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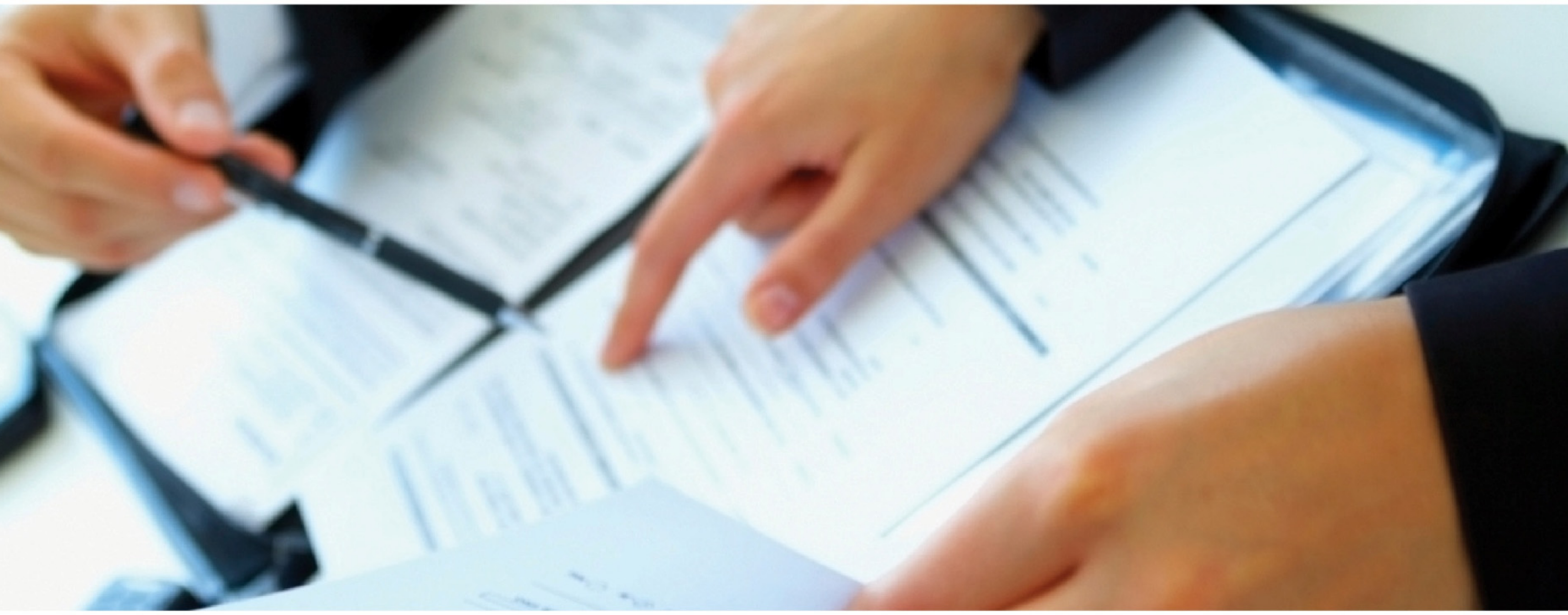

Examination Report:
California Teleconnect Fund Compliance Examination of TelePacific Communications

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Independent Accountants' Report

California Public Utilities Commission
San Francisco, California

We have examined U.S. TelePacific Corp. and its subsidiaries, dba TelePacific Communications' (TelePacific) compliance with the rules, regulations, and requirements of the California Teleconnect Fund (CTF) Program solely related to program costs and cost related activities for the fiscal year ended June 30, 2010. TelePacific is responsible for the compliance with the rules, regulations, and requirements of the CTF Program solely related to program costs and cost related activities. Our responsibility is to express an opinion on TelePacific's compliance based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence about TelePacific's compliance with the rules, regulations, and requirements of the California Teleconnect Fund (CTF) Program solely related to program costs and cost related activities and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion. Our examination does not provide a legal determination on TelePacific's compliance with specified requirements.

In our opinion, TelePacific has complied, in all material respects, with the rules, regulations, and requirements of the CTF Program solely related to program costs and cost related activities for the fiscal year ended June 30, 2010.

TelePacific's responses to the findings identified in our examination are described in the accompanying Schedule of Findings and Recommendations. TelePacific's responses were not subjected to the procedures applied in the examination of the compliance with the requirements described above, and, accordingly, we express no opinion on them.

Crowe Horwath LLP

Crowe Horwath LLP

San Francisco, California
December 30, 2013

California Teleconnect Fund Compliance

Executive Summary

The California Public Utilities Commission (CPUC) contracted with Crowe Horwath LLP (Crowe) to conduct an examination on U.S. TelePacific Corp. and its subsidiaries, dba TelePacific Communications' (TelePacific) compliance with the rules, regulations, and requirements of the California Teleconnect Fund (CTF) Program solely related to program costs and cost related activities pursuant to services provided during the program year ended June 30, 2010.

During our procedures, we noted exceptions related to TelePacific's compliance with the CTF program requirements. In total Telepacific overclaimed and received $41,542 too much from the CTF program for the fiscal year ended June 30, 2010. Telepacific should refund this amount to the CTF. Our observations are included in the ***Findings and Recommendations*** section of this reporting package. The following is a brief summary of our key findings.

1. TelePacific failed to demonstrate compliance with Decision 96-10-066. Specifically, TelePacific included the 0.11% CPUC User Fee to calculate the CTF discount claimed to the CPUC but failed to provide the discount to its CTF eligible customers. This resulted in an overpayment of $6,186 by the CTF program.
2. TelePacific failed to demonstrate compliance with Resolution T-16763. Specifically, some customers did not receive CTF discounts on eligible services provided by TelePacific. TelePacific never claimed these discounts from the CTF program. As such, there is not any monetary effect on the CTF program.
3. TelePacific failed to demonstrate compliance with Decision 96-10-066. Specifically, TelePacific claimed the CTF discount on thirteen (13) ineligible services during the examination period. This resulted in an overpayment of $32,022 by the CTF program.
4. TelePacific failed to demonstrate compliance with Decision 96-10-066. Specifically, TelePacific claimed its CTF discounts that were not properly supported by its detailed billing records, proper attribution and the appropriate time period. This resulted in an overpayment of $3,252 by the CTF program.
5. TelePacific failed to demonstrate compliance with Administrative Letter 17. Specifically, TelePacific reported inaccurate information for seven of its CTF eligible customers and omitted information of two CTF eligible customers. The information reported or omitted does not have a monetary effect on the CTF program.
6. TelePacific failed to demonstrate compliance with Resolution T-16763. Specifically, one customer received CTF discounted services prior to becoming CTF eligible. This resulted in an overpayment of $82 by the CTF program.

In addition to refunding $41,542 to the CTF for the over-claimed and over-reimbursed amounts, TelePacific should:

1. Review the requirements of Decision 96-10-066 for claiming the CTF discount on the CPUC User Fee.
2. Implement an effective review process to ensure that all eligible CTF customers properly receive the CTF discount on all CTF eligible fees and services.
3. Implement practices to avoid claiming CTF reimbursement for ineligible services.

4. Implement a procedure to reconcile the CTF discounts claimed to underlying billing records and the customer invoice prior to submitting the claim to the CPUC for reimbursement.
5. Review the requirements of Administrative Letter 17 as well as institute a quality control review of its CTF claims prior to submission to the CPUC.
6. Implement a review process to verify the CTF eligibility dates prior to providing that customer a CTF discount.

Introduction

The CPUC periodically conducts audits of CTF carriers, pursuant to California Public Utilities Code Sections 274 and 314. The CPUC selected TelePacific as one of the utilities to be examined for the year ended June 30, 2010.

Founded in 1998, TelePacific is a privately held subsidiary of U.S. TelePacific Holdings Corporation and headquartered in Los Angeles. TelePacific is a facilities-based competitive local exchange carrier. TelePacific offers voice services, local and long distance phone services, Internet access, private networking, data collocation, voice over IP applications, integrated services, and other data services. TelePacific provides services to more than 40,000 businesses nationwide, although it targets business customers primarily in California and Nevada.

TelePacific owns and operates extensive network assets including 37,000 fiber strand miles, a Juniper and Cisco-powered MPLS IP network, four datacenters and nearly 400 colocations in 273 wire centers throughout the Southwestern and Western United States. TelePacific operates from 40 regional offices in areas of California and Nevada, including Las Vegas, Los Angeles, Orange County, Sacramento, and San Diego.

At the beginning of the examination period, TelePacific provided telecommunications services to 354 different CTF customers (i.e. 354 unique application numbers). These customers consisted primarily of Community Based Organizations (CBOs) (289) and schools (63). By the end of the examination period, TelePacific's CTF customers increased to 591, 505 of which were CBOs. TelePacific's CTF claims totaled $5.6 million during the examination period.

The CTF Program

In Decision 96-10-066, the CPUC established the CTF program. The CTF program allows eligible public libraries, K-12 public and private schools, California community colleges, government-owned hospitals and health clinics, CBOs, and California Telehealth Networks participants to receive a 50% discount on select telecommunication and internet access services.

The CTF program is overseen by the CPUC's Communications Division, and its operations are modified through regulatory decisions and administrative letters. The program is funded by a surcharge (0.079% during the examination period) assessed by wireline and wireless telecommunications carriers on specific services and consumers' intra-state phone bills.

To receive the CTF discount, customers must apply to the CPUC for approval in the CTF program. If approved, the CPUC provides the customer an approval letter and number, which the customer presents to their service provider to obtain the discount. Approved customers are then eligible to receive their CTF discount as of their application (i.e., filing) date with the CPUC, provided they notify their carriers of acceptance in a timely manner. Service providers apply the discount to their eligible customers, and are later reimbursed through the CTF program by submitting claims to the CPUC.

The CPUC established the services that are eligible for the CTF Program in Decision 96-10-066 and expanded and clarified those services in subsequent decisions. The CTF-eligible services comprise the following:

- Measured Business service lines and basic Voice over Internet Protocols;
- Integrated Services Digital Network (ISDN);
- Switched 56 lines;
- DSL, T-1, DS-3, up to and including OC-192 services (high speed, high capacity lines);
- Internet access services;
- Multiprotocol Label Switching (MPLS) in conjunction with another CTF-eligible service; and
- Functional equivalents of these services, which may vary between service providers.

Carriers are required to charge qualified CTF customers at a rate that is 50% below tariff rates on tariffed CTF eligible services or at a rate that is 50% below regular service rates on non-tariffed CTF eligible services. Tariff rates are the intrastate rates that the local exchange service providers and many long-distance service providers file with the CPUC. Service providers file tariff changes by Advice Letter provided to the Communications Division of the CPUC. Tariffs contain the rates, terms, and conditions of certain services provided by telecommunications carriers.

Non-tariffed rates are the public or published rates that are not regulated. The carrier has the flexibility with charging the customers for the services that are not regulated.

The CTF discount also applies to carrier specific charges, such as company specific surcharges or surcredits, the CPUC user fee, the federal excise fee, the 9-1-1 fee, and local or city-specific taxes. Services not eligible for the CTF discount include, but are not limited to, nonrecurring charges (e.g. installation charges) and usage charges.

The Federal government also provides eligible entities (schools, libraries and CBOs that offer the Head Start program) a similar discount on eligible telecommunications charges (known as the education rate, “E-rate”, or the Universal Service Fund). E-rate discounts can range from 20% to 90%. The CTF discount is to be applied to eligible charges after the application of the E-rate discount. A library or school must apply for the E-rate discount, but if a library or school did not apply for the E-rate discount or if their application is pending, the carrier must first apply the statewide average E-rate discount, which was 70% during our examination period, before applying the CTF discount.

For carriers seeking reimbursement from the CTF program, the CPUC established monthly claim reporting and submittal requirements. These requirements include completing and submitting a CTF claim form to the CPUC. Claims are submitted after providing the CTF discount to eligible customers.

Carriers need to keep important information, such as pricing, tax, surcharge, E-rate percentages, and other CTF-claim related information, on a per customer, per service basis, readily available for at least five (5) years in accordance with the Public Utilities Commission of the State of California General Order No. 28.

On December 5, 2008, the CPUC adopted changes to CTF reimbursement claim protocol and to the claim form in Administrative Letter 17. Administrative Letter 17 specifies that each reimbursement claim -- a multi-tab, Excel workbook -- should include a cover letter; a claim form; a customer report; a services report; a service rate report, and a variance report. Each of these tabs has required data elements, such as customer names, categories, and CTF application numbers for the customer report. Claims filed during the examination period should follow the revised claim reimbursement protocol and utilize the revised claim form.

Changes to the CTF program are formally adopted through legislation, Resolutions, modifications to the Public Utilities Code and Administrative letters. We have summarized below the major changes to the CTF program since inception.

1. **Decision 96-10-066** established the CTF in compliance with Assembly Bill 3643 (Chapter 278, Statute 1994) to provide discounts on selected telecommunications services to qualified entities.

2. **Resolution T-16319** changed the filing requirement for the submission of claims to a maximum of 45 days for eligibility of receiving interest payments from CPUC; determined that telecommunications carriers shall receive interest when the administrative committee fails to complete its review and approval of a CTF claim within one calendar month; and determined that the CTF discount for bundled service offerings shall be based on either the bundled offering or the unbundled tariff rate for access line type services, whichever is lower.

3. **Public Utilities (PU) Code Sections 270-281**, as codified in October 1999 by the enactment of Senate Bill 669, require that the monies in the CTF only be disbursed pursuant to PU Code Sections 270-281 (pertaining to the operation of California's universal service programs) and upon appropriation in the annual State of California Budget Act.

4. **Rulemaking 01-05-046** investigated the "feasibility of redefining universal telephone service by incorporating two-way voice, video, and data service as components of basic service" and how the CTF program might be revised to better support this objective.

5. **Resolution T-16742** complied with portions of Senate Bill 1863 – intended to provide educational institutions, health care institutions, community-based organizations and governmental institutions with access to advanced telecommunications services – by

equalizing the CTF discount available to all program participants at 50%, and added hospital district owned-and-operated health clinics to the list of qualifying entities.

6. **Resolution T-16763** shortened the time frame for telecommunications carriers to file reimbursement claims from the CTF from two years forty-five days to one year forty-five days from the end of the month for which the claim is made; revised the format of the CTF claim worksheet; ordered carriers to discount services to CTF customers upon notification of customer eligibility and prior to submitting reimbursement claims; adopted rules that carriers may impose on E-rate customers who wish to also receive CTF discounts; specified when carrier claims will be eligible for interest and provides direction for carriers wishing to claim interest; and eliminated the filing of adjustment claims except in specified circumstances.

7. **Administrative Letter No. 15** dated December 1, 2006 implemented in part the PU Code Section 884 setting aside funds on a first come, first serve basis for nonrecurring installation costs for high-speed broadband services for eligible community organizations.

8. **Senate Bill 1102** added section 884.5 to the PU Code including a provision requiring carriers to first apply the Federal actual or statewide average E-rate discount – regardless of whether the customer has applied for or been approved – prior to applying the CTF discount to certain eligible services subscribed to by schools and libraries. (**Administrative Letter 10B** provides further clarification on the application of the E-Rate discount and application procedure.)

9. **Administrative Letter No. 11** dated February 1, 2006 revised the CTF claim procedure through a simplified claim form supported by new variance and management reporting.

10. **Resolution T-17142** issued on April 24, 2008 reduced the CTF surcharge rate from 0.130% to 0.079%.

11. **Rulemaking 06-05-028** involved a comprehensive review of the Telecommunications Public Policy Programs, including the CTF, which led to Decision 08-06-020.

12. **Decision 08-06-020** directed several key changes to the CTF program including: an expansion of CTF-eligible services; the removal of CTF tariff requirements for all carriers providing CTF-eligible services on a detariffed or non-regulated basis; the inclusion of CCCs, CTN participants and non-profit CBOs; a cap on total CTF discounts received by CCCs; and allowed partnering in the CTF program between Internet Service Providers and registered telecommunications carriers.

13. **Administrative Letter No. 17** dated December 5, 2008 made additional revisions to the claim form established by Administrative Letter No. 11 including: reformatting to present the claims per customer group and per fiscal year in a table; adding CCCs as customer groups; disclosing important information concerning the funding limitations for CTF discounts received by CCCs; and dividing schools and libraries into two separate customer groups.

14. **Resolution T-17314** adopted a policy requiring that Federal Communications Commission program support or discounts be deducted from the CTF service charges incurred by eligible non-profit CBOs and rural health care providers prior to computing the CTF discount.

Examination Engagement Process

The CPUC selected Crowe to conduct an examination and issue an opinion on TelePacific' s compliance with the rules, regulations, and requirements of the CTF program solely related to program costs and cost related activities for services provided during the fiscal year ended June 30, 2010. This examination was performed in accordance with AICPA standards for compliance examinations, under the direction of the CPUC's Division of Water and Audits.

Purpose
The CPUC provided two main objectives for this project, as follows:

Objective Number 1: Determine compliance with CPUC's directives related to:

- The timeliness of TelePacific's CTF claims;
- The completeness of TelePacific's CTF claims with respect to format and included data elements as provided in Administrative Letter 17;
- The eligibility of organizations receiving CTF discounts;
- The Reasonableness of tariffed and non-tariffed CTF eligible service rates including bundled and unbundled services;
- The eligibility of services receiving CTF discounts; and
- The proper application of E-rate.

Objective Number 2: Test the accuracy of CTF program discounts given to customers and resulting reimbursements claimed against the CTF program by the carriers.

We accomplished both objectives through a combination of analyzing the data on TelePacific's CTF claims (e.g., ascertaining the eligibility of included customers and services and the mathematical accuracy of calculations) and by evaluating a sample of TelePacific's CTF customer records including customer invoices and payments. We derived the criteria by which to measure both objectives from the CPUC's CTF program directives including Assembly and Senate Bills, Rulemakings, Decisions, Resolutions and Administrative Letters governing the CTF program.

Scope
Our examination covered the period of July 1, 2009 through June 30, 2010. The population consisted of all customers included in TelePacific's monthly claims to the CPUC. These included TelePacific's 12 monthly CTF claims as well as 10 adjusted claims that pertained to our examination period.

During the examination period, TelePacific submitted reimbursement claims for 664 unique customers (as measured by application numbers) consisting of 567 CBOs, 91 schools, 3 hospitals and 3 libraries. We selected a sample of 60 customer services for testing (i.e. each selection represented a unique customer and month). If a customer monthly claim included multiple services and/or invoices (i.e. multiple locations are invoiced separately under the same customer number) all services and invoices for that customer listed on the monthly CTF claim were included as part of our testing.

Risk Based Approach
Crowe utilizes a risk based approach for conducting examinations. As part of this risk based approach, we assess risks during the planning phase and re-assess risks throughout the examination. As such, our planning activities included establishing and documenting an overall examination strategy, developing a detailed written examination plan; and determining the extent of involvement of professionals with specialized skills. Based on the risks identified, we designed and implemented overall responses to address our assessed risks of material non-compliance with the rules and regulations of the CTF program and we performed examination procedures whose nature, timing, and extent were based on, and are responsive to, the assessed risks of non-compliance.

Examination Procedures
Our procedures performed for this engagement are provided in more detail in ***Appendix A – Procedures Performed***.

Sampling Methodology
Our sampling methodology for this examination was based on guidance from the American Institute of Certified Public Accountants - Government Auditing Standards and Circular A-133 Audit Guide - Chapter 11: Audit Sampling.

Sampling is the application of an examination procedure to less than 100 percent of the items within an account balance or class of transactions for the purpose of evaluating some characteristic of the balance or class. In other words, sampling may provide the accountant an appropriate basis on which to conclude on a characteristic of a population based on examining evidence regarding that characteristic from a subset of the population.

It is important to note that sampling is one of many techniques designed to provide sufficient appropriate examination evidence to support the accountant's compliance opinion. We often do not rely solely on the results of any single type of procedure to obtain sufficient appropriate evidence on compliance. Rather, our conclusions are based on evidence obtained from several sources and by applying a variety of testing procedures. Combined evidence obtained from the various types of procedures to determine whether there is sufficient appropriate evidence to provide an opinion on compliance.

Our sampling methods used a combination of both random and judgmental sampling. Judgmental sampling was utilized to test individually important items. Specifically, we used the judgment and experience in examining a population for risky or unusual transactions that were selected for testing. These individually important items were selected based on our risk assessment and based on the data analytical procedures that were completed during the examination.

When sampling is used to test transactions sampling risk exists. Sampling risk represents the risk that the sample is not representative of the population. In other words, that the evaluation of a population based on a sample is different from what it would be if the entire population was tested. Based on a statistically valid sample, our sampling methodology is designed to provide a high level of assurance (90 - 95%) in accordance with the AICPA Audit Guide's guidance on Sampling.

Findings and Recommendations

In planning and performing our examination of TelePacific's compliance with the rules, regulations, and requirements of the CTF program solely related to program costs and cost related activities related to services provided during the fiscal year ended June 30, 2010, we noted several items that we felt should be reported to CPUC management. This section of our report provides a listing of these findings that we noted during our testing procedures.

Finding 1: CPUC User Fee Claimed for Reimbursement

<u>Condition</u>
Telepacific added an additional 0.11% of the CTF discount provided to its CTF eligible customers (referred to "CPUC User Fee" in the detailed billing file) when submitting claims for CTF reimbursement. TelePacific collects 100% of the .11% CPUC User Fee from the customer and remits that amount to the CPUC. Telepacific did not provide any CTF discount on the CPUC User Fee to its CTF eligible customers. Therefore, Telepacific should not be entitled to the reimbursement for the additional 0.11% of the CTF discount provided to its CTF eligible customers, which was referred to "CPUC User Fee" by Telepacific. Telepacific was over-reimbursed for the amount of the CTF discount claimed to the CPUC by 0.11% of the CTF discount provided to the CTF eligible customers.

<u>Criteria</u>
Decision 96-10-066 specifies that carriers shall receive a subsidy for the discount provided. Decision 96-10-066 and subsequent amendments set this discount at 50% of the standard or negotiated service prices across all eligible customers.

<u>Cause</u>
The carrier stated that it was not aware that it could only claim the additional 0.11 % on the CTF discount if that amount was also provided to the customer.

<u>Effect</u>
The CTF program was overcharged and the CPUC made an overpayment in the amount of $6,186 due to TelePacific's inclusion of the CTF discount on CPUC User Fees that were not provided to customers.

<u>Recommendation</u>
TelePacific should review the requirements of Decision 96-10-066 and subsequent resolutions and administrative letters for claiming the CTF discount on the CPUC User Fee for reimbursement. In addition, TelePacific should reimburse the CPUC for the $6,186 of CTF discounts over claimed.

Management Response
In subsequent substantial research of the 2009 fiscal year, TelePacific confirms that we collect and remit CPUC User Fees on the total customer invoice and an additional 0.11% on the CTF-eligible portion of the charges submitted to the CTF for payment. TelePacific concurs with the overpayment amount as stated. TelePacific will no longer add an additional 0.11% on the CTF-eligible portion of the charges submitted to the CTF for payment and appreciates the clarification received on the required process.

Finding 2: CTF Discount not Provided to Customers

Condition
Two CTF eligible customers did not receive a CTF discount from TelePacific on a CTF eligible fee charged by TelePacific. During our testing, it was noted that for two (2) of the sixty-one (61) invoices sampled, the CTF discount was not provided to the customers for the Mileage Charge NSR fee. The Mileage Charge NSR is a reoccurring fee that is charged to customers that have multiple locations that need to be connected via data services. This fee is eligible for the CTF discount when applied to ISDN, T-1, and DS-3 services, which are CTF eligible services.

Criteria
Per Resolution T-16763, "The discount for qualified CBOs effective June 8, 2003 shall be 50% for measured business service, switched 56, Integrated Services Digital Network (ISDN), T-1 service, DS-3 and up to OC 192 or their functional equivalents."

Cause
TelePacific indicated that the aforementioned condition was caused by human error. TelePacific missed providing a CTF discount on this service because it did not ensure that a CTF discount was given for all the CTF eligible fees and services during TelePacific's invoice preparation process.

Effect
The customers, even though eligible for the CTF discount on the Mileage Charge NSR fee, were charged 100% of the service rate. Since, the customer never received the CTF discount on this fee and TelePacific never claimed the discount from the CTF program, there is no monetary effect on the CTF program.

Recommendation
TelePacific should implement an effective review process to ensure that all eligible CTF customers properly receive the CTF discount on all CTF eligible fees and services.

Management Response:
TelePacific concurs that in fewer than three instances a CTF-eligible charge on a customer invoice was not included in the credit calculation. TelePacific has made substantial changes to the processes involved in crediting customer accounts since the 2009-2010 fiscal year, including automating credits for the majority of the customers at the billing component level. This addressed issues such as these noted by providing better and more efficient crediting controls and monitoring ability.

Finding 3: Ineligible Services Claimed

Condition
TelePacific claimed a CTF discount for three (3) services that were ineligible for the CTF program. These services are as follow:

- Auto Attendant
- Colocation Cabinet Rental and
- Tier Equipment Upgrades

Criteria
Decision 96-10-066 (October 25, 1996) establishes California Teleconnect Fund (CTF) in compliance with Assembly Bill (AB) 3643 (Chapter 278, Statute 1994) to provide discounts for measured business service, switched 56, Integrated Services Digital Network (ISDN) service, T-1 service, and DS-3, or their functional equivalents.

Cause
TelePacific stated that it was unaware that these services were ineligible for the CTF program.

Effect
Improper identification of services as CTF eligible increases the likelihood that CTF discounts could be claimed on ineligible services resulting in overpayments made by the CPUC. The detailed billing support and sample testing indicates that over the examination period TelePacific overbilled the CTF program by $32,022 for these ineligible services.

Recommendation
TelePacific should implement practices to avoid claiming CTF reimbursement for ineligible services. In addition, a review should be conducted of the entire list of CTF eligible services along with the CTF program rules to ensure that all services listed are CTF eligible. If questions arise on a specific service, TelePacific should seek written clarification from the CPUC on that service. In addition, TelePacific should refund the CTF program for the $32,022 of overpayments made by the CPUC during the examination period.

Management Response:
TelePacific acknowledges that it was mistaken in its belief that the Auto-Attendant, Colocation Cabinet Rental, and Tier Equipment Upgrade charges were eligible for CTF reimbursement. TelePacific will no longer include these services in any claims submitted to the CTF for reimbursement.

Finding 4: Claimed Amounts not supported by Billing Records or Customer Invoices

Condition
TelePacific claimed discounts that were not properly supported by detailed billing records, proper attribution to customers or the appropriate time period. These items are summarized below:

- Four (4) TelePacific customers had CTF discounts on the monthly claim forms incorrectly attributed to other customers. However, the differences between the customers netted to zero and as such there was no financial impact to the CTF program.

- Three (3) TelePacific customers had CTF reimbursements on the monthly claim forms that were not supported by the detailed billing records. Since the discount claimed exceeded the amount supported by TelePacific's billing records, the excess amount claimed will be deemed as an over claim to the CPUC. The result was over claims to the CTF totaling $3,252.

- Forty-nine (49) customers appeared in TelePacific's supporting billing detail during one or more months however did not appear on CTF monthly claim. In most instances, TelePacific listed one customer's discount under a sister organization. Therefore, the total amount claimed to the CTF program was correct.

- In other instances, TelePacific provided the discount to the customer but did not claim reimbursements from the CTF until a subsequent month. When analyzing the entire examination period, these items had a zero net impact to the CTF discounts claimed.

Criteria
Decision (D.) 96-10-066 states that the CTF eligible customers can receive a 50% discount on CTF eligible services received. Furthermore, CTF Administrative Letter 17 (dated 12/5/2008) outlines a revised method for submitting CTF claims. Administrative Letter 17 states that "all payments will be made subject to a subsequent formal audit" and as such supporting records should be maintained to support each claim.

Cause
The discrepancies were a result of a combination of errors in worksheet formulas and human error in the manual development of the claims.

Effect
Claiming discounts to the CTF program that do not reconcile to underlying data increases the likelihood that amounts claimed to the CPUC are not correct and that CPUC could make overpayments. The net result of this finding was that TelePacific over claimed $3,252 from the CTF program.

Recommendation
TelePacific should implement a procedure to reconcile the CTF discounts claimed to underlying billing records and the customer invoice prior to submitting the claim to the CPUC for reimbursement. Additionally, Telepacific should refund the CTF program for the $3,252 of overpayments made by the CPUC during our examination period.

Management Response:
TelePacific concurs that human error resulted in some minor CTF claim line items that did not accurately reflect the customer invoices. TelePacific affirms the over claimed amount as stated. As noted in the response to finding 2, the automation of the credits has allowed us to control the process at the billing component level which also allows us to assemble the claims more efficiently and accurately.

Finding 5: CTF Monthly Claim Form Errors

Condition
Seven (7) TelePacific customers were listed inaccurately on at least one claim form. The customer name and number of incorrect claims are listed below:

- Challenge Day (12 CTF claims);
- Metropolitan Cooperative Library System (8 CTF claims);
- East Oakland Community Project (4 CTF claims);
- Youth Connection of Ventura County (1 CTF claim);
- La Plaza de Cultura y Artes (1 CTF claim);
- Advanced Education Services (3 CTF claims); and
- Buena Park Library District (2 CTF claims).

These errors included using a customer's service account number rather than its CTF application number, and using service names for customers that differ from the names in their CTF applications.

Additionally, on the Customer Report tab of the September 2009 claim, TelePacific omitted the customer type for 16 customers. These customers should have been designated as Community Based Organizations. Furthermore, on the Customer Report tab of the March 2010 claim, TelePacific listed the customer names in the application number column, and listed the application numbers in the customer name column.

Criteria
CPUC CTF Administrative Letter 17 outlines a method for submitting CTF claims. Under the "Customer Report" tab, there are four columns for inputting customer data: the "Customer Type," the "Applicant Name," the Application Number" and the "CTF Discount".

Cause
This condition was caused by human error due to the manual process of completing the monthly CTF claim form.

Effect
The above-listed seven customers were CTF-eligible at the time, so these errors had no financial impact on the CTF program or on the customers. Additionally, while omitting customer types and transposing customer names and application numbers prevents the CPUC from being able to easily search the CTF eligibility of TelePacific customers in its own database, there was no financial impact to CTF customers or to the CTF program.

Recommendation
TelePacific should review the requirements of Administrative Letter 17 as well as institute a quality control review of its CTF claims prior to submission to the CPUC.

Management Response
TelePacific concurs that human error resulted in some minor CTF claim line items that did not accurately reflect the CTF approvals of the customers. As noted in the response to Finding 2, the automation of the credits has allowed TelePacific to control the process at the billing component level which also allows TelePacific to assemble the claims more efficiently and accurately.

Finding 6: Reimbursements Claimed Prior to CTF Eligibility

Condition
Twelve (12) TelePacific customers became CTF-eligible in the middle of a claim month (i.e., the date that a customer's CTF application was received by the CPUC fell within the same month that the customer first appeared on a claim). TelePacific provided one of these customers CTF-discounted services prior to becoming CTF-eligible.

Criteria
CPUC Resolution T-16763 (May 27, 2004) sets rules regarding CTF eligibility. Section A of T-16763 (p. 26) under Application of CTF Discounts states that "CTF discounts are applicable as of the date the customer's application has been received by TD. This may involve credits to the customer's account because of the period between the application date and the date the customer is notified of CTF eligibility. New CTF customers will be notified that there is a thirty-day period from the date of the notification letter to advise their telecommunications provider(s) of CTF eligibility and identify services to which the CTF discount should be applied for applicability of CTF credits back to the application date." In other words, upon acceptance of the CTF application by the CPUC, customers are eligible for the CTF discount as of the date their application was filed with the CPUC, provided that they notify their carrier within 30 days of acceptance.

Cause
TelePacific prorated a customer's monthly eligible charges based on its CTF eligibility date. However, in this case human error during the manual claim development process resulted in no proration for this customer.

Effect
TelePacific improperly claimed a total of $82 in CTF reimbursements for this customer.

Recommendation:
TelePacific should implement a review process to verify the CTF eligibility dates prior to providing that customer a CTF discount. In addition, TelePacific should reimburse the CTF program for the $82 that improperly claimed prior to the customer being eligible.

Management Response

TelePacific concurs that human error resulted in CTF claim line items that did not accurately reflect the CTF approval date of the customer. TelePacific affirms the amount stated as improperly claimed. As noted the response to finding #2, the automation of the credits has allowed TelePacific to control the process at the billing component level which also allows TelePacific to assemble the claims more efficiently and accurately.

Appendix A – Procedures Performed

List of Records Obtained

Records obtained for our TelePacific testing procedures included:

- The twelve (12) monthly claims obtained from the CPUC that were filed by TelePacific during the examination period and the ten (10) adjusted claims filed subsequently that pertain to the examination period
- CPUC's CTF Claim Tracking
- Tariff service rate documents
- Service revenue report for nontariffed customers – This report detailed service charge rates for non-CTF customers for the same services provided to CTF customers within our sample
- Detailed electronic data reports provided by TelePacific that support each customer's CTF discount on every monthly claim. These data reports included each CTF customer's
  - application number
  - organization name
  - account number
  - service description
  - service quantities
  - unit price of service
  - exchange billing surcredit or surcharge, if applicable.
  - toll billing surcredit or surcharge, if applicable.
  - access billing surcredit or surcharge, if applicable.
  - E-rate discount
  - CTF discount after E-rate
  - CPUC User Fee
  - 911 Tax
  - Federal Excise Tax
  - local tax
  - monthly claim amount for each organization and service claimed
- The crosswalk provided by TelePacific between TelePacific's specialized communications services and the CPUC's list of CTF-eligible services
- TelePacific's tariffed rate schedules obtained from TelePacific that correspond to the examination period
- 61 customer invoices and payment support from TelePacific for each customer-month included in the sample selection made by Crowe
- Canceled checks to confirm customer payments for the 61 sampled invoices
- TelePacific Bank Statements that contained CPUC payments for the CTF program
- Form 486 for E-rate eligible customers within our sample

Summary of Procedures Applied

Our engagement was divided into two phases. The first phase of our project consisted of completing an off-site data analysis on data provided by the carrier and testing supporting documentation. The second phase involved on-site visits to TelePacific to perform additional testing and procedures over compliance.

In the first (data analysis) phase, Crowe designed, developed, and populated a CTF claims database. The database captured available data from TelePacific' s Fiscal Year 2009-10 monthly and adjusted claims, as well as supporting information from TelePacific and the CPUC including CTF-eligible organizations (including application date, CPUC number, and approval date) and CTF-eligible services and their functional equivalents. Crowe analyzed this data to identify anomalies that might indicate problems with TelePacific's data and conducted compliance tests, as described in the following sentence, of the data that supplemented our field work. Crowe used the CTF claims database to test the timeliness of each CTF claim; the eligibility of TelePacific's CTF customers and services; the correct application of the E-rate; the accuracy of the math underlying each claim; and the completeness of the claim format.

The second phase involved on-site visits to TelePacific during the weeks of February 18, 2012 and February 25, 2013. During the on-site visits, Crowe conducted an entrance conference with TelePacific to confirm the scope and extent of our procedures, and requested documentation. We tested a sample of claims and their supporting invoices with respect to the CTF-eligibility of organizations and services including bundled services; tariffed rates and non-tariffed prices; application of the E-rate; and the adequacy and accuracy of reimbursement claims.

CPUC specified key objectives for evaluating the compliance with administrative directives and the accuracy of CTF claims for the fiscal year ended June 30, 2010. Below, we have provided a summary of these objectives and our approach to meet these objectives as part of our testing procedures.

Objective 1: Compliance with the CTF's Administrative Directives

1. Determine whether the carriers filed their original CTF claims with the timeframe specified in Resolution T-16763, Ordering Paragraphs (OP) 1-2.

> <u>Approach</u>
> We tested each monthly claim filed during the engagement period to determine if the claim for reimbursement was filed within the required timeframe per Resolution T-16763, Ordering Paragraphs, 1-2. Resolution T-16763 requires the reimbursement claim be filed within one (1) year and forty-five (45) days from the period being claimed.

2. Determine whether the format of the carrier's CTF claim is in conformance with the Commission's directives, specifically Administrative letters 11 and 17 as well as Decision 08-06-020, the claim contains all required elements, and contains complete supporting information.

Approach
We tested each monthly claim filed during the engagement period to determine if the claim was prepared in conformity with the Commission's directives and contained all required elements. For each claim, we then tested whether the claim was filed on the CPUC approved Claim Form and the claim form was complete. We additionally tested that TelePacific had properly filed all the annual Customer Report and Service Report as required by Administrative Letter 17. Finally, we tested if the Rate Report and/or Guidebook were properly included with the claims filed during the engagement period.

3. Determine whether the carriers are in compliance with the CPUC's directives, Decisions 96-10-066 and 08-06-020, and Resolutions T-16763, and T-16742, in providing CTF discounts to the CPUC's approved CTF eligible organizations only after the CPUC's approval dates.

Approach
For each customer selected, we tested if the customer was approved to receive the CTF discount and that the discount was provided to the customer only after the CPUC's approval date. We tested CPUC's approval dates for the 664 unique CTF-customers, as listed on the CPUC's website, to determine whether CPUC approval occurred prior to TelePacific's provision of any CTF discount.

4. Determine whether the carriers' tariffs are in compliance with the CPUC's directives, Decision 08-06-020, and provide that the rates for qualifying schools, libraries, government owned hospitals and health clinics, and CBOs for CTF eligible services are 50% below the rates charged to other business for those same services or their functional equivalents.

Approach
For each invoice selected for testing, we compared the amount billed for eligible services to Tariffed rates or if a detariffed service to published rates or to rates charged to other customers for similar services in the same geographic region. We then tested if the rates charged for CTF eligible services were 50% below the rates charged to other business for the same service by comparing the rate to the approved range for rates for that service per the tariff and the Rate Report. We then tested the CTF discount was properly applied to applicable charges.

5. Determine whether the carrier is in compliance with the CPUC's directives including Decisions 96-10-066 and 08-06-020, Resolution T-16742, and Administrative Letter 16 with respect to providing CTF discounts on approved CTF-eligible services.

Approach
TelePacific provided a list of all the CTF-eligible services it provided in Fiscal Year 2009-10 and how these services related to the CPUC's list of CTF-eligible services (the "crosswalk"). We obtained feedback from the CPUC on TelePacific's crosswalk to determine CTF eligibility and followed up with TelePacific to clarify the definition of certain services. Then, for each customer invoice selected through our sample, we compared the billed services per the invoice to the crosswalk to determine if TelePacific calculated the CTF discount only on eligible services.

6. Determine whether the carriers are in compliance with the CPUC's directives, PU Code 884, and administrative letter 10b and 14, with respect to applying the E-rate discount before providing and claiming CTF discounts. Test claims supporting detail to determine if E-rate discount was properly applied. Obtain Form 486 per customer from Carrier and Verify the E-rate applied was properly supported by Form 486.

Approach
For each school selected for testing, we tested whether TelePacific properly applied the E-rate discount to customer's bills prior to calculating the CTF discount.

Objective 2: Accuracy of the CTF Reimbursement Claims

1. Determine the CTF discount (i.e. 50%) was properly calculated on the eligible services (after properly applying E-rate) in accordance with Resolution T-16742.

Approach
We obtained a list of all CTF eligible services provided by TelePacific (the "crosswalk"). For each customer invoice selected in our testing sample, we compared the billed services per the invoice to the crosswalk. Using the crosswalk and invoice, we tested if TelePacific calculated the CTF discount only on eligible services and used the proper 50% CTF discount rate.

2. Determine whether CTF claim payments agree to the carrier's claimed amount, the amounts of the CTF claim reimbursement that the carriers received agree to the CPUC's CTF claim payment records and that the CTF claim payments were deposited into the proper accounts.

Approach
We obtained claim payment information from the CPUC. Using this information we traced the amounts paid by the CPUC (per their claim payment detail) to the amounts claimed by TelePacific. Next, we traced the amount paid by the CPUC to the amount received by TelePacific and traced this amount to TelePacific's bank account to determine it was properly deposited.

3. Determine if there was an underpayment or overpayment of CTF claims to the carrier. Recalculate interest due to or from the carrier in accordance with Resolution T-16763.

Approach
We compared the final, calculated CTF discount to the amount claimed on the CTF claim. If there was an underpayment or overpayment, we calculated the interest due to / from TelePacific as required by regulations.

Appendix B – Carrier Responses

December 30, 2013

Crowe Horwath LLP
575 Market Street, Suite 3300
San Francisco, California 94105-5829

Ladies and Gentlemen:

Please find below TelePacific Communication's response to the 2009-10 audit performed by Crowe Horwath LLP.

Finding 1: CPUC User Fee Claimed for Reimbursement

In subsequent substantial research of the 2009 Fiscal Year, TelePacific confirms that we collect and remit CPUC User Fees on the total customer invoice and an additional 0.11% on the CTF-eligible portion of the charges submitted to CTF for payment. TelePacific concurs with the overpayment amount as stated. TelePacific will no longer add an additional 0.11% on the CTF-eligible portion of the charges submitted to the CTF for payment and appreciates the clarification received of the required process.

Finding 2: CTF Discount not Provided to Customers

TelePacific concurs that in fewer than three instances a CTF-eligible charge on a customer invoice was not included in the credit calculation. TelePacific has made substantial changes to the processes involved in crediting customer accounts since the 2009-2010 Fiscal Year, including automating credits for the majority of our customers at the billing component level. This addressed issues such as these noted by providing better and more efficient crediting controls and monitoring ability.

Finding 3: Ineligible Services Claimed

TelePacific acknowledges that it incorrectly included Auto-Attendant, Colocation Cabinet Rental, and Tier Equipment Upgrade charges for CTF reimbursement. TelePacific will no longer include these services in any claims submitted to the CTF for reimbursement. TelePacific concurs with the overbilled amount as stated. As noted in Finding 2, the automation of the credits in 2012 has allowed us to control the process at the billing component level, enabling us to exclude any ineligible components at their actual cost as opposed to applying a standard blanket reduction to account for any and all ineligible charges that could be a part of the monthly charge for an integrated service.

Finding 4: Claimed Amounts not supported by Billing Records or Customer Invoices

TelePacific concurs that human error resulted in some minor CTF claim line items that did not accurately reflect the customer invoices. TelePacific affirms the over claimed amount as stated. As noted in Finding 2, the automation of the credits has allowed us to control the process at the billing component level which also allows us to assemble the claims more efficiently and accurately.

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Finding 5: CTF Monthly Claim Form Errors

TelePacific concurs that human error resulted in some minor CTF claim line items that did not accurately reflect the CTF approvals of the customers. As noted in Finding 2, the automation of the credits has allowed us to control the process at the billing component level which also allows us to assemble the claims more efficiently and accurately.

Finding 6: Reimbursements Claimed Prior to CTF Eligibility

TelePacific concurs that human error resulted in a CTF claim line items that did not accurately reflect the CTF approval date of the customer. TelePacific affirms the amount stated as improperly claimed. As noted in Finding 2, the automation of the credits has allowed us to control the process at the billing component level which also allows us to assemble the claims more efficiently and accurately.

As TelePacific has grown both organically and thru acquisition, resulting in more CTF claims, previous manual processes did not scale. The automation implemented in periods after the audit timeframe, have improved both the accuracy and timeliness of our CTF claims processing.

Sincerely,

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