

INVESTIGATION TO VERIFY THAT GTE CALIFORNIA, INC. (GTE-C) AND CONTEL OF CALIFORNIA, INC. (CONTEL-C) ASSESSED THE CHCF-B SURCHARGE AND THE CTF SURCHARGE AND REPORTED SURCHARGE REVENUES TO THE CALIFORNIA PUBLIC UTILITIES COMMISSION

A. EXECUTIVE SUMMARY

This report provides the analysis and results that were the basis for the Accountant's Letter at the end of the report. While the Accountant's Letter indicates that "the schedules referred to above represent the submission of surcharge collections for the company in all material respects, in conformity with the California Public Utilities Commission Rules and Regulations", there were a number of specific findings that indicates errors or raised legal issues. In total eleven findings are presented in this report, of which four indicate required corrections or raise questions as yet unanswered. We summarize these here:

- Finding F-4 indicates that for the months of January, 1998 through December, 1998 a clerical error that occurred in working with the computer files resulted in under reporting CHCF-B surcharge revenues in the amount of \$133, 741 for GTE and CTF surcharge revenues in the amount of \$4,546 for Contel. Verizon has agreed to correct this error.
- Finding F-5 indicates that for the months of February, 1997 through December, 1999 surcharge revenues on tele-services used by Verizon in the total amount of \$6,336,550 were not reported. There is a legal question as to whether surcharges should be collected for internal tele-services. The initial analysis indicates that Verizon pays the surcharge for non-regulated operations, but not for regulated activities. The argument being that tele-services incurred by the regulated activities of the Company are simply the cost of doing business and not taxable. We believe this requires a regulatory or legal interpretation which we are not qualified to do.
- Finding F-6 indicates a clerical error was identified in June, 1999, which resulted in under reporting of surcharges in the amount of \$46,056. Verizon has agreed to correct this error.

- Finding F-8 indicates results of IOSC tests revealed approximately \$91,000 in un-assessed surcharges due to incorrect tagging of IOSCs for surchargeability. The company uses Item of Service Codes (IOSC's) in connection with its billing system to aid in producing customer bills. These are 'tagged' as taxable or nontaxable for add on type charges such as local and federal taxes or surcharges for the CHCF-B or CTF. A number of the 19,000 IOSC's were audited and challenged as to the appropriateness of the exemption. By extrapolating this sample, one concludes that \$91,749 in errors could exist.

Based on these findings, we reach two conclusions. First, underpayments totaling \$276,091.29 have occurred as a result of findings F, 4, 6, and 8. This amounts to \$263,746.90 for the CHCF-B fund and \$12,344.90 for the CTF fund as indicated in the table below. Secondly, a decision needs to be rendered regarding the applicability of the surcharges to internal tele-services costs.

Category of Correction	CHCF-B	CTF
Finding 4	\$133,741.00	\$4,546.00
Finding 6	\$44,863.90	\$1,191.90
Finding 8	\$85,142.00	\$6,607.00
Total by Fund	\$263,746.90	\$12,344.90
Total for Both Surcharges		\$276,080.80

B. INTRODUCTION

The work performed by Vantage Consulting, Inc. and Smith, Turner & Reeves and summarized in this report has been conducted in accordance with the work description included in the RFP issued by the California High Cost Fund-B (CHCF-B) Administrative Committee and the California Teleconnect Fund (CTF) Administrative Committee to conduct an investigation of GTE California, Inc. (GTE-C) and Contel of California, Inc. (Contel-C). The purpose of the investigation is to verify whether GTE-C and Contel-C assessed the CHCF-B surcharge and the CTF surcharge, and reported the surcharge revenues to the California Public Utilities Commission (CPUC) for the period February, 1997 through December 31, 1999 in accordance with the directions of the CPUC.

In addition to the final report, we were instructed to provide a detailed description of the following items for GTE California, Inc. for the period February, 1997 through December, 1999.

- What are the procedures in place to identify entities that purchase services for resell purpose and not subject to the CHCF-B and the CTF surcharges?
- Did GTE California, Inc. report intrastate telecommunications revenue and associated surcharges for other entities that GTE California, Inc. rendered billings for?

- Did GTE California assess and report surcharges on discounts associated with the Federal Communications Commission's discount program for schools and libraries?

In planning this engagement it was agreed among Vantage Consulting, Inc; Smith, Turner & Reeves; and CPUC staff, that the engagement would be an Attestation Examination as defined in the American Institute of Certified Public Accountants' (AICPA) Statements on Standards for Attestation Engagements (SSAEs).

The first SSAE, Attestation Standards, was issued by the AICPA in 1986 but it was not numbered. In 1989, that standard, along with standards on prospective financial statements and pro forma financial statements, were codified as AT section 100 of the AICPA professional Standards, Volume 1. In 1993 the codification became officially designated SSAE No. 1, Attestation Standards. Since then, SSAE Nos. 2 through 9 have been issued.

The AICPA's rationale in issuing the attestation standards was threefold:

- To recognize the expansion of the practitioner's function. Practitioners are often called on to attest to many things other than historical financial statements. The practitioners report adds credibility to an assertion and reduces information risk to users, thus providing a valuable service.
- To provide consistency among practitioners. The standards were intended to promote consistence among practitioners in performing services and reporting on them.
- To increase public acceptance and understandability. The standards narrow available services to a common set of functions understandable to the public.

SSAE No. 1 (At 100.1), as amended, defines an attestation engagement as follows:

"An attest engagement is one in which a practitioner is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party."

The written assertion in this engagement is GTE-C's and Contel-C's submissions of the following reports:

- CHCF-B Deposit & Declaration Form for February 1, 1997 through September 30, 1999, dated November 5, 1999.
- CTF Deposit & Declaration Form for February 1, 1997 through September 30, 1999, dated November 5, 1999.
- Combined California PUC Telephone Surcharge Transmittal for the month of October, 1999, dated December 3, 1999.

- Combined California PUC Telephone Surcharge Transmittal for the month of November, 1999, dated January 1, 2000.
- Combined California PUC Telephone Surcharge Transmittal for the month of December, 1999, dated February 7, 2000.

These reports include GTE-C's and Contel-C's assessment of the CHCF-B surcharge and the CTF surcharge, and their reports of the surcharge revenues to the California Public Utilities Commission (CPUC) for the period February, 1997 through December 31, 1999 in accordance with the directions of the CPUC.

C. APPROACH

This section of our report describes in detail our approach to this engagement. This description does not represent the specific audit program utilized by Smith, Turner & Reeves in conducting its attestation engagement, and does not include all the specific audit procedures performed in that engagement. It is a general description of the work performed by Vantage Consulting, Inc. and Smith, Turner & Reeves in order to understand the accounting system and procedures utilized by Verizon to bill and report surcharge revenues, to assess the degree of reliance which can be placed on these systems and procedures, and to provide the supplemental information required by the additional service requirements of the overall engagement.

Exhibit 1, Outline of Project Approach, presents an overall view of the work performed and our approach. The discussion below presents more details of our approach and the work performed.

i GTE-C is a regulated utility authorized to provide local and long-distance telephone services in California. Contel-C was a regulated utility authorized to provide local and long-distance services in California. In 1994 and by Decision (D.)94-04-083, the Commission approved the merger of Contel-C into GTE-C the surviving company but deferred the decision on the consolidation of operations to a later phase. In 1997 and by D.97-12-091, the Commission approved the consolidation of operations of Contel-C into GTE-C effective January 1, 1998. As of January 1, 1998, Contel-C disappeared as a Commission regulated utility. On October 30, 2000, GTE-C filed a name change with the Commission to Verizon California, Inc. (Verizon). For the purpose of this report, GTE-C, Contel-C and Verizon are used interchangeably

Investigation of Verizon CHCF-B and CTF Surcharges

Exhibit -1 Outline of Project Approach

Review Procedures & Controls	Verify & Reconcile Data	Report
Procedures Overview - Regulatory Staff West	Obtain Copies of Surcharge Reports	Report on Review of Procedures & Controls
Review Procedures & Controls	- CHCF-B Deposit & Declaration Form for February 1, 1997 thru September 30, 1999, dated November 5, 1999	Report Examination Findings
- National Integrated Products and Services (NIPS)	- CTF Deposit & Declaration Form for February 1, 1997 thru September 30, 1999, dated November 5, 1999	Accountant's Report on Attestation Examination
- National Tables Group	- Combined California PUC Telephone Surcharge Transmittal for the Month of October, 1999, dated December 3, 1999	
- Customer Billing & Services System	- Combined California PUC Telephone Surcharge Transmittal for the Month of November, 1999, dated January 1, 2000	
- Customer Billing Center - West	- Combined California PUC Telephone Surcharge Transmittal for the Month of December, 1999, dated February 7, 2000	
- GTE Data Center Operations		
Review Internal Audit Reports re: Billing, Collection and Remittance of Surcharges		
Review Internal Audit Reports re: Customer Billing & Services System (CBSS)		
Review Data Center Operations Certification by SGS International Certification Services (SGS)	Obtain Copies of Objective Supporting Data	
Conduct Site Visit to Customer Billing West, Newbury Park, California	- Monthly Accounting Records (CBSS Reports)	
- Review Bill Print & Distribution Center	- Excel Worksheets	
- Review Quality Assurance Procedures	- Surcharge Remittance Worksheets	
Review Procedures for FCC Discount Program for Schools & Libraries	Extract Data and Prepare Workpaper Schedules	
Review Procedures for Identifying Entities that Purchase Services for Resale	- Analysis of Monthly Transmittals - CHCF-B	
Review Procedures for Reporting Intrastate Telecommunications Revenue and Associated Surcharges for Other Entities that GTE Rendered Billings For	- Analysis of Monthly Transmittals - CTF	
	Reconcile Monthly Surcharge Transmittals to Monthly Accounting Records	
	Perform Substantive Testing	
	- Select Test Months	
	- Select Sample of Customer Bills	
	- Perform Detail Review of Customer Bills	
	Identify and Summarize Exceptions	

REVIEW OF PROCEDURES AND CONTROLS

It is normal to perform a review of internal controls when reviewing or examining financial statements or financial information as a basis for determining the degree of reliance which can be placed on the accounting system to provide reliable information. In this engagement we extended our review of procedures and controls to comply with the additional service requirements of the engagement. Our extended review also helped us to more fully understand the origin of the data used by GTE-C and Contel-C to assess surcharges and, accumulate and report surcharge balances due.

Information Requests Obtained and Reviewed

Exhibit 2, Information Requests, outlines the general Information Requests processed in this engagement.

Investigation of Verizon CHCF-B and CTF Surcharges

Exhibit -2 List Information Requested During Investigation

Request Number	Requested From	Requested By	Description of Information Required	Date Requested
101	Les Munjas	Robert Wilkinson	Please provide a copy of end user of billing system procedures, including NIPS and National Table Group's Functions. (Provide Narrative and any available flow charts)	9/25/00
102	Les Munjas	Robert Wilkinson	Please provide copies of any internal or external audit reports of billing system or internal control reviews during 1997, 1998, 1999, or 2000.	9/25/00
103	Les Munjas	Robert Wilkinson	Please provide copies of any "Service Bureau" audit reports. (Audits conducted in connection with your providing billing services to other entities.)	9/25/00
104	Les Munjas	Robert Wilkinson	Please describe where (physical location and department /organizational unit) all end user billing functions are performed and, how they interface.	9/25/00
105	Les Munjas	Robert Wilkinson	Please provide copies of all Table Star reports related to CHCF-B and CTF surcharges.	9/25/00
106	Les Munjas	Robert Wilkinson	Please provide copies of all California Public Utility Commission (CPUC) Orders related to CHCF-B and CTF surcharges.	9/25/00

107	Les Munjas	Robert Wilkinson	Please Provide a list and description of all ISOC's in use during the period February 1, 1997 to December 31, 1999.	9/25/00
108	Les Munjas	Robert Wilkinson	Please provide a description of all significant billing systems software changes made during the period February 1, 1997 to December 31, 1999, including the changes made to expand the number of tax and surcharge codes available.	9/25/00
109	Les Munjas	Robert Wilkinson	Please provide a description of system security procedures and controls in place to ensure the propriety of customer bills.	9/25/00
110	Les Munjas	Robert Wilkinson	Please provide copies of monthly Combined CPUC Telephone Surcharge Transmittal Forms, for each month beginning February, 1997 through December 1999, including Combined CPUC Telephone Surcharge Reports for Contel and GTE for each month.	9/25/00
111	Les Munjas	Robert Wilkinson	Please provide a listing of California Billing Telephone numbers (BTNs) for April, 1997; Sept. 1998; and June 1999.	9/25/00
112	Les Munjas	Robert Wilkinson	Please provide a listing of California BTNs receiving CTF and CHCF-B surcharge discounts during April, 1997; September, 1998; and June, 1999.	9/25/00
113	Les Munjas	Robert Wilkinson	Please provide a complete copy of the CBSS system procedures manuals	10/4/00
114	Les Munjas	Robert Wilkinson	Please provide a copy of the GTEDS/DCO's ISO9002 certification.	10/4/00
115	Les Munjas	Robert Wilkinson	Please provide a list of entities for which GTE California, Inc. and Contel reported intrastate telecommunications revenues and associated surcharges during the period February 1, 1997 thru December 31, 1999	10/4/00
116	Les Munjas	Robert Wilkinson	Please provide a description of the procedures in place during the period February 1, 1997 through December 31, 1999 to identify entities that purchase services for resale, and not subject to the CHCF-B and the CTF surcharges. Please provide a list of these entities.	10/4/00
117	Les Munjas	Walter Drabinski	Provide a copy of surcharge rate changes since program inception	10/4/00

118	Les Munjas	Walter Drabinski	Provide a copy of surcharge remittance sheets showing interest charges and the associated declaration form.	10/4/00
119	Les Munjas	Robert Wilkinson	Please provide a monthly breakdown of revenues and associated surcharges by user and by class, e.g., tele-services used by: regulated utility and above-the-line operating centers, regulated utility and below-the-line operating centers, regulated-affiliates/subsidiaries, nonregulated-affiliates/subsidiaries for the period February 1, 1997 through December 31, 1999.	11/20/00

These information requests were processed to provide the data and information necessary to perform our review of procedures and controls in place for GTE-C and Contel-C to assess the CHCF-B surcharge and the CTF surcharge, and report the surcharge revenues to the CPUC; to verify that the surcharge revenues reported to the CPUC are the revenues billed by Verizon's Customer Billing Services System (CBSS); to reconcile the surcharge revenues reported on the CHCF-B and CTF Deposit & Declaration Forms to Verizon's monthly revenue and billing records; and to provide the data necessary to perform a sufficient test of transactions to determine that Verizon's billing and revenue reporting system is producing reliable information.

Review of Procedures and Controls

The review of procedures and controls included analysis of Information Requests 101, 102, 103, 104, 105, 108, 109, 113, and 114. In addition to obtaining and reviewing these data requests, the examination planning process included an overview of the surcharge billing process by Verizon's Regulatory Affairs staff in Irving, Texas.

Also, a site visit was made to Verizon's Customer Billing Center – West in Newbury Park, California. This visit included a physical review of the customer bill printing and distribution center, and a review of the quality control procedures applied to customer bills.

F1 The review of the Information Requests and the site visit outlined above indicate that adequate controls are in place and that the systems comply with company practices and policies.ii

The major components of the overall customer (surcharge) billing process and their physical location are:

- National Tables Group (NT) – Tampa Florida
- National Integrated Products and Services (NIPS) – Irving, Texas

ii / IR #102.

- Regulatory Staff West – Irving, Texas
- GTE Data Services/Data Center Operations (DCO) – Newbury Park, California
- Customer Billing West (Quality Assurance, Bill Printing and Bill Distribution Groups) – Newbury Park, California

The National Tables Group maintains the automated tables of attributes which interface with the CBSS system to provide the product, service, tax and surcharge rates to be applied to each customer's bill. Changes to tables are made only upon receipt of properly approved "Table Stars".

National Integrated Products and Services determines the specific products and services included in any order (external or internal), and prepares the Table Star for that customer order. Table Stars are also used to initiate and change tax rates and surcharge rates. Table Stars include General Information (company code, state, wholesale/retail), Date Information (target date, effective date), Requestor Information (name, department, phone), Tariff Information (tariff required, type, regulatory reference, effective date, approval date, OLTS number): and, Miscellaneous Information (regulated/deregulated, bill message, total ISOCs affected, product type). Table Stars may include several data attachments supporting the entries on the Table Star. They also include several approval entries and processing dates.

Regulatory Staff West maintains data regarding tariffs and monitors Table Stars for proper application of tariffed rates and surcharges.

GTE Data Services/Data Center Operations (DCO) operates, maintains and controls the hardware and systems that processes customer bills (CBSS system).

Customer Billing West prints and mails customer bills, and conducts continuous quality assurance reviews of customer bills.

F2 Internal audits by GTE/Verizon of Customer Billing Services System and End User Billing indicate that adequate controls are in place and that the systems comply with company practices and policies.iii

Three separate audits were conducted by the Internal Audit department of GTE/Verizon during the last two years that are applicable to this audit. Each audit reviewed different systems that are key to accurate collection of surcharges.

Review of the Surcharge Amounts for the Initial Payment to the CPUC for the CHCF-B and the CTF Surcharges for GTE California, Inc. and Contel's Network Services operations. (No. 99:045)

This audit report was issued on November 18, 1999. The scope of the audit included the following:

iii / IR #102.

- Verification of the weekly seven-day compound yield on taxable funds used in interest calculation to that printed in the Wall Street Journal between December, 1997 and May, 1999.
- Verification of the monthly surcharges for the CHCF-B and the CTF for the CTF for the above mentioned companies as recorded in the CBSS system between February, 1997 to May, 1999.
- A review of a sample of the company official charges in 1998 and 1999. These are the intra-company charges that are deducted from the monthly surcharge base for CHCF/CTF reporting.

The opinion of this audit was as follows:

“Based on the information reviewed, it appears that GTE has provided accurate information, as recorded in the CBSS reporting system, to the CPUC concerning surcharges for the CHCF-B and CTF for GTE California, Inc. and Contel California.”

GTE Network Services CBSS Application Audit (No. 00:323)

This audit report was issued on July 18, 2000 and addressed the Customer Billing Services System (CBSS) Application for the former GTE Network Services. The objective was to evaluate the adequacy of controls over CBSS operations and to ensure compliance with company practices and policies. Specifically the audit was aimed at determining that the CBSS application captured customer account data and provided accurate billing, reporting, and maintenance of customer accounts for the services and products the customers received. It should be noted that the CBSS application is mature and has been in production since 1991. The scope of the audit included:

- Policies and Procedures
- System Functionality
- System Environment
- System Management and Processes
- Production Support
- Data Integrity
- Logical Security
- Disaster Recovery and Backup.

The opinion of the audit was that the controls were good. The audit did not identify any reportable findings to indicate control weaknesses in the CBSS application.

GTE Network Services End User Billing Audit (No. 98:052)

This audit report was issued on November 23, 1998 and addressed End User billing functions performed by the Customer Billing Departments located in Ft. Wayne, Indiana and Thousand Oaks, California. The audit also visited the National Tables group in Tampa, Florida to gain an understanding of the interaction between the departments. The objectives of the audit included:

- Evaluate of adequacy of management and processing controls over End User Billing function.
- Ensure compliance with Company policies and procedures.

The opinion of the auditors was that the controls were good. While there were no significant findings, four minor recommendations for improvement were made.

F3 Verizon Data Services Data Center Operations have been certified by SGS International Certification Services Inc. (SGS).

SGS conducted an on site audit of the Verizon Data Services Data Center Operations in Newbury Park, California in September, 2000. SGS issued Certificate Number US98/1502 certifying that the quality management systems of Verizon's Data Systems Operations have been assessed and registered as meeting the requirements of ISO 9002/ANSI/ASQC Q002: 1994. The scope of the assessment included management, control, and operation of internal networks, computing systems, and applications to meet Verizon and Commercial Services business requirements

Verification of Surcharge Revenues Reported

Verification of surcharges reported included Information Requests 105, 106, 107, 110, 110 Supplemental, 111, 112, 117, and 118.

Information Requests #110 and #110 Supplemental provide key data for verifying that the monthly surcharge revenues recorded in the CBSS system were the monthly surcharge revenues reported to the CPUC.

Verizon's procedures for preparing the "Monthly Surcharge Transmittals" included downloading surcharge revenues from the billing system and accounting system to Excel worksheets. The Excel worksheets were then combined into two Excel schedules entitled:

CHCF-B Surcharge Transmittal Worksheet
And
CTF Surcharge Transmittal Worksheet

These worksheets for the period February 1, 1997 through September 30, 1999 are included in Appendix A - (Proprietary Information). These worksheets indicate the amounts reported to the CPUC.

To verify that the amounts included in these worksheets are the amounts from the CBSS billing system and Verizon's accounting system the following schedules were prepared:

- Schedule I – GTE – CHCF-B Surcharge – Analysis of Monthly Transmittals
- Schedule II – GTE – CTF Surcharge – Analysis of Monthly Transmittals
- Schedule III – Contel – CTF Surcharge – Analysis of Monthly Transmittals
- Schedule IV – Contel – CHCF-B Surcharge – Analysis of Monthly Transmittals

These worksheets for the period February 1, 1997 through December 31, 1999 are included in Appendix A – (Proprietary Information).

These schedules include the monthly data taken directly from CBSS/accounting system monthly reports. For each month the total surcharge revenues in these schedules were compared to the total surcharge revenues reported to CPUC. Each monthly difference was investigated and resolved.

F4 For the months of January, 1998 through December, 1998 a clerical error that occurred in working with the computer files resulted in under reporting CHCF-B surcharge revenues in the amount of \$133, 741 for GTE and CTF surcharge revenues in the amount of \$4,546 for Contel.

These amounts have been discussed with Verizon, and the additional amounts due are not disputed. The amounts shown above do not include interest. Details of the monthly amounts of these errors are included in Appendix A – (Proprietary Information) in the schedule entitled Exceptions Noted.

F5 For the months of February, 1997 through December, 1999 surcharge revenues on tele-services used by Verizon in the total amount of \$6,336,550 were not reported.

Verizon is unable to provide a breakdown of Company Official revenues between regulated (above-the-line) and non-regulated (below-the-line) operations. When a telecommunication service is requested by one of Verizon's entities, it completes an order that is submitted to the National Internal Provisioning Center (NIPC) for processing. Based on the information provided on the order, the NIPC determines whether to classify the service as Company Official (identified as "T") or business (identified as "B"). The determination is based on the company code, the location, and budget center. If the company code indicates it is Network Operations then a classification of "T" is given to the telecommunications service. No local service is billed for this classification, however, if toll calls are placed from this service, then these calls are treated as any other toll calls subject to appropriate taxes and surcharges. If a service is classified as "B", then all charges for this service are billed with appropriate taxes and surcharges. No information is provided when establishing a service that enables the processing center to determine whether a requested telecommunication service for Network Operations is regulated or non-regulated.

Monthly adjustments for surcharges on Company Official tele-services are shown in Schedules I through IV which are included in Appendix A – (Proprietary Information).

F6 A clerical error was identified in June, 1999, which resulted in under reporting of surcharges in the amount of \$46,056.

Details of the surcharge amounts due to CPUC as a result of this clerical error is included in the schedule entitled "Exceptions Noted" which is included in Appendix A – (Proprietary Information).

In June, 1999 the surcharge amounts due were calculated from preliminary revenue numbers. After all adjusting journal entries for the month of June, 1999 were posted, the

adjusted amount of surcharges due were not included in Verizon's monthly transmittal. Verizon reported and paid surcharges based on the unadjusted numbers.

F7 Surcharge rates for the CHCF-B and CTF have changed a number of times during the audit period. These changes were implemented by Verizon on a timely basis.

Each change in a surcharge rate is based upon analysis by the CPUC staff and the appropriate CHCF-B and CTF Committees as well as input from other intervenors. Based on the facts presented,

Resolution T-16165, July 2, 1998

On April 27, 1998 the California Teleconnect Fund (CTF) Interim Administrative Committee (IAC) filed a letter with the Executive Director of the Public Utilities Commission requesting that the All End User Surcharge (AEUS) used to fund the CTF be reduced from 0.41% to 0.05%. This resolution grants this request effective August 1, 1998.

The Interim Administrative Committee's April 28 Letter Request seeks to change the CTF surcharge level initially established in D.96-10-066 from 0.41% to 0.05%. The IAC's request is based on analysis provided in the Telecommunication Division's 1997 California Teleconnect Fund Annual Report. The IAC's letter request concurs with the Telecommunication Division's conclusion that the CTF surcharge is too high and should be lowered.

Resolution T-16374, December 16, 1999

On September 30, 1999, the California Teleconnect Fund (CTF) Administrative Committee (AC) filed with the Executive Director of the Public Utilities Commission its 2000 budget and surcharge rate level for year 2000. This proposed budget would maintain the All End User surcharge for year 2000 at the current rate of 0.05%. This resolution approves the year 2000 budget of \$33.472 million for the CTF program and the year 2000 surcharge of 0.05%. Further, this resolution approves a budget for the first six-month of year 2001 of \$16.932 million and a surcharge rate of 0.185% for the first six-months of 2001.

The AC's September 30, 1999 request seeks approval of its year 2000 budget and the maintenance of the current surcharge at 0.05% for 2000. This budget request was filed in compliance with Ordering Paragraph 24 of D.98-06-065. Further, this letter request is consistent with similar requests for other public programs that have submitted year 2000 budgets for Commission consideration. The AC indicated that its year 2000 budget is a forecast that is based upon an estimated/reported outlook for year 1999 and projected fund flows and expenses for the year 2000. As the last phase relating to the establishment of a trust account with Union Bank for CTF was adopted by the Commission in September 1999, the carriers are now depositing CTF surcharges and associated interest income held by the carriers from February 1997 to September 1999. All carriers are required to deposit these funds by November 12, 1999. Further, carriers are required to deposit in December 1999 the ongoing remittance of CTF surcharge revenues beginning with the surcharge revenues billed by the carriers during October 1999.

Resolution T-16244, December 3, 1998

On October 1, 1998, the California High Cost Fund - B (CHCF-B) Administrative Committee (AC) filed with the Executive Director of the Public Utilities Commission its 1999 budget. The adopted budget will increase the All End User surcharge for 1999 from its current rate of 2.87% to 3.8%. This resolution approves the 1999 budget of \$446.15 million for the CHCF-B and the 1999 surcharge of 3.8%.

The AC's October 1, 1998, letter request seeks approval of its 1999 Budget and the increase of the CHCF-B surcharge from 2.87% in 1998 to 3.40% in 1999. Even though the AC was not required by the Commission to submit its 1999 budget for the CHCF-B program, the AC filed this letter request in order to seek Commission approval for an increase in CHCF-B surcharge to 3.40%. Further, this letter request is consistent with other public programs that were submitting 1999 budgets on October 1, 1998, for Commission consideration. The AC indicated that its 1999 budget is an outlook and it is based upon a Pro-Forma outlook for years 1997 and 1998. As of October 1, 1998, the program is only partially implemented as the establishment of the trustee functions is not yet completed.

Resolution T-16365, December 2, 1999

On September 30, 1999, the California High Cost Fund - B (CHCF-B) Administrative Committee (AC) filed with the Executive Director of the Public Utilities Commission its year 2000 budget. The adopted budget will decrease the All End User surcharge rate to 2.6% in year 2000 from the current rate of 3.8% in 1999. This resolution approves for the year 2000 a budget of \$502.801 million and a surcharge rate of 2.6% for the CHCF-B.

The AC's September 30, 1999 letter request seeks approval of its year 2000 Budget and a CHCF-B surcharge of 2.4% for the year 2000, a decrease of 1.4% from the 1999 level of surcharge level of 3.8%. This budget request was filed in compliance with Ordering Paragraph 24 of D.98-06-065. Further, this letter request is consistent with similar requests for other public programs that have submitted year 2000 budgets for Commission consideration. The AC indicated that its year 2000 budget is a forecast that is based upon an estimated/reported outlook for year 1999 and projected fund flows and expenses for the year 2000. As the last phase relating to the establishment of a trust account with Bank of America for CHCF-B was adopted by the Commission in September 1999, the carriers are now depositing CHCF-B surcharges and associated interest income held by the carriers from February 1997 to September 1999. All carriers were required to deposit these funds by November 12, 1999. Further, carriers are required to deposit in December 1999 the ongoing remittance of CHCF-B surcharge revenues beginning with the surcharge revenues billed by the carriers during October 1999.

Investigation of Verizon CHCF-B and CTF Surcharges

**Exhibit -3
Surcharge Rates From Inception of Telecommunications Program**

Period	CHCF-B	CTF
02/01/97 to 12/31/97	2.87%	.41%
01/01/98 to 07/31/98	2.87%	.41%
08/01/98 to 12/31/98	2.87%	.05%
01/01/99 to 12/31/99	3.80%	.05%
01/01/00 Present	2.6%	.05%

F8 Results of IOSC tests revealed approximately \$91,000 in un-assessed surcharges due to incorrect tagging of IOSCs for surchargeability.

The company uses Item of Service Codes (IOSC's) in connection with its billing system to aid in producing customer bills. These codes are assigned to all customers for each type of service a customer may have. A rate is then assigned to each IOSC and the bill for local service is produced by the billing system multiplying each customer's IOSC's times the applicable rate. Each of these IOSC's are 'tagged' as taxable or nontaxable for add on type charges such as local and federal taxes or surcharges for the CHCF-B or CTF.

In IR #107 we obtained a complete listing of all California IOSC's in place since inception of the billing program. IOSC's in use totaled approximately 19,000. The IOSC's were identified as taxable or nontaxable for the applicability of CHCF-B and CTF. Each IOSC identified as nontaxable was challenged as to appropriateness of exemption.

The result of this procedure identified 54 items, which should have been surcharged, tagged as nonsurchageable. Due to lack of availability of detail item counts by IOSC throughout the period, the total estimated impact of the unsurcharged items was based on item counts currently in place. To estimate the total unreported surcharge, it was assumed the item quantities currently in place were consistent with item quantities throughout the test period.

D. ADDITIONAL SERVICE REQUIREMENT

In addition to the final attestation report, we were instructed to provide a detailed description of the following items for GTE California, Inc. for the period February, 1997 through December, 1999.

- What are the procedures in place to identify entities that purchase services for resell purpose and not subject to the CHCF-B and the CTF surcharges?

- Did GTE California, Inc. report intrastate telecommunications revenue and associated surcharges for other entities that GTE California, Inc. rendered billings for?
- Did GTE California assess and report surcharges on discounts associated with the Federal Communications Commission's discount program for schools and libraries?

Our findings regarding these issues are presented below:

F9 GTE California, Inc. and Contel of California have procedures in place to identify entities that purchase services for resell purpose.

A CLEC (Competitive Local Exchange Carrier) may order services through the California Resale Tariff or through contracts. The California Resale Tariff references the requirement that a reseller must be a certified CLEC as approved by the California Public Utilities Commission (CPUC) in order to obtain services from the resale tariff. Contracts must be approved by the CPUC and contain standard language representing the CLEC is a certified provider of local dial-tone service and that the CLEC must provide a copy of its Certificate of Operating Authority if requested before ordering services.

In order for a CLEC to be provided service in the GTE/Contel billing system (CBSS), it must first complete a CLEC profile. Included in the profile are the CLEC's Operating Company Number, Company Code and Customer Carrier Name Abbreviation. The CLEC also must represent and warrant to GTE/Contel that it is a certified provider of telecommunications service and document its Certificate of Operating Authority.

F10 Verizon has procedures in place to report intrastate telecommunications revenue and associated surcharges for other entities for which GTE/Contel rendered billings .

Carriers send data to Verizon in either invoice or non-invoice format. Invoice formatted data is provided by the larger carriers and is usually for those end users that are PIC'd to that carrier. Non-invoice formatted data is provided by all carriers (including those that also provide invoice data) and is usually for non-PIC'd end users that dial casually - 1010XXX.

If the carrier sends invoice formatted data, the taxes and surcharges are calculated by the carrier and included as part of the invoice. Verizon includes the carrier's invoice on a separate bill page in the ILEC bill. Verizon settles with the carrier for the amounts billed to the end users. The carrier has internal tax reporting information, and is responsible for remitting payment to the taxing authorities.

If the carrier sends non-invoice formatted data, Verizon calculates the taxes and includes these on the carrier's bill page. Verizon settles with the carrier for amounts billed to end users (including Verizon calculated taxes), and also provides the carrier various tax reports from CBSS on a monthly basis. The carrier is responsible for using these reports to remit payment to the taxing authorities.

F11 GTE/Contel has procedures in place to assess and report surcharges on discounts associated with the Federal Communication Commissions' discount program for schools and libraries.

Throughout the majority of the period under review, the company has treated customers receiving schools and library discounts as if they were not discounted customers for the generation of billing and surcharges. These customers were billed regular rates, and had the surcharges applied accordingly. The customer was then responsible for making application for reimbursement under the FCC program.

Effective October, 1999, Verizon began transitioning to a system whereby the customers were billed at the discounted rate. This was implemented on a limited basis through December 31, 1999. This type of customer bill was reviewed as part of our procedures to determine the surcharges were applied to a pre-discounted rate. Based on our procedures, surcharges were being appropriately assessed and reported for the FCC's schools and library discount program.

E. ACCOUNTANT'S REPORT

Investigation of Verizon CHCF-B and CTF Surcharges

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