

STATEMENT OF GEORGE MCDONALD

**Universal Service Administrative Company Vice President,
Schools and Libraries Division**

Before the

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

HOUSE COMMITTEE ON ENERGY AND COMMERCE

July 22, 2004

SUMMARY OF STATEMENT OF GEORGE MCDONALD

Our internal controls at USAC are designed to ensure that commitment and disbursement of E-rate funds are consistent with FCC rules. Among the many tools we use to help assure compliance are: detailed application and invoice review procedures, denying funding commitments when appropriate, rejecting incorrect invoices, auditing program beneficiaries and service providers, recovering funds where rule violations are found, investigating whistleblower hotline complaints, supporting law enforcement investigations, and referring matters involving suspected program abuse to law enforcement authorities.

San Francisco Unified School District (SFUSD) has received funding in each year of the program. We have disbursed approximately \$6.4 million to various service providers for providing eligible products and services to SFUSD for the past six years. In regard to SFUSD's application for products and services to be provided by NEC, which is the focus of this hearing, we committed approximately \$48.6 million to SFUSD. SFUSD later cancelled those funding requests, and consequently, we never disbursed any of these funds.

I believe we made the wrong decision in response to this funding request and that we had information that should have provided a clear warning to us. My review of the file indicates that we had reason to question whether one of the pieces of documentation that SFUSD provided to us – its budget – had been improperly altered when it was submitted to us. We should have done more to assure ourselves that the budget SFUSD provided to us was accurate, but we did not. If we had, in light of what we have learned since, I believe we would have denied this funding request.

We sought SFUSD's budget as part of our review of whether SFUSD had the funds to pay the non-discount portion of the cost of eligible services and had acquired the goods and services not eligible for discount but necessary to make effective use of these services, such as computers and software. This particular review has been part of our application review procedures since the first year of the program, and we have strengthened this review every year.

For example, in the year in which we reviewed this particular application, our reviewers' notes were not entered into our computer system, and our reviewers brought novel issues to the attention of their supervisors orally. Today, reviewers note their observations in our computer system, and novel issues such as SFUSD's budget must be communicated in writing and are required to be addressed. Beyond these changes, we have established an additional layer of review through our quality assurance function to review the work of our application reviewers, which further safeguards program funds.

Since August 2001, we have provided support to the law enforcement investigation of NEC and strengthened our joint efforts with the FCC Inspector General and law enforcement agencies to protect the program from waste, fraud and abuse.

7/22/2004

Good morning, Mr. Chairman and Members of the Subcommittee. My name is George McDonald. I am the Vice President of the Universal Service Administrative Company (“USAC”) responsible for the Schools and Libraries Division. It is my privilege to be here today to speak with you again about USAC and its administration of the Schools and Libraries Universal Service Support Mechanism, commonly referred to as the “E-rate” program.

Overview

I appeared before this Subcommittee on June 17, 2004, and my statement at that time provided an overview of USAC and its administration of the E-rate program. In the interest of time, I will not repeat that overview, but I would like to reiterate a few key points.

Before we began making funding commitments in 1998, our internal controls were carefully reviewed by PricewaterhouseCoopers (PwC) and staff of the U.S. General Accounting Office (GAO). PwC provided an attest opinion about those procedures, and USAC implemented all of GAO’s recommended changes. As we have gained experience, we have strengthened some procedures and added others to continue to protect the integrity of the program and the Universal Service Fund. An early enhancement was the establishment of the whistleblower hotline, which receives an average of 100 calls per year. Our Special Investigations Team investigates every call and ensures that appropriate follow up action is taken.

Today we have an assortment of tools to help assure compliance with program rules. These include employing detailed application and invoice review procedures, denying funding commitments when appropriate, rejecting incorrect invoices, auditing program beneficiaries and service providers, recovering funds where rule violations are found, investigating whistleblower hotline complaints, supporting law enforcement investigations, and referring matters involving suspected program abuse to law enforcement authorities. But, as I indicated to you last month, it has become clear to us that we need another tool – a larger oversight presence in the field. We are now reviewing proposals we have received in response to a Request for Proposals (RFP) soliciting bids to conduct some 1,000 site visits a year. These visits will allow us to assess even more fully how E-rate funds are being used, to learn about and publicize best practices in education technology and program compliance, and to help ensure that products and services have in fact been delivered and are being used effectively.

Participation of the San Francisco Unified School District in the E-rate Program

Let me now turn to the participation of the San Francisco Unified School District (SFUSD) in the E-rate program. SFUSD has received funding in each year of the program. We have disbursed approximately \$6.4 million to various service providers for providing eligible products and services to SFUSD for the past six years. In regard to SFUSD's application for products and services to be provided by NEC Business Network Solutions, Inc. (NEC), which is the focus of this hearing, we committed approximately

\$48.6 million to SFUSD. SFUSD later cancelled those funding requests, and consequently, we never disbursed any of these funds.

Mr. Chairman, I regret to report to you that I believe we made the wrong decision in response to this funding request and that we had information that should have provided a clear warning to us. My review of the file indicates that we had reason to question whether one of the pieces of documentation that SFUSD provided to us – its budget – had been improperly altered when it was submitted to us. We should have done more to assure ourselves that the budget SFUSD provided to us was accurate, but we did not. If we had, in light of what we have learned since, I believe we would have denied this funding request.

We requested SFUSD's budget and other documentation as part of our review of whether SFUSD had the funds to pay the non-discount portion of the cost of eligible services and had acquired the goods and services not eligible for discount but necessary to make effective use of these services, such as computers and software. This particular review has been part of our application review procedures since the first year of the program, and we have strengthened this review every year.

For example, in the year in which we reviewed this particular application, our reviewers' notes were not entered into our computer system, and our reviewers brought novel issues to the attention of their supervisors orally. In this case, the issue of whether SFUSD's budget was accurate was a novel issue, and so the reviewer would have communicated the concerns orally. Today, reviewers note their observations in our computer system, and novel issues such as SFUSD's budget must be communicated in writing and are required to be addressed. The decision regarding the novel issue must be

documented before a final decision is made with respect to the application. Beyond these changes, we have established an additional layer of review through our quality assurance function to review the work of our application reviewers, which further safeguards program funds.

Since August of 2001, we have provided support to the law enforcement investigation of NEC in the form of documentation, answering numerous questions about the program in general and this application in particular, and meeting with law enforcement officials. As we provided this support, we coordinated closely with the Federal Communications Commission Office of Inspector General, and through that process, strengthened our joint efforts to protect the fund from waste, fraud and abuse by supporting law enforcement investigations of those who would take advantage of the program. As a result of our support of this investigation, we learned that SFUSD officials and NEC had provided us with false information in response to our many questions about this application.

Conclusion

Mr. Chairman, thank you for providing me with the opportunity to address the Subcommittee. I would be happy to respond to any questions you may have.

GEORGE MCDONALD BIOGRAPHY

Mr. McDonald is Vice President of the Universal Service Administrative Company (USAC) with responsibility for the Schools and Libraries Division. He was selected for that position in September 2001. Mr. McDonald manages all aspects of the Schools and Libraries Universal Service Support Mechanism.

Mr. McDonald joined the Schools and Libraries Corporation (the predecessor to the Schools and Libraries Division of USAC) in December 1997 as the Director of Operations. He oversaw development of the Program Integrity Assurance review process – the internal control procedures that help ensure that funds are used in accordance with FCC rules. Prior to joining SLC, Mr. McDonald served as the Deputy Director of Budget and Programs for the U. S. Department of Transportation (DOT). He helped manage the Department's budget of over \$40 billion and assisted with DOT's implementation of the strategic and performance planning requirements of the Government Performance and Results Act. During his 25 years with DOT, he also served in the National Highway Traffic Safety Administration and supported implementation of the requirements of the Americans with Disabilities Act in the nation's transportation systems. Prior to joining DOT, he served as a KC-135 navigator in the United States Air Force. Mr. McDonald received a B.A. degree in mathematics from Fordham University.

July 2004

House Committee on Energy and Commerce

Witness Disclosure Requirement - "Truth in Testimony"

Required by House Rule XI, Clause 2(g)

Your Name: George McDonald		
1. Are you testifying on behalf of a Federal, State, or Local Government entity?	Yes	No
2. Are you testifying on behalf of an entity other than a Government entity?	Yes	No
3. Please list any federal grants or contracts (including subgrants or subcontracts) which <u>you have received</u> since October 1, 1999: None		
4. Other than yourself, please list what entity or entities you are representing: Universal Service Administrative Company (USAC)		
5. If your answer to question number 2 is yes, please list any offices or elected positions held or briefly describe your representational capacity with the entities disclosed in question number 4: USAC Vice President, Schools and Libraries Division		
6. If your answer to question number 2 is yes, do any of the entities disclosed in question number 4 have parent organizations, subsidiaries, or partnerships to the entities for whom you are not representing? [Note: USAC is a subsidiary of the National Exchange Carrier Association, which I am not representing and which, pursuant to 47 C.F.R. §54.703(a), has a separate board of directors from USAC and is prohibited from participating in the functions of USAC.]	Yes	No
7. If the answer to question number 2 is yes, please list any federal grants or contracts (including subgrants or subcontracts) which were received by the entities listed under question 4 since October 1, 1999, which exceed 10% of the entities revenue in the year received, including the source and amount of each grant or contract to be listed: None		

Signature:



Date:

7/19/04