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Audit Report

**TELECOMMUNICATIONS
ACCESS LINE FEES**

May 19, 2009

Office of the City Auditor
Austin, Texas

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This audit was conducted in compliance with the Generally Accepted Government Auditing Standards.

Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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City of Austin



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Date: May 19, 2009
To: Mayor and Council
From: Taylor Dudley, Acting City Auditor
Subject: Telecommunications Access Line Fees

I am pleased to present this audit report on telecommunications access line fees.

We found that, among the five providers audited in this phase of the project, access line fees due to the City of Austin total more than \$58,000. We also found that the Office of Telecommunications and Regulatory Affairs does not conduct regular reviews of access lines, and they do not notify all the local providers of annexations. Furthermore, the rules established by the Texas Public Utility Commission create difficulties for municipalities wishing to review access line reports.

We have issued four recommendations to assist the City of Austin in collecting revenue owed and minimizing future unpaid fees. Management has concurred with three of these recommendations and partially concurred with one.

We appreciate the cooperation and assistance we received from staff in the Office of Telecommunications and Regulatory Affairs during this audit.

Taylor Dudley, CIA, CGAP, CFE
Acting City Auditor

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COUNCIL SUMMARY

This report presents the results of the Telecommunications Access Line Fee audit. The purpose of this audit is to determine if the Office of Telecommunications and Regulatory Affairs (TARA) ensures that certificated telecommunications providers (CTPs) remit fees for all access lines within the Austin city limits. Currently 66 CTPs operate within the Austin city limits. We selected the ten largest CTPs, representing just over 98 percent of all the access lines in Austin. We completed an audit of five CTPs for Phase I. Phase II will include the remaining five and will be presented at a future Audit and Finance Committee meeting.

The City of Austin does not have franchise agreements with the CTPs. Instead, CTPs pay access line fees for use of City right-of-ways (ROW) for their communication lines. The Public Utility Commission of Texas (PUCT) establishes the rates for each municipality. The CTPs collect access line fees and pay the City.

The projected competitive landscape is changing with mobile phone usage up and landline use declining. Even with a growing population, Austin is experiencing a decline in revenue from access line fees due primarily to wireless penetration. Fewer access lines equal less revenue from access line fees for the City.

We found access line fees not remitted to the City of Austin total \$58,111 for the CTPs examined. We discovered 559 access lines that were mistakenly identified as either being outside the city limits or not recognized by the CTPs as owing the access line fee to Austin.

Further, we found while the City has no legal requirement to directly notify CTPs of annexations, TARA does notify the PUCT of Austin annexations, and this information is available to all the CTPs via the PUCT website. However, updates by the PUCT are not timely. TARA also, as a policy, notifies the three largest CTPs directly of annexations. The fact that the CTPs we audited had not remitted all access line fees due to the City in full purpose annexed areas may be attributable, at least in part, to a lack of direct notification from TARA about new annexations that affect the payment of these fees.

We found that TARA has never conducted a municipal authorized review of access line fees. We also found the PUCT rules would make it challenging for TARA to complete such reviews. This is in part because the standard for the type of information that CTPs must share with cities is open to varying and selective interpretation by the CTPs.

We have issued four recommendations for TARA as a result of our audit work. Specifically, we recommended that TARA:

- work to ensure that delinquent access line fees revenue identified in the audit is collected;
- conduct consistent reviews of CTPs;
- verify PUCT posting of annexation notices; and
- work with the City's Office of Intergovernmental Affairs to seek changes to the PUCT rules to improve the processes related to conducting municipal authorized reviews.

Management has concurred with three of the four recommendations and partially concurred with one recommendation.

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ACTION SUMMARY TELECOMMUNICATIONS ACCESS LINE FEES AUDIT



Recommendation Text	Management Concurrence	Proposed Implementation Date
01. To ensure revenues owed to the City are paid by responsible Certificated Telecommunications Providers (CTPs), the City of Austin Telecommunications and Regulatory Affairs (TARA) Officer should contact the CTPs audited to collect all unpaid access line fees.	Concur	3 rd calendar quarter of 2009
02. To ensure that CTPs are properly collecting and remitting access line fees, the TARA Officer should periodically conduct reviews of CTPs to improve compliance rates.	Partially Concur	N/A
03. To ensure that all CTPs are aware of jurisdiction changes that may affect the payment of access line fees to the City, the TARA Officer should verify that the annexation notification is posted on the PUCT website in a timely fashion.	Concur	Next full-purpose annexation approved by City Council.
04. To improve the processes and streamline the rules related to conducting municipal authorized reviews, the TARA Officer should work with the Office of Intergovernmental Affairs to partner with other Texas cities to seek changes to the Public Utility Commission of Texas rules.	Concur	N/A

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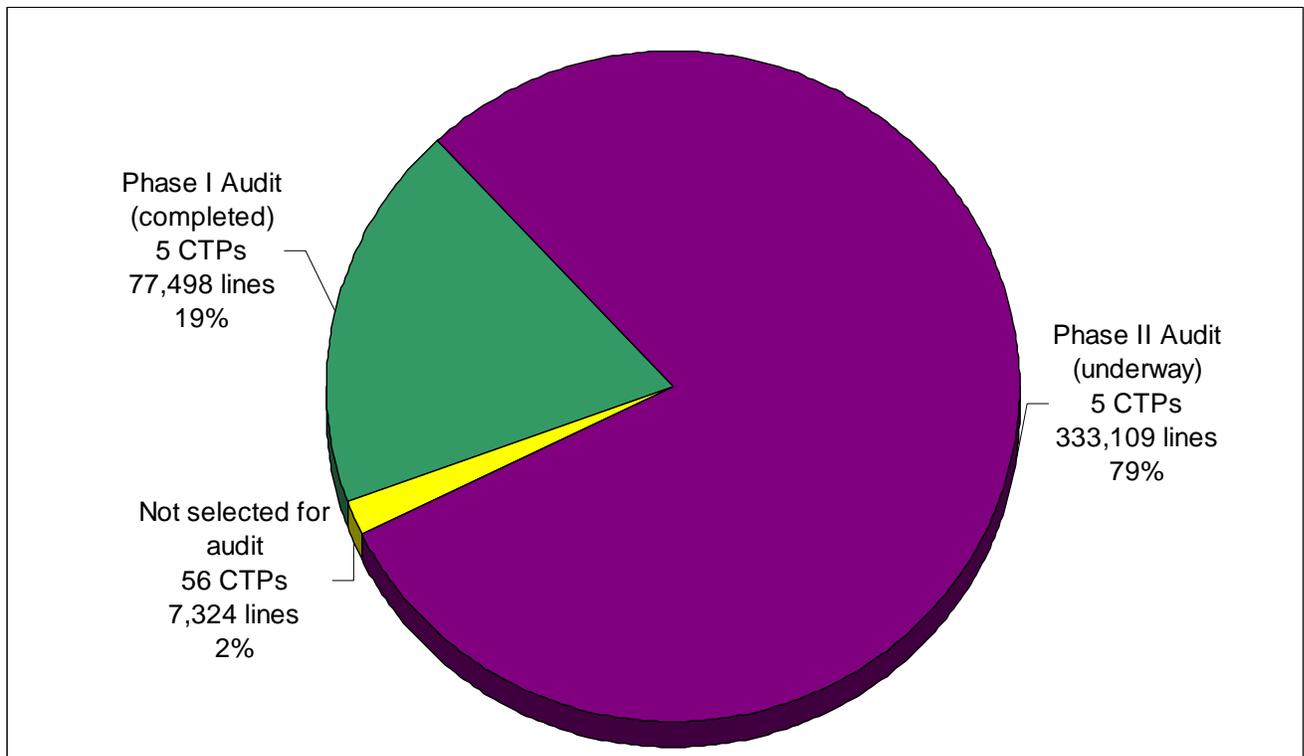
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BACKGROUND

This audit is one of a series of audits conducted by the Office of the City Auditor designed to explore the optimization of revenue. Prior revenue work includes sales tax, property tax, hotel occupancy tax, natural gas, and cable television audits. The goal of this Telecommunications Access Line Fee audit is to determine if the Office of Telecommunications and Regulatory Affairs (TARA) ensures that certificated telecommunications providers (CTPs) accurately remit access line fees for all telecommunications access lines within the Austin city limits. Currently 66 CTPs operate within the Austin city limits (as of the fourth quarter of 2008). For this audit, we selected the 10 largest CTPs, representing just over 98 percent of the access lines in Austin. This audit was split into two separate phases due to challenges we faced obtaining requested data from some CTPs in a timely fashion. Thus, we have audited five CTPs for Phase I, the results of which are presented in this report. Phase II, which is currently underway, includes the remaining five CTPs and will be presented at a future Audit and Finance Committee meeting. The chart below shows our audit coverage of the CTPs with access lines in Austin and the relative number of access lines represented by each group.

EXHIBIT 1
CTP Line Counts: Audited vs Unaudited



SOURCE: CTP quarterly filings with the Public Utility Commission of Texas, unaudited

The City of Austin does not have franchise agreements with the CTPs. Instead, the Public Utility Commission of Texas (PUCT) monitors access line reporting for CTPs serving the local market. TARA, a division of the Financial and Administrative Services Department, does play a local regulatory role in overseeing the private use of public ROWs.

CTPs use access lines as the transmission path connection to their customers. When these lines are located within a public ROW, the providers must compensate the municipality for ROW use. The PUCT establishes the ROW usage rates for each municipality. The CTPs collect access line fees from customers and pay the City. The revenue goes to the City's General Fund.

TARA could review this revenue through a process called a municipal authorized review (MAR), established by PUCT Rule 26.469. A MAR is not an audit and is not necessarily a review of revenue; it is simply a review of business records or quarterly filings. A municipality must submit notification of intent to review within 90 days of the provider's filing its quarterly access line report. The CTPs determine which types of business records are relevant, depending on the municipality's stated purpose for the review. PUCT rules state that if cooperative efforts between the parties have failed to resolve all issues related to the authorized review, the commission staff may mediate any dispute(s) filed by the CTP or the municipality. A formal complaint may be filed with the Commission by either a CTP or municipality to resolve remaining disputed issues not settled by informal dispute resolution.

Trends in mobile phone usage have impacted CTPs. The PUCT has recently warned the State Legislature regarding the future of wireless phone usages versus landline phone usage. According to PUCT's Report to the 81st Texas Legislature, *Scope of Competition in Telecommunications Markets*:

The telecommunications industry continues to undergo rapid change both in Texas and nationally. Much of the change has been driven by technological advances and investment in mobile wireless and broadband technologies. Two of the indicators for these changes are the increase in mobile wireless subscribers and the decline in land-line subscribers, so that today in Texas, there are roughly twice as many mobile wireless subscribers as land-line subscribers served by incumbent local exchange carriers.

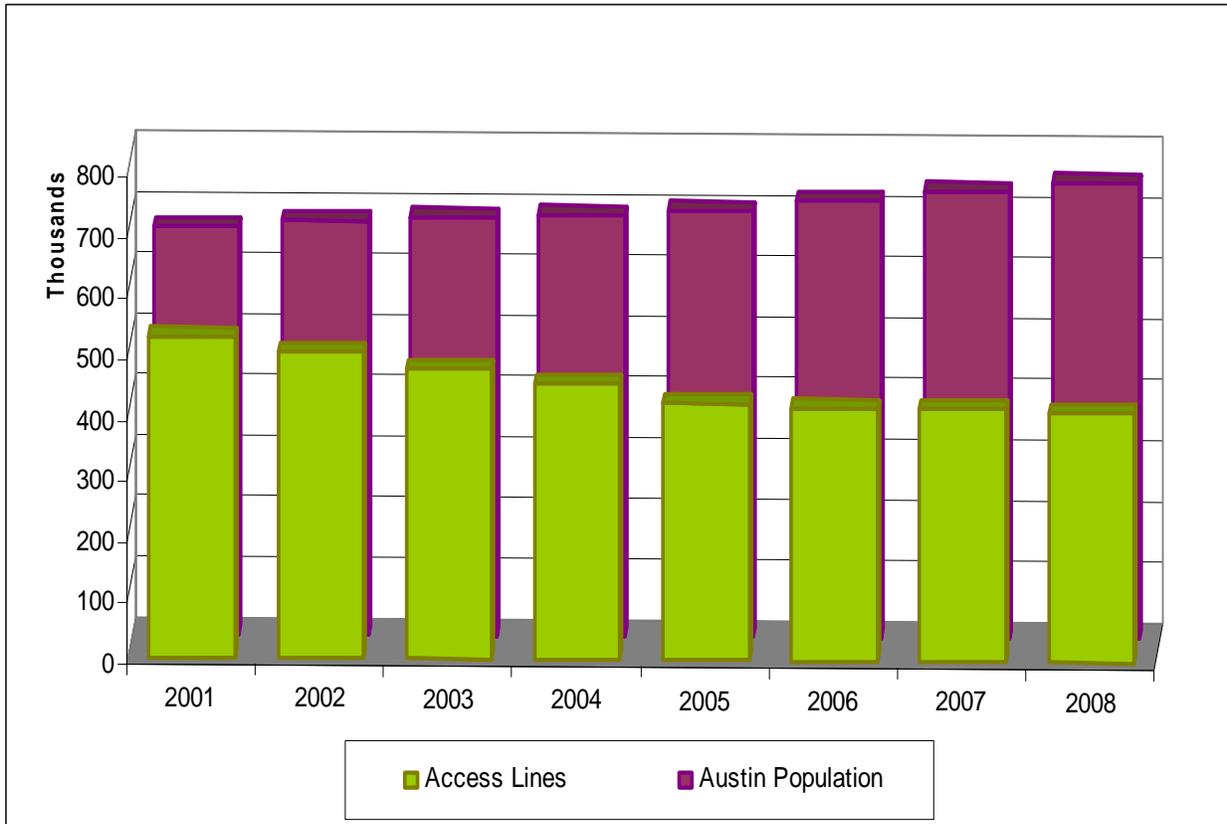
This Report to the Texas Legislature goes on to explain that:

Mobile phones have had a huge impact on consumer telephone use. According to the FCC, the overall wireless penetration in the United States has reached 80 percent and virtually everyone between the ages of 15 and 69 has a wireless phone. Texas ranked second in the nation in June 2007 with 18.8 million wireless subscribers, nearly 79 percent of its population. Wireless phones are increasingly serving as a substitute for traditional wireline telephone service.

Thus, the projected competitive landscape is changing with mobile phone usage up and landline usage declining. The chart below demonstrates how wireless penetration has impacted Austin's access line trend; access lines are decreasing even as population rises.

EXHIBIT 2

Though Austin's Population Has Increased, the Number of Access Lines Has Declined

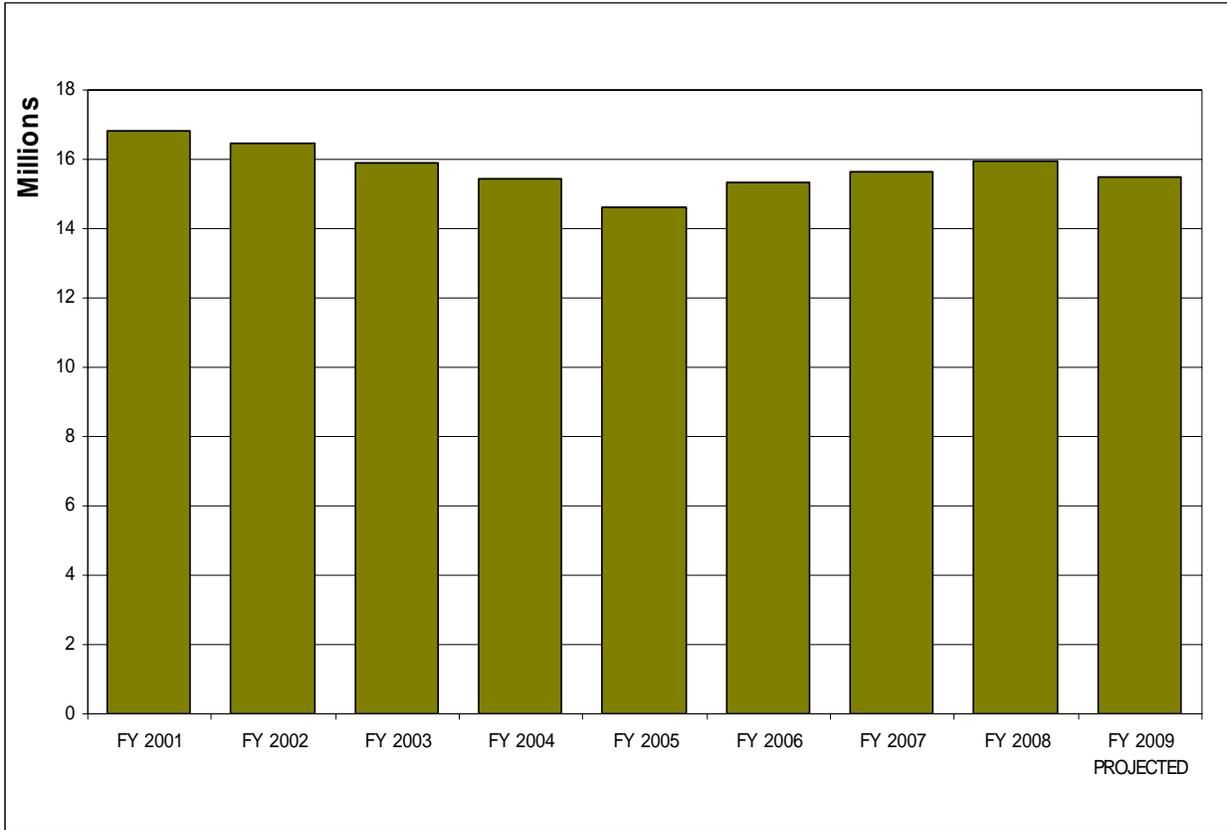


SOURCES: Austin's population figures obtained from the City of Austin Demographer, unaudited; access line figures obtained from the CTP quarterly filings with the Public Utility Commission of Texas, unaudited.

The result is that the access line fee revenue has not kept pace with population. The chart below shows revenue from access line fees for FY 01 through FY 08, along with the estimated revenue for FY 09.

EXHIBIT 3

Since 2001, City of Austin Access Line Fee Revenue Has Fluctuated and Declined Overall



SOURCE: Office of Telecommunications and Regulatory Affairs, unaudited

Revenue has increased in the last few years, despite decreasing numbers of access lines. Wireless penetration primarily impacts residential lines rather than business lines, and the rates for residential lines are much lower. Residential and business lines both declined from 2001 to 2005, resulting in a drop in revenue. Since 2005, residential lines have continued to decrease, while business lines have increased slightly. Though this, combined with the steady increase in access line rates, has contributed to a rise in revenue, current levels are still below those from 2001, and TARA projects that access line revenue will decline slightly in FY 09.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

The objective of this audit was to determine if the City of Austin Office of Telecommunications and Regulatory Affairs (TARA) ensures that certificated telecommunications providers (CTPs) accurately remit access line fees for all telecommunications access lines within the City limits.

Scope

The scope comprised the controls in place and activities carried out by TARA related to access line fees. For our data analysis, the scope also included all accounts paying access line fees within Austin zip codes. We analyzed data for a single quarter from each of the CTPs audited. Four out of the five CTPs provided data from the first quarter of 2008; the fifth CTP provided data from the fourth quarter of 2007. For calculating revenue related to non-conforming addresses we extended the scope to 2000, when the access line fee was initiated.

Methodology

To accomplish the audit objectives we performed the following steps.

- Obtained an understanding of the legal issues and Public Utility Commission of Texas Rules surrounding municipal authorized reviews.
- Obtained an understanding of the activities carried out by TARA to assure that the City receives the revenue to which it is entitled from CTPs.
- Obtained data sets for each of the five CTPs.
- Analyzed and geocoded data obtained from the CTPs.
- Identified addresses within the Austin full-purpose jurisdiction for which the City of Austin was not receiving access line fees (non-conforming addresses).
- Calculated the revenue owed to the City for the non-conforming addresses.

To calculate the revenue owed to the City for non-conforming addresses, we multiplied the number of lines at each address by the rate for the relevant line type (residential, business, or point-to-point). To estimate past liability, we multiplied the lines reported for the quarter audited by the relevant rate for each month dating back to the service activation date, annexation date or inception of the access line fee in 2000 (whichever is more recent).

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

For purposes of this audit, we did not conduct a municipal authorized review as defined by the PUCT Substantive Rules. Those rules include restrictions on information gathering that might result in a scope limitation per GAGAS. These restrictions are detailed further in the Audit Findings section of this report.

AUDIT RESULTS

The Certificated Telecommunications Providers (CTPs) we audited underpaid access line fee revenue to the City totaling \$58,111 for the period audited, due mainly to not updating customer records to include all customers in the Austin full purpose jurisdiction area. Additional revenue could accrue to the City if the Telecommunications and Regulatory Affairs Office (TARA) conducted regular municipal authorized reviews of the CTPs and notified all CTPs when annexations occurred. However, restrictions for municipal authorized reviews under Public Utility Commission of Texas (PUCT) rules might make it challenging to carry out such reviews.

CTPs examined failed to remit telecommunications access line fees for all lines within the city limits, resulting in \$58,111 due to the City of Austin. We discovered 559 access lines that were mistakenly identified as either being outside the city limits or not recognized by the CTPs as owing access line fees to Austin. We found that all CTPs examined owed additional access line fees to the City of Austin for the period audited. The table below shows the calculated liability for the quarter audited and the total calculated liability.

EXHIBIT 4
Money Owed to Austin for Non-Conforming Addresses

TELECOM	NON-CONFORMING ACCESS LINES SINGLE QUARTER	ACCESS LINE FEE LIABILITY SINGLE QUARTER	ACCESS LINE FEE LIABILITY ACCUMULATION
CTP A	290	\$1,157	\$4,712
CTP B	24	\$350	\$10,272
CTP C	78	\$1,117	\$19,939
CTP D	47	\$685	\$12,718
CTP E	120	\$1,691	\$10,471
TOTAL	559	\$5,000	\$58,111

SOURCE: OCA analysis of non-conformance based on records provided by CTPs

Using the access line count records provided to us by the five CTPs audited, we calculated the access line fee liability for the quarter audited to be \$5,000. After taking into consideration the length of time the lines were non-conforming based upon service activation and annexation dates, we estimated the total accumulated liability for all five CTPs audited to be \$58,111. Though our scope included all years since 2000, we found that most non-conforming accounts dated back no earlier than 2004.

The total amount owed to the City is a function of two factors: the type of line (business versus residential) and the length of time the customer has been receiving service. Therefore, the CTP with the most non-conforming addresses will not necessarily be the CTP with the largest liability to the City.

TARA does not regularly conduct municipal authorized reviews of the larger CTPs to ensure continued compliance. The PUCT Rule 26.469 establishes a municipal authorized review process (MAR), which enables municipalities to review access line records maintained by CTPs. However, TARA management has stated that they have been unable to conduct any

audits of telecommunications access line fees due to a lack of resources. We have found in other assessment work conducted such as the Hotel Occupancy Tax series, the Texas Gas Services audit, and the Time Warner Cablevision audit that a planned regular cycle of audits can yield revenue for the City and increase compliance rates.

When full purpose annexations are approved by City Council, TARA directly notifies only 3 of the 66 CTPs currently registered with the City. The City is under no legal requirement to directly notify CTPs of annexations affecting payment of access line fees. However, per policy, TARA does notify three of the largest CTPs directly of City of Austin full-purpose annexations. Specifically, TARA directly notifies one of the five CTPs audited in Phase I and two of the five that will be a part of Phase II audit work. This leaves 63 CTPs that TARA does not directly notify about annexations that may result in changes to access line fee payments.

TARA does notify the PUCT of Austin annexations, and this information is made available to all the CTPs via the PUCT website. However, we found that the PUCT does not always update the information on its website in a timely manner. The lack of direct, timely notification of all CTPs when full-purpose annexations occur could be one reason that these providers fail to remit all applicable access line fees to the City.

The PUCT rules related to municipal authorized reviews (MAR) make it challenging to complete reviews of the access line fee revenue. While municipalities may request information informally, CTPs are not required to comply with reviews or audits that do not follow MAR procedures. The standard for the type of information that CTPs must share with cities is open to varying and selective interpretation by the CTPs, and the CTPs can limit MARs to on-premise records which cannot be removed or reproduced except at the discretion of the provider. Additionally, CTPs may redact customer-specific information and/or require non-disclosure agreements in order to protect confidential or proprietary information.

As an example, a number of the CTPs being audited for Phase II have claimed that they can not provide service addresses of their customers, only billing addresses. This is significant due to the fact that many CTP customers have billing addresses in other jurisdictions, and this creates challenges in pinpointing whether the customers were within the City's jurisdiction or elsewhere. The methodology adjustments this necessitates have not yet been fully realized. Nothing in PUCT rules requires a CTP to provide a municipality with any data that the CTP thinks is not necessary to the review. Since the PUCT rules do not specify a particular methodology for MARs, it is difficult for a municipality to say that any record type must, by definition, be necessary.

Additionally, the PUCT rules contain only very limited sanctions and no clear consequences for CTPs who choose not to fully cooperate with cities conducting MARs. According to PUCT rules, commission staff may mediate disputes filed by the CTP or municipality, and if any disputes remain unresolved, the CTP or municipality may file a formal complaint. However, unlike other portions of the PUCT rules, the rules allowing MARs contain no penalties for failure to comply.

After a search of major Texas cities' audit work as well as other sources, we believe that this audit is only the second audit of its type done in the State of Texas by a city. Difficulty in obtaining access line data from the CTPs may be a contributing factor to this low number of assessments completed.

Legislative changes to State law that would trigger rule changes at PUCT would enhance Austin's and all other Texas cities' ability to verify that CTPs are properly collecting and remitting access line fees.

Recommendations

01. To ensure revenues owed to the City are paid by responsible Certificated Telecommunications Providers (CTPs), the City of Austin Telecommunications and Regulatory Affairs (TARA) Officer should contact the CTPs audited to collect all unpaid access line fees.

MANAGEMENT RESPONSE: CONCUR

TARA will coordinate with the OCA to send out payment demand letters.

02. To ensure that CTPs are properly collecting and remitting access line fees, the TARA Officer should periodically conduct reviews of CTPs to improve compliance rates.

MANAGEMENT RESPONSE: PARTIALLY CONCUR

TARA does not have revenue auditing resource, however, TARA recommends that the Office of the City Auditor continue conducting regular audits of CTPs with existing revenue auditing resources.

03. To ensure that all CTPs are aware of jurisdiction changes that may affect the payment of access line fees to the City, the TARA Officer should verify that the annexation notification is posted on the PUCT website in a timely fashion.

MANAGEMENT RESPONSE: CONCUR

TARA will continue to notify the Public Utility Commission via email of full-purpose annexations to post on their website for CTPs. Austin currently has 62 CTP's which can change quarterly. The PUC is the regulatory authority and the single point of contact used by CTPs for all updates, correspondence, and annexation notices from municipalities. Within four (4) business days of sending notification to PUC, TARA will verify annexation notification has been posted to the PUC website. If not, TARA will forward another reminder notice to the PUC.

04. To improve the processes and streamline the rules related to conducting municipal authorized reviews, the TARA Officer should work with the Office of Intergovernmental Affairs to partner with other Texas cities to seek changes to the Public Utility Commission of Texas rules.

MANAGEMENT RESPONSE: CONCUR

TARA will work with the City's Government Relations Office and Law Department to develop the best approach to advocate for an improvement in the processes and streamline rules and/or legislation related to municipal authorized reviews.

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APPENDIX A
MANAGEMENT RESPONSE

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April 24, 2009

To: Taylor Dudley, Acting City Auditor

In response to the recommendations resulting from the Telecommunications Access Line Fee Audit:

1. **To ensure revenues owed to the City are paid by responsible Certificated Telecommunications Providers (CTPs), the City of Austin Telecommunications and Regulatory Affairs (TARA) Officer should contact the CTPs audited to collect all unpaid access line fees.**

TARA will coordinate with the OCA to send out payment demand letters.

2. **To ensure that CTPs are properly collecting and remitting access line fees, the TARA Officer should periodically conduct reviews of CTPs to improve compliance rates.**

Management concurs that regular audits should be conducted; however, TARA does not have revenue auditing resources, however, TARA recommends that the Office of the City Auditor conduct periodic reviews of CTPs with existing revenue auditing resources.

3. **To ensure that all CTPs are aware of jurisdictional changes that may affect the payment of access line fees to the City, the TARA Officer should verify that the annexation notification is posted on the PUCT website in a timely fashion.**

TARA will continue to notify the Public Utility Commission via email of full-purpose annexations to post on their website for CTPs. Austin currently has 62 CTP's which can change quarterly. The PUC is the regulatory authority and the single point of contact used by CTPs for all updates, correspondence, and annexation notices from municipalities. Within four (4) business days of sending notification to PUC, TARA will verify annexation notification has been posted to the PUC website. If not, TARA will forward another reminder notice to the PUC.

4. **TARA should work with the Intergovernmental Affairs Office to plan a campaign to partner with other Texas cities to request changes to the Texas Public Utility Commission rules to improve the processes and streamline the rules related to conducting municipal authorized reviews.**

TARA will work with the City's Government Relations Office and Law Department to strategize and advocate for an improvement in the processes and streamline rules and/or legislation related to municipal authorized reviews

Sincerely,

Rondella M. Hawkins, Manager, Office of Telecommunications & Regulatory Affairs

cc: Leslie Browder, Chief Financial Officer

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ACTION PLAN
TELECOMMUNICATIONS ACCESS LINE FEES AUDIT

Rec #	RECOMMENDATION TEXT	Concurrence	Proposed Strategies for Implementation	Status of Strategies	Responsible Person/ Phone Number	Proposed Implementation Date
01	To ensure revenues owed to the City are paid by responsible Certificated Telecommunications Providers (CTPs), the City of Austin Telecommunications and Regulatory Affairs (TARA) Officer should contact the CTPs audited to collect all unpaid access line fees.	Management concurs with recommendation.	TARA will coordinate with the OCA to send out payment demand letters.	Planned	Rondella Hawkins, 974-2422	3 rd calendar quarter of 2009
02	To ensure that CTPs are properly collecting and remitting access line fees, the TARA Officer should periodically conduct reviews of CTPs to improve compliance rates.	Management concurs that periodic reviews of CTP's should be conducted; however we recommend OCA conduct periodic reviews with existing revenue auditing resources. For this reason, we partially concur with recommendation.	TARA does not have revenue auditing resources, however, TARA recommends that the Office of the City Auditor conduct periodic reviews of CTPs with existing revenue auditing resources.	N/A	Rondella Hawkins, 974-2422	N/A

Rec #	RECOMMENDATION TEXT	Concurrence	Proposed Strategies for Implementation	Status of Strategies	Responsible Person/ Phone Number	Proposed Implementation Date
03	To ensure that all CTPs are aware of jurisdiction changes that may affect the payment of access line fees to the City, the TARA Officer should verify that the annexation notification is posted on the PUCT website in a timely fashion.	Management concurs with recommendation.	TARA will continue to notify the Public Utility Commission via email of full-purpose annexations to post on their website for CTPs. Austin currently has 62 CTP's which can change quarterly. The PUC is the regulatory authority and the single point of contact used by CTPs for all updates, correspondence, and annexation notices from municipalities. Within four (4) business days of sending notification to PUC, TARA will verify annexation notification has been posted to the PUC website. If not, TARA will forward another reminder notice to the PUC.	N/A	Rondella Hawkins, 974-2422	Next full-purpose annexation approved by City Council.

Rec #	RECOMMENDATION TEXT	Concurrence	Proposed Strategies for Implementation	Status of Strategies	Responsible Person/ Phone Number	Proposed Implementation Date
04	TARA should work with the Intergovernmental Affairs Office to plan a campaign to partner with other Texas cities to request changes to the Texas Public Utility Commission rules to improve the processes and streamline the rules related to conducting municipal authorized reviews.	Management concurs with recommendation.	TARA will work with the City's Government Relations Office and Law Department to strategize and advocate for an improvement in the processes and streamline rules and/or legislation related to municipal authorized reviews.	Planned	Rondella Hawkins, 974-2422 and John Hrcir, Government Relations Office and Law Department	2009-2010