

**THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS**

Before Commissioners: John Wine, Chair
 Cynthia L. Claus
 Brian J. Moline

In the Matter of Filing of the Audit Report)
for the Kansas Universal Service Fund)
Year 3, March 1999 through February 2000,) Docket No. 02-GIMT-116-AUD
and Providing Recommendations Regarding)
Future Audits.)

ORDER ADDRESSING RECOMMENDATIONS AND COMMENTS

The above-captioned matter comes before the State Corporation Commission of the State of Kansas (Commission) for a decision. Having reviewed its files and records, and being duly advised in the premises, the Commission finds and concludes as follows:

1. On August 11, 2001, Commission Staff filed a Motion requesting the Commission accept the Audit Report provided by the National Exchange Carrier Association (NECA) for the operations of the Kansas Universal Service Fund (KUSF) for its third year of operations, beginning March 1, 1999 and ending February 28, 2000. Staff noted that NECA also made recommendations regarding future audits. Staff stated it believed the recommendations were reasonable and that implementation of the recommendations would help control cost while still providing assurance that contributors report accurately. Staff recommended the Commission request comment on the recommendations.

2. On August 20, 2001, the Commission mailed Order 1 in this docket. In that Order the Commission accepted the Audit findings and requested Comments on NECA's recommendations by August 31, 2001. Order 1 was served on all contributors to the KUSF. Southwestern Bell Telephone Company (SWBT) filed Comments on August 31, 2001. No other

party submitted Comments.

3. NECA made three recommendations:
 - a. An evaluation of the requirement to examine three months of data rather than two. NECA noted that findings typically affect all months in the audit period, so it is redundant and increases cost to examine more months.
 - b. The number of companies audited should remain constant. Therefore, the number of companies selected randomly should be reduced by the number of companies specifically selected for audit by the Commission Staff because of a perceived need to audit that particular company.
 - c. Audit travel costs should be reduced by:
 - i. considering location of companies so that audit trips may be combined.
 - ii. elimination of the requirement for the auditor to go on-site for small companies and for companies audited in previous years.
 - iii. Consideration should be given to reducing the sample size.

NECA explained that small companies are often able to provide documentation for review without a need for the auditor to go on site. Companies that have previously been audited have experience with the requirements and may be able to provide documentation via correspondence. Finally, NECA observed that the limited number and the magnitude of findings justify reducing the sample size.

4. In its Comments SWBT supported NECA's recommendation to reduce the number of months audited from three to two. SWBT also supported NECA's recommendation to hold the number of audited companies constant by reducing the randomly selected number of companies by any explicitly selected companies. SWBT agreed that costs can be reduced by auditing companies located in the same cities, but cautioned that eventually all companies should

be audited regardless of location. SWBT strongly supported the recommendation to eliminate on-site audits for companies that have previously been audited. SWBT stated it can provide the required documentation via correspondence. SWBT also agreed that the size of the sample should be reduced for future audits.

5. SWBT specifically observed that when the Commission established audit criteria it grouped Kansas companies in four groups. SWBT is currently the only company in group 1. The audit criteria require that all companies in group 1 be audited every year. 2 companies in group 2 are to be audited every year. SWBT notes that its audits have resulted in either minor findings with immaterial impact on the KUSF or in no findings, as in this year's audit. It is SWBT's position that annual audits of companies with little or no findings are redundant and costly. SWBT recommends that the Commission exclude companies in groups 1 and 2 that had minimal or no findings in their last audit from the sample group for the following year. SWBT notes that this could result in no audits for both group 1 and 2 companies in any given year. SWBT adds that if the Commission agrees to perform audits for group 1 and 2 companies only biannually the overall sample size should be reduced by those companies so that a lower number of companies is audited.

6. The Commission finds NECA's and SWBT's argument that it is redundant to audit three months of a company's operations, rather than two deserves consideration. NECA explains that findings typically affect all months of the year and auditing more months does not yield additional information but increases the amount of work and cost. However, it is the Commission's understanding that the requirement to audit three months rather than two, was only implemented last year because a three month period is the norm under the AICPA's Rules

of Conduct. If the audit of the data for one quarter reveals material problems, the test period is expanded. NECA has only indicated that findings “typically” affect all months. The Commission finds, that the practice of reviewing three months of data shall be continued for next year and requests that NECA specifically address whether the audit of only two months of data instead of three would have resulted in any difference in findings for the audited companies. The Commission will then determine whether an audit of only two months of data would be sufficient.

7. The Commission agrees that the sample size should be held constant, so that if Staff selects certain companies for audit, the randomly selected sample of companies shall be correspondingly reduced. The reduction shall be made so that the number of companies in each group that is audited remains consistent with the criteria established by the Commission.

8. SWBT’s Comments explain that SWBT is the only company in group 1, for which the Commission has determined that audits should be performed every year, and that the audit findings with respect to SWBT have been minor with immaterial impact on the KUSF and that there were no findings in the last audit of SWBT. SWBT recommends that for companies in groups 1 and 2 for which findings are either minor or none in one year that no audit be performed the following year. Audits have now been performed for three years and NECA has determined that “the information contributors provide to NECA on the monthly KUSF Carrier Remittance Worksheets is complete and accurate.” (NECA’s Final Report, filed July 27, 2001.) NECA further stated that “no findings discovered during the audit process [] significantly impact contributions to the KUSF.” (Final Report) There currently are 6 companies in group 2, and only 2 of those are audited each year. Those companies are randomly selected for audit. Thus

companies in group 2 could be selected for audit every year, two years in a row, every other year or not at all. The Commission finds that it is appropriate to continue to audit two companies in this group every year, but to modify the selection so that so that each company is audited once every three years instead of selecting the audited companies randomly. It is not necessary to amend the criterion for group 2, because it only states 2 companies each year. The Commission finds that SWBT's recommendation is reasonable for group 1 and amends the criterion for group 1 to state that "companies in group 1 that have minor or no findings in one year shall not be audited the following year." Assuming that SWBT continues to have minor or no findings this would mean that SWBT would be audited every other year.

9. NECA also made several recommendations designed to reduce audit travel costs. NECA recommended that locations of companies be considered so that audits could be combined on trips. SWBT agreed this is a good idea, but cautioned that NECA must ensure that all companies eventually are audited regardless of location. The Commission finds that NECA should continue to randomly sample companies for audit, but that consideration may be given to excluding a company in a particular year if travel to that location would be very inconvenient or costly. Other decisions in this order may greatly alleviate concern on this issue.

10. NECA recommended that the Commission eliminate the requirement of on site audits of smaller companies and companies that have been previously audited because such audits could be conducted by requiring the companies to provide review documentation to NECA. NECA notes that smaller companies often are able to provide sufficient and proper review documentation without the need to go on site. NECA notes that companies which have previously been audited may be able to provide documentation via correspondence. SWBT

strongly supported the recommendation that previously audited companies not be audited on site and stated its ability to provide the necessary data by correspondence. The Commission finds this recommendation reasonable and adopts for the next audit year. NECA has gained experience with these audits and the Commission believes that NECA will be able to convey the necessary data requirements to previously audited companies and small companies to obtain the requisite documentation for the audit. The Commission directs NECA to work with Commission staff to determine which small companies may be audited without going on site, when the next audit sample is determined. The Commission requires NECA to document, in its next audit report, any problems it encountered in auditing without going on site.

11. Finally, NECA recommended that consideration should be given to reducing future sample sizes. SWBT agreed that the sample size should be reduced. Considering the Commission's decision to keep the sample size constant and not increase it for specially selected companies and to only audit SWBT every other year, if the audit findings continue to be minor or none, the Commission will not further reduce the audit sample size this year. The Commission requests that NECA raise this issue again next year, if it continues to believe that a reduction in the sample size would be appropriate. If so the Commission requests that NECA recommend an appropriate reduction by groups and explain why NECA believes the size of the recommended sample will provide the necessary assurance that reporting to the KUSF is accurate.

IT IS, THEREFORE, BY THE COMMISSION ORDERED THAT:

- A. NECA shall continue to audit three months of data for each company selected for audit for the next year.
- B. NECA may consider the location of companies as set out above.

- C. The sample size shall be held constant.
- D. Small companies may be audited without going on site.
- E. The audit criterion for companies in group one shall be amended as set out above.

- F. NECA shall report and make recommendations in next year's audit report as set out above.

- G. The parties have fifteen days, plus three days if service of this Order is by mail, from the date of service of this Order in which to request rehearing on any matter decided herein.

- H. The Commission retains jurisdiction over the subject matter and the parties for the purpose of entering such further order or orders as it may deem necessary.

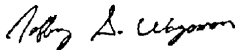
BY THE COMMISSION IT IS SO ORDERED.

Wine, Chr.; Claus, Com.; Moline, Com.

Dated: SEP 18 2001

ORDER MAILED

SEP 19 2001

 Executive Director

Jeffrey S. Wagaman
EXECUTIVE DIRECTOR

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