance for doubtful accounts. A USF Accountant records the amounts into GP following review and approval by the USF Accounting Manager.

USF Disbursements

Disbursements are subject to the FCC rules and orders governing each USF program. All disbursements are processed via ACH (Automated Clearing House). Each program approves its respective disbursements and submits payment file(s) to a secured designated network directory for uploading to GP for Finance to process payment.

A Disbursements Analyst verifies that the total amount and total number of line items in GP are consistent with programs' authorizations. Either the Manager of Accounting Operations or Senior Manager of Accounting Operations approves the Authorization Batch and GP Poster Master systematically posts the Authorization Batch through the GL in GP after batches are approved. The Disbursement Analyst then processes any adjustments and Red Light reconciliation systematically in GP. Next, the payment files are created. A quality control (QC) consolidation of the process is provided to the Senior Manager of Accounting Operations for review and approval. Subsequently, the Controller or Director of Financial Planning & Analysis (FP&A) and the Chief Financial Officer (CFO) shall perform additional review and provide authorization via email to release bank feeds. Only the Controller, Director of FP&A, and CFO are authorized to release the payment files securely through GP with their own unique access.

USF Accounting and Reporting

The USF general ledger and sub-ledgers are closed within eight business days following the end of the month for both reporting and non-reporting periods. Reporting periods are those periods in which USF financial statements are provided to the FCC. GL entries into the USF GP are made through system downloads (integrations) from the Billing System, as described above, and through manual journal entries.

The USF Accounting Team prepares and posts manual journal entries to the GL. Each of the Staff and Senior Accountants prepare a monthly reconciliation of the GL accounts for the module for which they are responsible. The USF modules are Accounts Receivable (AR), Accounts Payable (AP), cash and investments, and Federal budgetary accounting. Each reconciliation ties beginning balances for module GL accounts, plus both automated and manually entered activity for the period, to the ending GL account balances per the trial balance. The reconciliations are used to review the activity impacting all USF pam GL accounts and are signed by the responsible USF Accountant and the USF Accounting Manager.

The manual GL entry process has several layers of controls to help verify the completeness, existence, and accuracy of the recorded amounts. Staff Accountants prepare journal entries which are reviewed and posted by the USF Accounting Manager. The Staff Accountants also prepare monthly account reconciliations that are reviewed and approved by the USF Accounting Manager. A closing checklist is maintained to ensure that all entries are recorded. After all entries are recorded, the FCC-required financial reporting is reviewed and approved by the USF Accounting Manager and Controller.

Administrative Costs

The USAC Accounting Team enters the USAC administrative costs into the USAC GP on a daily basis. USAC administrative transactions include payroll, administrative AP, and depreciation and amortization. On a daily basis, the USAC cash management function tracks USAC's check and electronic payments to determine whether an adequate cash balance exists in the operating account to cover USAC's disbursement of funds. ACH disbursements are initiated online through JP Morgan, and the bank requires that one individual upload the Electronic Funds Transfer (EFT) payment file and that a second, independent individual must release the EFT payments. Checks can only be printed by another USAC AP staff member who is not processing the invoices. The system-generated check register with sequential check numbers corresponding to the payee and amounts are verified by the Controller before the check file is uploaded to JP Morgan for funds disbursement. Only registered users with access to the JP Morgan account have their own unique security key for transmitting EFTs and uploading check payment files. During month-end, the USAC Accounting Team prepare an accrual for AP by period of service and by vendor, and reverses the accrual once a transaction clears the AP account. The USAC Accounting Team may only originate an entry and only the USAC Accounting Manager may approve and post an entry to the GL.

On a monthly basis, USAC bills the USF for prior month cash expenditures. The resulting receivable and payable amount is recorded on the USAC and USF financial statements, respectively. The USAC Accounting Manager reviews and approves final entries before a USAC Senior Accountant records them in the GP, which USAC utilizes to generate monthly financial statements. The USAC general ledger and sub-ledgers are closed on a monthly basis within five business days following the end of the month, with the exception of 2 months, December & January. December remains open throughout the month of January to achieve accurate accounting for all prior year-end transactions. January closes soon after December is closed, which could be within nine business days following the end of the month. USAC Financial Statements are reviewed by the USAC Accounting Manager and the Controller. Reviewed statements are then sent to USAC Leadership and the FP&A team each month for further review and become the basis of the audited financial statements for the year. A USAC Senior Accountant manually prepares the cash flow statement from the data in GP.

Financial Planning & Analysis

Monthly, the FP&A team prepares a variance analysis of administrative costs for each division, comparing month and year-to-date actuals to the board approved budget. These variance

analyses are reviewed by the CFO before distribution to each division's VP and budget manager. A high level consolidated report is prepared for the CFO's review.

Audits

The USF is audited twice each year, in a financial statement audit and agreed-upon procedures (AUP) engagement. Further, an A-123 audit of the key controls for financial reporting is performed every three years. In addition, FCC auditors perform a financial statement audit because the USF is included in the FCC's consolidated financial statements. The FCC's and the USF's fiscal year-end is September 30. USAC is also required by the FCC to have an annual audit performed by an independent accounting firm (currently PricewaterhouseCoopers).³ The audit process includes the audit of USAC financial statements and extensive procedure and rule compliance testing through the AUP engagement for the USF. USAC's year-end is December 31.

³ See 47 C.F.R. § 54.717.

Universal Service Administrative Company Audit Committee Meeting

INFORMATION ITEM

USAC Audit and Assurance Division Business Update

Information Presented

This information paper provides an update on the status of audits and assurance activities performed by the USAC Audit and Assurance Division (AAD). The activities reported in this paper include the work performed in the Beneficiary and Contributor Audit Program (BCAP), the Payment Quality Assurance (PQA) program, and the Corporate Assurance function.

Each month, the Committee is provided with a report summarizing key activities and accomplishments within the division for the month, summarized by each of the key lines of business within the division (BCAP, PQA, and Corporate Assurance).

Beneficiary and Contributor Audit Program (BCAP)

The BCAP audits are designed to assess beneficiary and contributor compliance with the Federal Communications Commission (FCC) rules and requirements (collectively, FCC Rules). To demonstrate USAC's continued program integrity efforts and effective oversight of beneficiaries and contributors, USAC, in coordination with the FCC Office of Managing Director (OMD) and the FCC Wireline Competition Bureau (WCB), develop BCAP plans designed to:

- Assess beneficiaries' and contributors' compliance with FCC Rules;
- Identify correct contribution obligations (for contributor audits);
- Identify overpayments that must be recaptured (for beneficiary audits);
- Deter waste, fraud and abuse; and
- Identify FCC Rules that may require the attention of USAC or FCC management.

As a reminder, in 2013, USAC AAD and FCC OMD developed an audit plan for fiscal years 2014 and 2015 that was designed to select entities at random with the goal of concentrating on entities receiving larger federal Universal Service Fund (USF) disbursements. In 2015, USAC AAD, FCC OMD and FCC WCB developed audit plans for fiscal years 2016 to 2018 that were designed to focus audit resources on USF participants with the highest risk of noncompliance with FCC Rules.

USAC AAD, in consultation with FCC OMD and FCC WCB, are developing an audit plan for fiscal year 2019 that will incorporate a hybrid approach for selecting beneficiaries and contributors for audit. The selection methodology will be based on a combination of high risk factors, high dollar, random selection, and targeted entities selected as a result of whistleblower allegations, FCC or the USAC Board of Director's request. The BCAP plan is under development and will be presented to the Committee at the January 2019 quarterly meeting upon receiving FCC approval.

The BCAP audits are performed using AAD internal staff and resources from external audit firms that either: (i) work under USAC AAD's supervision in a co-source arrangement (i.e., staff augmentation) or (ii) perform audits without USAC AAD's direct supervision, but with USAC AAD project oversight. The combined status of all audits in process from each fiscal year plan is summarized in the table below.

**Audits in Process
As of September 30, 2018**

Audit Status					
Program	Announced	Fieldwork	Reporting	Audits in Process	Target Completion
CR	1	9	2	12	Jan 2020
HC	0	24	8	32	Apr 2019
LI	9	9	19	37	Aug 2019
SL	15	23	23	61	Aug 2019
RHC	0	3	4	7	May 2019
Total	25	68	56	149	

In addition, three external audit firms were engaged to perform Lifeline audits to support the Congressional Committee's and FCC Chairman Pai's requirements to identify waste, fraud and abuse by beneficiaries receiving Lifeline support. A majority of these audits have been announced, and work is in progress to ensure a consistent sampling methodology and testing approach is used by the external firms to address the testing requirements.

Each month, the Committee is provided with a report summarizing the BCAP audit reports that were completed in the prior month.

Payment Quality Assurance (PQA) Program

PQA is designed to assess the accuracy of Universal Service Fund (USF) disbursements and determine whether improper payments exist. The PQA team performs payment verification on a statistically valid sample of disbursements made in a calendar year. The PQA program also assists the FCC in meeting its reporting obligations under the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA).¹

¹ See The Improper Payments Elimination and Recovery Act of 2012, Pub L. No. 112 -248 (Jan. 10, 2013).

The table below provides the number of disbursements that were tested for calendar year 2017.

Assessments Completed

Program	Disbursement Sample Size
High Cost	309
Lifeline	365
Schools & Libraries	443
Total	1,117

AAD is working with the FCC on the fiscal year 2019 planning. This work includes selecting disbursement samples, as well as updating the PQA procedures for changes to FCC Rules and USAC processes, and coordinating with the FCC to determine whether these changes warrant a new baseline error rate for a Program.

The Rural Health Care Program will be included in the scope of the fiscal year 2019 PQA review due to an increased risk that the Program is potentially susceptible to significant improper payments. PQA testing for the Rural Health Care Program was performed for fiscal years 2011 to 2015. In fiscal year 2015, there were no improper payments identified from the PQA testing of the Program. As a result, the FCC determined that USAC did not need to conduct PQA testing to determine an improper payment rate for Rural Health Care Program disbursements for fiscal years 2016 to 2018. However, due to changes in the Program and the identification of improper payments in audits and other program integrity efforts, the Rural Health Care Program will be subject to PQA testing in fiscal year 2019. AAD has developed a plan to restructure the team and add additional resources to manage the increased workload.

Corporate Assurance

1. *USAC Procurement Process Audit.* USAC engaged the audit firm of Crowe Horwath LLP (Crowe Horwath) to perform an audit of USAC's procurement processes. The objective of the audit was to audit documentation and evaluate all related processes and internal controls, including all procurement activities from the request for services through payment of invoices for products and services. The draft audit report is with the FCC for review of management corrective actions.
2. *USAC Compensation Audit.* USAC engaged the audit firm of Crowe Horwath to perform an audit of USAC's compensation policies and procedures. The objective of the audit was to examine USAC's compensation policies, procedures and practices for officers and employees of the company, including both traditional and non-traditional employees. The draft audit report is with the FCC for review of management corrective actions.

3. *Internal Controls Review of the Rural Health Care Program.* AAD has completed its audit of the system of internal controls established for the Rural Health Care Program. The purpose of this review was to assess the design of the internal controls and to test the effectiveness of selected key controls with a medium to high risk rating. The audit report is included as agenda item aAC04cf 102918.

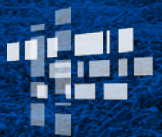
4. *Follow-up Reviews on High Cost Modernized Funds.* AAD has completed follow-up work in relation to four High Cost Program audits that were performed in 2017. Exit meetings were held with USAC management, who agreed with the findings and have identified corrective action plans to correct the deficiencies. The four areas that were examined were:
 - High Cost Operational Review
 - High Cost Universal Broadband (HUBB) Portal
 - High Cost Mobility Phase 1
 - High Cost CAF Phase 1, Round 1

Audit Committee Meeting

iAC01A Attachment A

Audit and Assurance Business Update

October 29, 2018



Universal Service
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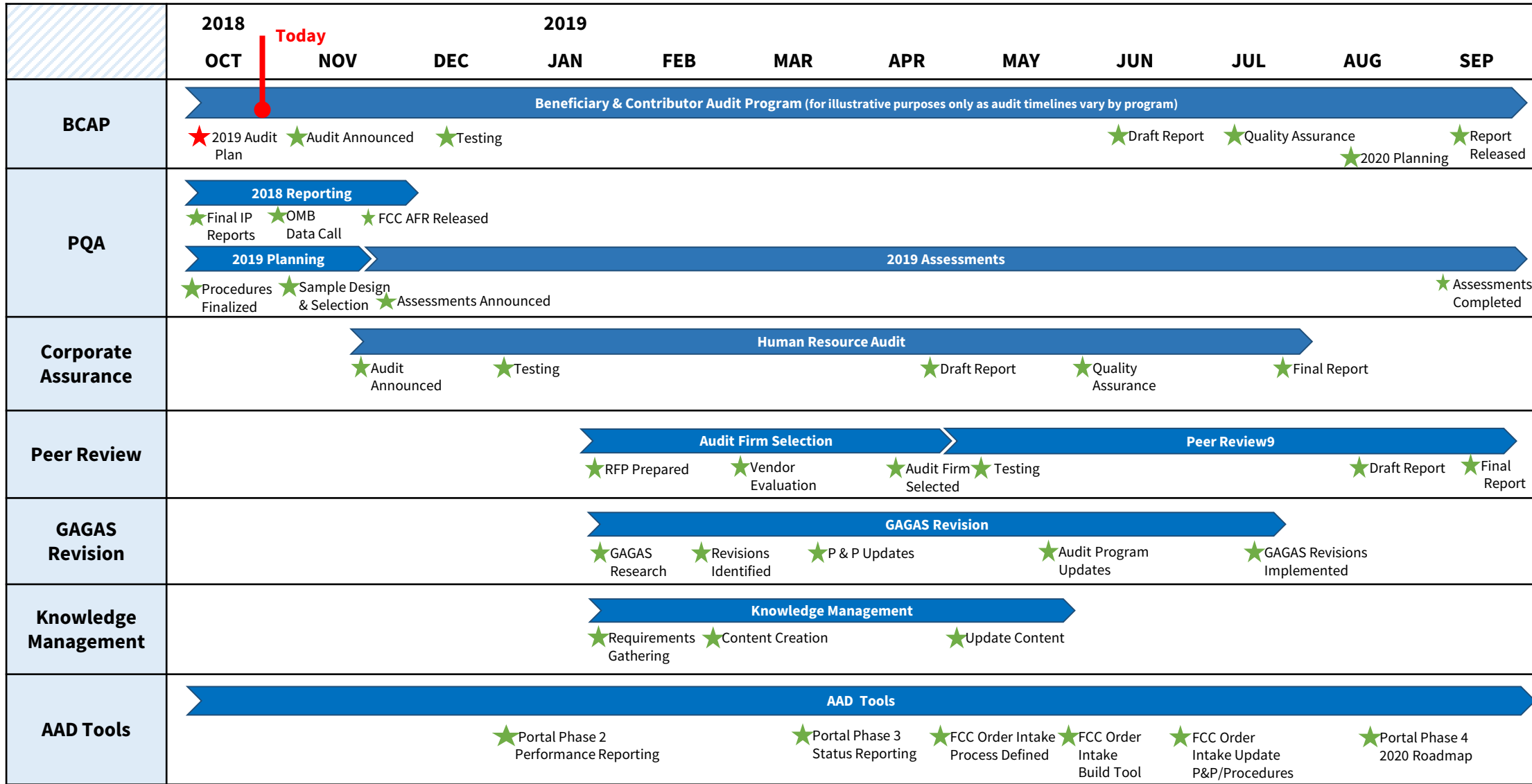
Agenda

Briefing book excludes all materials discussed in Executive Session.

Topic	Description
OPEN SESSION	
Audit & Assurance Division (ADD) at a Glance	<ul style="list-style-type: none">• Audit in Progress• Fiscal Year 2019 Planning• Ancillary Activities
Lifeline Activity	<ul style="list-style-type: none">• Forensic and Chairman Pai Audits
Corporate Assurance	<ul style="list-style-type: none">• Rural Health Care• High Cost• Human Resources
EXECUTIVE SESSION	
Payment Quality Assurance (PQA)	<ul style="list-style-type: none">• Improper Payment Results for FY 2018• Key Observations• Schools & Libraries Comparative Results

Audit & Assurance Division at a Glance

Briefing book excludes all material discussed in Executive Session.

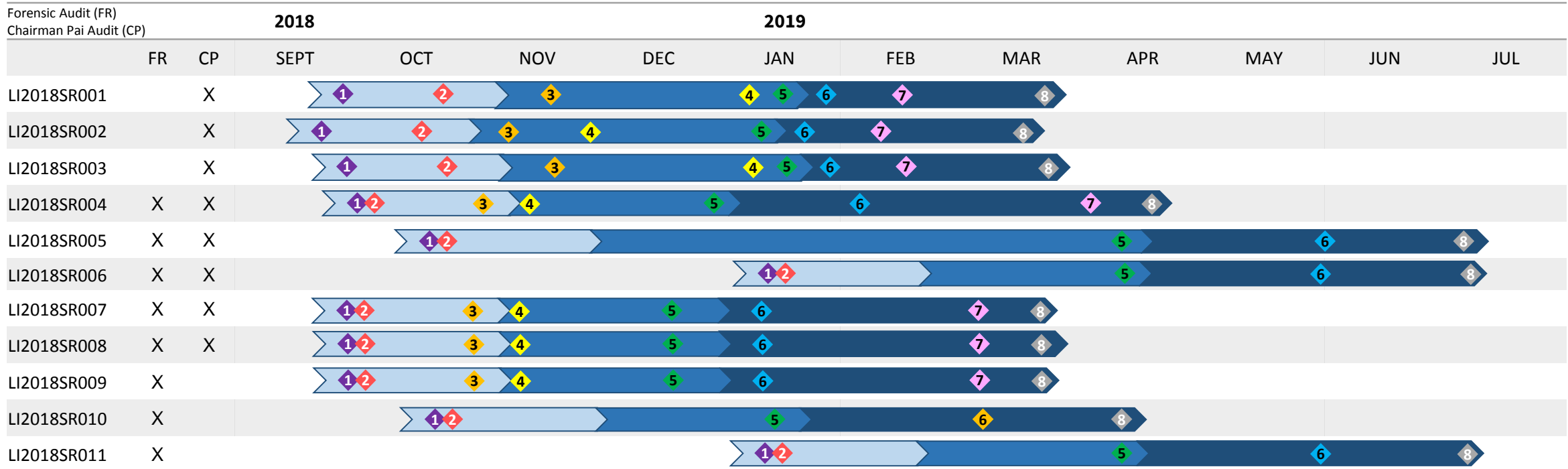


Milestone Legend

- ★ Completed
- ★ On Track
- ★ At-Risk
- ★ Delayed
- ★ On Hold/TBD

Lifeline Activity

Briefing book excludes all materials discussed in Executive Session.



Notional Timeline



Audits and Assessments	Carriers	Milestone Legend							
BCAP	16	1. Announced	2. Data Requests	3. Samples Selected	4. Data Received	5. Testing	6. Draft Report	7. Quality Assurance	8. Report Released
PQA	~127								
Biennial Audits	33								

CORPORATE ASSURANCE

Briefing book excludes all materials discussed in Executive Session.

Rural Health Care

- Internal Control Testing
 - Item presented in aAC04 102918

High Cost

- Operational Review
- High Cost Universal Broadband (HUBB) Portal
- Mobility Fund Phase 1
- Connect American Fund (CAF) Phase I, Round 1

Human Resources

- Planning

Thank You!



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