



Secretary of State Audit Report

Oregon Public Utility Commission: Residential Services Protection Fund Surcharge Reporting and Remittance Can Be Improved

Summary

PURPOSE

The purpose of our audit was to determine whether the Oregon Public Utility Commission (PUC) ensured that telecommunication providers reported and remitted all calendar year 2006 Residential Services Protection Fund (RSPF) surcharge revenue to which the state was entitled.

BACKGROUND

The Oregon Public Utility Commission (PUC) administers three telephone assistance programs. One helps individuals with low incomes pay their telephone bills. Another loans specialized telephone equipment to people with hearing, vision, speech, or mobility impairments. The third program assists individuals who are deaf, hard of hearing or speech impaired by relaying messages verbally or over a text telephone to the hearing parties to whom they are communicating.

The three programs are funded by a monthly surcharge of up to \$.35 per telecommunication access line, which goes into the Residential Service Protection Fund (RSPF). The PUC is responsible for ensuring telecommunication providers report and remit the surcharge for their access lines.

RESULTS IN BRIEF

While the PUC collected a quarterly average of about \$1 million in RSPF revenue during 2006, our analysis of PUC and Oregon Department of Revenue (DOR) tax records showed that the state could be entitled to as much as \$18,800 in additional RSPF revenue for the last quarter of 2006.

Furthermore, our analysis using Federal Communications Commission (FCC) data suggests as much as \$110,000 more in RSPF revenue may have gone underreported during the fourth quarter of 2006.

Finally, we found that some VoIP and prepaid wireless providers did not believe their customers were subject to paying the RSPF

surcharge, even though other VoIP providers did pay it. According to the Oregon Department of Justice, PUC's authority to impose RSPF charges on VoIP customers is unclear under current Oregon statutes.

The FCC data mentioned above may include some VoIP and pre-paid wireless lines. Because the data were not available in provider-specific form, we were unable to determine the dollar amounts associated with these types of access lines. Accordingly, if the RSPF tax does not apply to these lines, some portion of the \$110,000 figure cited above would not represent missing RSPF revenue. Notwithstanding the uncertainty about whether the RSPF surcharge applies to these lines, we believe that some of them may result from Oregon providers that did not report to either PUC or DOR, but should have.

While PUC has not needed to rely on revenues from VoIP and prepaid wireless customers, if current trends continue and more people shift away from traditional service to these emerging technologies, RSPF revenue could decrease to a level that would impact PUC's ability to maintain the RSPF programs.

When we examined the reasons for the uncollected surcharges, we found that PUC could improve its process for ensuring that amounts it receives are complete and that all providers are complying with RSPF reporting and remittance requirements. This includes increasing its use of available information in order to improve compliance and educating the providers and the public about entities that are exempt from paying the RSPF surcharge.

AGENCY ACCOMPLISHMENTS

During the course of our audit, PUC reported several actions it took to improve the RSPF reporting and remittance process. For example, it revised the remittance process and the filing instructions, and educated providers on the RSPF surcharge requirements.

RECOMMENDATIONS

We recommend PUC take the following actions:

- Continue to improve the way it manages reporting and remittance of RSPF surcharges by using internal information to ensure provider payments are reasonable and to identify nonfilers and underreporters.
- Continue to explore the possibility of exchanging information with DOR and performing comparisons to ensure the accuracy of access lines reported on remittance forms.
- Work with DOR, Oregon Emergency Management, FCC and others who may have information about providers to develop and maintain a comprehensive and current list of providers operating in the state.
- Work with DOR and providers to identify unpaid RSPF surcharge amounts from prior years, and collect amounts owed, when possible.

- Obtain clarification from the Oregon Department of Justice regarding the RSPF surcharge's applicability to prepaid wireless customers.
- Determine the future funding needed to support RSPF programs and whether the current RSPF statute provides a sufficient and sustainable source of revenue. Consider whether PUC should pursue legislation that would clearly establish its authority to impose the RSPF surcharge on VoIP and prepaid wireless customers.
- Continue to educate providers about RSPF requirements, including exemptions from paying the surcharge, and changes to the requirements.
- Educate the public about exemptions.

AGENCY'S RESPONSE

The Oregon Public Utility Commission generally agrees with the recommendations.

Background

In 1987, the Oregon Legislature passed a law supporting the state's public policy that adequate and affordable residential telephone service be available to all Oregonians. Based on that legislation, the Oregon Public Utility Commission (PUC) implemented three telephone assistance programs:

- Oregon Telephone Assistance Program (OTAP)
- Telecommunication Devices Access Program (TDAP)
- Oregon Telecommunications Relay Services (OTRS)

OTAP allows Oregonians who receive certain types of federal or state assistance, such as food stamps or Medicaid, to also receive up to a \$13.50 reduction in their monthly bill for local residential telephone service. According to PUC, 37 telecommunication providers provided OTAP assistance to an average of about 62,500 Oregon families during calendar year 2006.

TDAP loans specialized telephone equipment at no cost and with no income restrictions to eligible Oregonians who have at least one of the following impairments: hearing, vision,

speech or mobility. According to PUC, in December 2006, there were about 3,600 Oregonians who used specialized equipment from the TDAP program.

The OTRS program provides full telephone accessibility to people who are deaf, hard of hearing, or speech impaired. Trained specialists complete all calls and stay on the line to relay messages electronically over a text telephone, (also called a TTY), or verbally to people who are able to hear. In the second half of 2006, an average of 50,000 monthly calls were relayed for Oregonians.

These programs are funded by a monthly surcharge of up to \$.35 per telecommunication access line. This fee is known as the Residential Services Protection Fund (RSPF) surcharge. During calendar year 2006, the surcharge was \$.08 and generated about \$4 million in RSPF surcharge revenue.

The majority of surcharge revenue comes from traditional and wireless lines. The program also receives money from some telecommunication providers that employ computer technology to relay voice communication via the Internet, also known as Voice-over Internet Protocol (VoIP).

Some entities are exempt from paying the monthly surcharge. These include federal, state and local governments, regional housing authorities, certain federally chartered corporations, and others.

Telecommunication service providers collect the surcharge from customers and remit it to PUC. Providers with 1,000 or more customers report and remit the RSPF surcharge monthly. Providers with fewer than 1,000 customers can remit it either monthly or quarterly.

Audit Results

While the PUC collected an average of about \$1 million in RSPF revenue per quarter in 2006, our analysis of PUC and Oregon Department of Revenue (DOR) data revealed that the state could be entitled to as much as \$18,800 in additional RSPF revenue for the last quarter of 2006.

We also found that access line information from the Federal Communication Commission (FCC) suggests as much as \$110,000 more in RSPF surcharge revenue may be owed to the state for the same period.

We conducted this audit as an extension of our audit of the

Department of Revenue's management of the 9-1-1 tax program. That audit is documented in the Secretary of State's Report No. 2007-23, titled Oregon Department of Revenue: 9-1-1 Tax Review, issued September 19, 2007.

Some Providers Failed to Report or May Have Underreported Access Lines to PUC

We identified 18 providers that did not pay the RSPF surcharge to PUC during the fourth quarter of 2006. This represents about 14 percent of the 129 providers in our analysis.¹ Based on remittance information these providers reported to DOR, the state could have been entitled to about \$3,500 in additional RSPF revenue for the last quarter of 2006. This amount corresponds to about 44,000 quarterly access lines or about 14,500 monthly customers.

We also found that an additional 10 providers, or about 8 percent of the 129 providers in our analysis, reported about 191,000 fewer quarterly access lines to PUC than to DOR.² This represents more than \$15,300 in potentially lost revenue from an average of 64,000 monthly customers. We contacted the providers responsible for approximately 98 percent of these 191,000 lines, but they did not provide us with an explanation for the apparent underreporting.

Based on our review of the laws and rules governing the RSPF surcharge and the 9-1-1 tax, we would expect providers to report similar numbers of lines to PUC and DOR. However, in addition to the above potential underreporting, we noticed that, in general, providers rarely report the same

number of access lines to the two agencies. In fact, only 22 out of the 129 providers or about 17 percent reported the same number of lines to both agencies.

We believe the results of our comparison of PUC and DOR reporting highlight the need for PUC to work more closely with providers to ensure compliance with RSPF surcharge requirements.

FCC Data Show More Revenue May Be Missing

In addition to the missing revenue we identified by comparing PUC and DOR data, our analysis of FCC data suggests as much as \$110,000 more may have been owed to the state for the last quarter of 2006.³ Wireless lines account for about 80 percent of this amount, or about \$88,000, and traditional lines account for the remaining 20 percent, or about \$22,000. Wireless lines include some pre-paid accounts, and traditional lines may include some VoIP lines. As discussed below, some providers of these types of services question whether the RSPF requirements apply to their customers. However, because the data were not available in provider-specific form, we were unable to determine the dollar amounts associated with these types of access lines. Therefore, if the RSPF surcharge does not apply to these lines, some portion of the \$110,000 does not represent missing RSPF revenue.

Notwithstanding the uncertainty about whether the RSPF surcharge applies to VoIP and prepaid wireless lines, we believe that some

of the additional unreported lines may result from providers operating in Oregon that did not report to either PUC or DOR but should have. For example, we used past DOR remittances and identified six providers that paid the 9-1-1 tax in recent tax periods, including the first three quarters of 2006. None of these providers paid the RSPF surcharge or the 9-1-1 tax for the last quarter of 2006. We were unable to determine whether these providers went out of business, merged or simply stopped reporting to DOR. However, if they continued to offer service to end consumers in Oregon, they may have been required to report and remit both RSPF surcharges and 9-1-1 taxes to PUC and DOR, respectively.

Industry Changes Could Impact Future Program Funding

In recent years, customers have started to shift from using traditional phone lines to using new telecommunication technologies. This shift could have a detrimental effect on future RSPF funding if PUC is unable to collect the surcharge from providers of these new technologies.

Advances in Telecommunication Technology Are Transforming the Way People Communicate

In recent years, some people have switched from traditional lines to wireless and VOIP technologies. Specifically, when we reviewed data reported to DOR, we noted that traditional line use is slowly decreasing, as the popularity of wireless and VOIP services increases. For example, between 2002 and 2006 wireless lines grew by 64 percent, while traditional lines decreased by 13 percent. During the same period, VoIP adoption was even more dramatic growing almost seven fold from 2002 to 2006. Furthermore, between the last quarter of 2005

¹ These providers reported to PUC, DOR, or both agencies during the last quarter of 2006.

² These providers reported in excess of five percent fewer access lines to PUC than to DOR.

³ The FCC makes provider data available in aggregate form. These data are self-reported by providers and are not audited by the FCC. They are, however, certified by one officer at each provider that files. In addition, the \$110,000 estimate does not include exempt lines, which we eliminated from the FCC aggregate data based on data we obtained from PUC, and assumes that providers could collect 100 percent of the \$110,000.

and the last quarter 2006 alone, VOIP usage more than doubled.

Applicability of RSPF Surcharge to Some Providers Needs Clarification

This apparent shift from traditional telecommunication services to new technology could have a detrimental effect on future RSPF funding. This is especially true in the case of VoIP and prepaid wireless. We found that some providers of these technologies had been remitting the RSPF surcharge for some time, while others thought the surcharge did not apply to their customers.

When we followed up on this issue we determined there are no specific exclusions noted for these types of lines in the state laws and rules governing the RSPF surcharge. Moreover, the surcharge uses the same definition of customers subject to or exempt from the surcharge as that used for the 9-1-1 tax and, according to Oregon Emergency Management (OEM), the agency that manages the state's 9-1-1 program, the 9-1-1 tax should be assessed on both VoIP and prepaid wireless customers.

However, we also found that PUC sought clarification from the Oregon Department of Justice (DOJ) regarding the RSPF's applicability to VoIP lines. According to DOJ, PUC's authority to impose RSPF charges on VoIP customers is unclear under current Oregon statutes.

While PUC has not needed to rely on revenues from VoIP and prepaid wireless customers, if current trends continue and more people shift away from traditional service to these emerging technologies, RSPF revenue could decrease to a level that would impact PUC's ability to adequately fund the RSPF programs.

The PUC Can Improve Its Oversight of Telecommunication Providers

Oregon Administrative Rules direct providers to file remittances with PUC. The PUC is responsible for ensuring providers properly remit and report the RSPF surcharge. In order to fulfill this responsibility, PUC may audit providers and use available information to estimate surcharges due.

We noticed PUC did not have a process for assuring that amounts received were complete and that all providers were complying with RSPF surcharge reporting and remittance requirements. In addition, we noted that PUC could increase its use of available information in order to improve compliance.

The PUC Does Not Verify Whether Surcharge Remitted Is Complete

The PUC does not have a process to identify providers that may underreport their surcharge liability or not report at all. PUC staff processes remittances, registers new providers, updates them on surcharge reductions or increases and follows up if a provider unexpectedly stops reporting. However, staff does not perform analytical work to verify the reasonableness of payments. For example, staff does not estimate surcharges due and follow up when payments fall short of estimates or use available information to identify providers that may not be reporting the RSPF surcharge.

This work is necessary because as noted earlier, some providers may not report at all or may underreport. For example, one of the 11 non-reporting providers we contacted was unaware it was not complying. This provider had been remitting the RSPF surcharge along with its 9-1-1 tax to DOR instead of submitting separate amounts to the

two state agencies. In 2007, this provider started to report to PUC. Another non-reporting provider had been collecting the surcharge for several years and not remitting it. The PUC is now working with this provider to ensure compliance. In addition, several non-reporting providers we contacted were unaware of RSPF requirements or unsure whether the surcharge applied to them.

Of the 11 providers we contacted regarding not reporting RSPF during the last quarter of 2006, six are now filing, according to PUC. Three of the six providers even paid surcharge amounts for previous periods. Furthermore, according to PUC, an additional 13 providers registered to pay the RSPF surcharge in 2007. In total, these 19 providers remitted about \$65,000 in RSPF funds for 2007 and past years.

Some Providers Are Charging Exempt Customers

We found that some providers are charging exempt customers. Specifically, we surveyed 12 entities that appeared to be exempt from paying the RSPF surcharge and found that seven of them were assessed the surcharge during the course of our audit. We were unable to determine the full effect, as we could not develop a complete list of exempt entities and their total number of access lines. However, we identified several hundred exempt lines, including some state lines, for which state agencies paid the RSPF surcharge. Providers told us that they generally rely on customers to notify them if they are exempt. However, most of the exempt entities in our survey were not aware that they qualified for an exemption, nor had they requested exempt status.

PUC Has Not Fully Used Available Information

The PUC receives and stores provider information for various

business purposes. This information, even though not now used for the RSPF program, could prove valuable in identifying providers that may not comply with RSPF requirements. For example, we compared the names of providers that participated in the OTAP program to names of providers that reported RSPF during the fourth quarter of 2006. This analysis revealed several OTAP providers that were not complying with RSPF requirements. The PUC has since worked with these providers to remedy the situation. We also identified one additional OTAP provider that had not been complying with the RSPF surcharge requirements for several years. In 2007, this provider remitted surcharges owed since 2003.⁴

In addition, we used another PUC source, annual reports providers file with PUC, to identify providers that may be operating in Oregon and therefore should be subject to the RSPF surcharge. We found 10 providers active at the end of 2005 that did not pay the RSPF surcharge for the last quarter of 2006.⁵ While some of these providers may have gone out of business during calendar year 2006, others could still have been operating at the end of 2006 and thus may have been subject to the RSPF surcharge requirements.

Valuable Information Is Not Available to the PUC

While we were able to perform our analysis using some publicly available information, we identified some of the uncollected revenue discussed earlier in the report by

⁴ This provider was included in the previously reported number of providers not complying with RSPF reporting and remittance requirements.

⁵ These providers were not included in the non-filer data reported previously, which we identified from our comparison of DOR and PUC remittance data.

comparing access lines reported to PUC for RSPF purposes to the lines reported to DOR for the 9-1-1 tax. The PUC is not currently able to replicate this analysis because it does not have access to DOR's information. While PUC could share its information with DOR, DOR considers the information it provided us for our audit to be confidential and has maintained it cannot share it with another state agency. However, both agencies would benefit from sharing some tax information in order to verify the completeness and reasonableness of the payments they receive.

During the course of our audit, PUC officials told us they contacted DOR regarding the possibility of exchanging tax information. According to PUC, DOR officials indicated they would research ways to collaborate with PUC without violating confidentiality rules.

Agency Accomplishments

During the course of our audit, PUC reported several actions it took to improve the RSPF reporting and remittance process. For example, PUC revised the remittance form and the instruction sheet to make the reporting and remittance process clearer and more user friendly. The PUC also worked with OTAP providers to correctly apply the RSPF surcharge to their customers.⁶ We also noted that, in an effort to inform providers of surcharge requirements and improve compliance, the PUC RSPF program manager gave a presentation at an Oregon

⁶ While OTAP is funded by the RSPF surcharge, customers who receive OTAP assistance are not exempt from the RSPF surcharge. Our audit revealed that some providers thought they did not have to assess the RSPF surcharge to OTAP customers.

Telecommunications Association meeting.⁷

Recommendations

We recommend PUC take the following actions:

- Continue to improve the way it manages reporting and remittance of RSPF surcharges by using internal information to ensure provider payments are reasonable and to identify non-filers and under-reporters.
- Continue to explore the possibility of exchanging information with DOR and performing comparisons to ensure the accuracy of access lines reported on remittance forms.
- Work with DOR, OEM, FCC and others who may have information about providers to develop and maintain a comprehensive and current list of providers operating in the state.
- Work with DOR and providers to identify unpaid RSPF surcharge amounts from prior years, and collect amounts owed, when possible.
- Obtain clarification from the Oregon Department of Justice regarding the RSPF surcharge's applicability to prepaid wireless customers.
- Determine the future funding needed to support RSPF programs and whether the current RSPF statute provides a sufficient and sustainable source of revenue. Consider whether PUC should pursue legislation that would clearly establish its authority to impose the RSPF surcharge on VoIP and prepaid wireless customers.
- Continue to educate providers about RSPF requirements,

⁷ The Oregon Telecommunications Association is a trade association representing the telecommunications industry in Oregon.

including exemptions from paying the surcharge, and changes to the requirements.

- Educate the public about exemptions.

Agency's Response:

We commend the research and analysis performed by the Audit Team, as well as their collaboration throughout this audit. They have made a number of valid observations and recommendations. We also appreciate the Team's acknowledgement of our efforts to improve RSPF surcharge reporting and remittance.

We value the Team's comments and believe that overall, the RSPF program functions well and, given the available resources, does a good job of collecting the vast majority of the surcharge due. We are committed to continuing our efforts to seek out new and improved methods to track the massive amounts of data in our ever-changing environment, and to continue to be good stewards of public resources.

In general, we agree with the Auditor's recommendations. We have made substantial progress in many of these areas since the initiation of this audit in early 2007. Below we address specific recommendations outlined in the audit report.

VoIP

Statutory language related to the collection of RSPF surcharges for VoIP lines lacks clarity as to just which types of technologies it pertains. Given this uncertainty, it would be legally challenging for us to attempt to impose the RSPF surcharge on all types of VoIP technologies. Oregon is not alone in struggling with this dilemma. Many states are wrestling with similar problems related to the complexities of applying surcharges to the various types of new technologies. This is a difficult, complicated and often times convoluted subject that

requires extensive exploration to address the many legal, policy and political issues related to emerging technologies. We will continue to pursue this issue. And as we do, we will also endeavor to obtain the status of prepaid wireless customers.

Exemptions

We provide general information, guidelines, and specific exemptions to telecommunication providers on the RSPF remittance form. We also make information about exemptions available to the general public on our website. In addition to these efforts, we will modify our website to make exemption information more accessible, and improve and increase our educational efforts to both the telecommunication providers and the public.

Department of Revenue Information

As the audit report noted, we have attempted to obtain relevant information from the Department of Revenue. However, according to DOR, their statute (ORS 314.840) does not allow them to share taxpayer information with us. We will continue to pursue this issue with DOR.

Policy option packages

In keeping with our desire for continual improvement, and consistent with this Audit Report, we have proposed two relevant policy option packages (POPs) in our 2009-2011 budget request. One of these POPs requests funding for the development of software to track and correlate the dynamic line count information on approximately 4.5 million lines for which the RSPF surcharge is collected and remitted each month or quarter.

The second POP requests a dedicated auditor to perform audit functions for all three of the RSPF programs—OTAP, OTRS, and TDAP. One of the primary duties of this position will be to audit the records of the 130 Oregon telecommunication providers to ensure accurate line count,

collection and remittance information.

Objectives, Scope and Methodology

The purpose of our audit was to determine whether the Oregon Public Utility Commission (PUC) ensured that telecommunication providers reported and remitted all calendar year 2006 Residential Services Protection Fund (RSPF) surcharge revenue to which the state was entitled.

To accomplish our objective, we analyzed revenue PUC received for the fourth quarter of 2006. More specifically, we compared access lines reported to PUC with those reported for the same time frame to the Oregon Department of Revenue (DOR) for the Emergency Communication Tax (9-1-1 tax).

While we did not perform detailed analysis on the first three quarters of 2006, we know of no significant event or policy changes that would have affected PUC's management of the program. Accordingly, we do not believe that RSPF receipts for the first three quarters of 2006 were significantly more complete than those in the fourth quarter. Therefore, we believe we can sufficiently answer our audit objective and affirm that PUC did not ensure that telecommunication providers reported and remitted all calendar year 2006 RSPF surcharge revenue.

We assessed the reliability of electronic remittance data we received from PUC and from DOR and deemed them to be sufficiently reliable for audit purposes.

Our audit methodology included comparing access lines reported to PUC with those reported to DOR for 911 tax purposes. We were able to make this comparison because both the RSPF surcharge and the 9-1-1 tax use the same definitions of access lines and exemptions. In addition, we sought input from telecommunication providers during a quarterly meeting of the

Oregon Telecommunication Association. Providers at that meeting stated that comparing access lines for the RSPF surcharge and the 9-1-1 tax was a valid and fair approach.

We allowed for a five percent difference between total access lines reported to PUC and to DOR for the fourth quarter of 2006. Thus, if the difference in the number of lines a provider reported to PUC and DOR was five percent or less, we did not include that provider in our findings.

In addition, to better determine the level of RSPF reporting, we used the most recently available aggregate telecommunication customer data from the Federal Communications Commission (FCC). We adjusted these June 2006 data to December 2006 by using growth factors we developed based on access lines reported to DOR between the second and fourth quarter of 2006. These data are self-reported by providers and are not audited by the FCC. While we were not able to test the reliability of these data, we determined that using the FCC aggregate numbers posed a minimal risk of material misstatement.

We subtracted an estimate of Oregon exempt lines from the total access line estimates we developed using FCC data adjusted by growth factors. To do so, we developed an exemption rate for each of the two categories of lines and applied it to the FCC aggregate totals in order to estimate the number of total possible Oregon exempt lines at the end of 2006.

We were not able to estimate the number of uncollectible provider accounts. Thus, the estimates of missing tax revenue that we developed using FCC data assume 100 percent collection.

In addition, in order to determine why providers reported different access lines to PUC and to DOR for the same timeframe, we

selected eight providers that reported fewer access lines to PUC and 11 that did not report at all. We contacted all of these providers and, of the 17 providers that responded to our inquiries, only one was able to support its reason for reporting different access lines to the two Oregon agencies. This provider did not owe RSPF surcharge to PUC for the fourth quarter of 2006, and thus we excluded this provider from our findings.

In order to identify telecommunication providers operating in Oregon, we used remittance records from PUC and DOR, as well as other publicly available information from PUC and FCC.

We reviewed applicable statutes and administrative rules and other related documents. We spoke to PUC staff and management, as well as to experts at the Oregon Telecommunications Association, the Cellular Telecommunication and Internet Association, Oregon Emergency Management, and other states.

We conducted our audit in accordance with generally accepted government auditing standards.



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Courtesies and cooperation extended by officials and staff of the Oregon Public Utility Commission were commendable and much appreciated.

This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained:

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