Avoiding Common Audit Findings
High Cost Program
November 5, 2020
Housekeeping

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• We will answer questions at the end of the presentation
Welcome

Today’s Speakers:

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  Program Analyst, High Cost

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  Senior Manager, High Cost

• Kianna Braxton-Johnson  
  Director, Internal Audit

• Jeanette Santana-Gonzalez  
  Deputy Director, Internal Audit
1. Improper Inclusion of Unallowable Items
   • Not Used for High Cost Purposes
   • Improper Data Period

2. Inadequate / Inaccurate Documentation

3. Improper Affiliate Transactions

4. Improper Allocation Methodology
   • Inaccurate/Misclassified Access Line/Loop Counts
   • Misclassified Assets, Expenses, and/or Liabilities

5. Inaccurate Depreciation Calculation

6. Key Takeaways & Resources

7. Questions
Improper Inclusion of Unallowable Items

Potential Errors

• Inclusion of expenses not necessary for the provision, maintenance, or upgrading of facilities and services for which the support is intended.

• Improper inclusion or allocation of non-regulated assets or expenses
Improper Inclusion of Unallowable Items

- Ineligible Items
  - 47 CFR § 54.7
  - FCC 15-133

- Best Practices
  - Review accounting costs for unallowable and non-regulated items
  - Maintain adequate documentation
Inadequate / Inaccurate Documentation

- **Potential Errors**
  - Insufficient Continuing Property Records (CPRs)
  - Insufficient supporting documentation for affiliate transactions, cost study balances and adjustments, expenses, and geocoded locations
  - Inaccurate/Misclassified Assets, Expenses, liabilities, Access line and/or loops counts
  - Reporting Errors (misapplication of Rules)
Inadequate / Inaccurate Documentation

▶ Error Detection
  • Review Policies and Procedures (P&Ps)

▶ Best Practices
  • Implement / update P&Ps as appropriate
  • Confirm data available after software conversion, acquisition/merger, or other data-related event
  • 47 CFR §54.320(b) and §32.12
Improper Affiliate Transactions

- Potential Errors
  - Not observing a price ceiling when purchasing from an affiliate
  - Not observing a price floor when providing services to an affiliate
  - Insufficient documentation / record retention
Improper Affiliate Transactions

※ Error Detection
  • Compare pricing and costs related to transactions with affiliates versus fees for non-related entities

※ Best Practices
  • Policies, Procedures, Systems
  • Sufficient documentation to support proper compliance (47 CFR §32.27 and §36.2c)
## Improper Affiliate Transaction: Best Practice

<table>
<thead>
<tr>
<th>Transaction Type</th>
<th>Asset/Service Type</th>
<th>Annual Asset Value/Annual Service Amount</th>
<th>Transferring Entity</th>
<th>Recipient</th>
<th>Appropriate Pricing</th>
</tr>
</thead>
<tbody>
<tr>
<td>asset transfer</td>
<td>general asset</td>
<td>less than $500,000</td>
<td>regulated carrier</td>
<td>subsidiary</td>
<td>regulated carrier</td>
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<tr>
<td></td>
<td></td>
<td>greater than $500,000 (a)</td>
<td>regulated carrier</td>
<td>subsidiary</td>
<td>regulated carrier</td>
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<tr>
<td></td>
<td>tariffsd asset (b)</td>
<td>all</td>
<td>regulated carrier</td>
<td>subsidiary</td>
<td>regulated carrier</td>
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<tr>
<td></td>
<td>prevailing price asset (c)</td>
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<td>regulated carrier</td>
</tr>
</tbody>
</table>

Notes:

(a) If the total aggregate annual value of the asset(s) or service(s) reaches or exceeds $500,000 for the first time, the carrier must perform a market valuation to determine fair market value.

(b) Tariffed Assets are assets that are sold or transferred between a carrier and its affiliate pursuant to a tariff.

(c) In order to qualify for prevailing price valuation, sales of a particular asset or service to third parties must encompass greater than 25% of the total quantity of such product or service sold by an entity. Carriers shall apply this 25% threshold on an asset-by-asset and service-by-service basis rather than on a product line or service basis.
Improper Allocation Methodology

- Potential Errors
  - Failure to use cost allocator
  - Use of inaccurate factors
  - Outdated inputs
  - Failure to maintain supporting documentation
  - Failure to use documented factors or methodology
Improper Allocation Methodology

- **Error Detection**
  - Review accounting costs for de-regulated activity
  - 47 CFR §64.901

- **Best Practices**
  - Implement policies and procedures to approve underlying data used in development of allocation factors
  - Maintain adequate documentation to support allocation factors
Inaccurate Depreciation Calculation

Potential Errors

- Using month end balances to calculate depreciation
- Retired assets not removed and/or asset additions not included.
- Formula errors in the calculation.
- Rate used was not applicable to that asset type.
- Rate used was not approved by the state commission.
Inaccurate Depreciation Calculation

- **Error Detection**
  - Review accounting costs for de-regulated activity
  - See 47 CFR §32.2000(g)

- **Best Practices**
  - Establish adequate controls
  - Perform a review and reconciliation of historical data
  - Enhance the preparation, review and approval processes
  - Implement and maintain policies and procedures
Inaccurate Depreciation Calculation: Best Practice

**Depreciation Expense Calculation**

Monthly Depreciation Expense Calculation = Monthly average balance of the associated plant category \( \times \) Annual depreciation rate (12 months)

\[(\text{Asset Balance on first day of the month} + \text{Asset Balance on the last day of the month}) / 2\]
Key Takeaways

1. Maintain Sufficient Documentation
2. Develop, Review, and Update Policies and Procedures, as Necessary
3. Stay Abreast of Updates from the FCC on Allowable Expenses and other High Cost regulations
Links

- **Common Audit Findings**: https://www.usac.org/about/appeals-audits/beneficiary-and-contributor-audit-program-bcap/common-audit-findings-high-cost-program/


Links (cont.)

- **Code of Federal Regulations** *(highlighted Rules)*: https://www.ecfr.gov/
  - Intended use of USF: 47 CFR §54.7 and 47 CFR 54.7(c)
  - CPRs: 47 CFR § 32.2000(e) and 32.2000(f)
  - Affiliate Transactions: 47 CFR § 32.27
  - Documentation Retention: 47 CFR § 54.320(b)
  - Record Keeping: 47 CFR §32.12
  - Cost Allocations: 47 CFR §64.901
Questions?