

Like its April 2005 report, this report first addresses implementation of recommendations the Staff made in the Staff's Initial Report Regarding the Impact of the Allegations of Criminal Activities by Kenneth Matzdorff on Missouri Utility Consumers, then addresses the implementation of directives of the Commission in the Commission's Order that established this Case No. TO-2005-0237.

The Staff's Initial Report Regarding the Impact of the Allegations of Criminal Activities by Kenneth Matzdorff on Missouri Utility Consumers - Recommendations

Kenneth M. Matzdorff relinquish all managerial and financial authority for Cass County Telephone Company L.P.

GVNW, through mssrs. Bob Schoonmaker and Scott Smith, is currently performing the duties of General Manager of Cass County Telephone. Staff understands that Mr. Matzdorff is still President/CEO of LEC, LLC and that he has been occupied with the affairs of LEC, LLC.

Rebecca Matzdorff be suspended by the Company from all managerial and financial authority for Cass County Telephone Company LP pending the completion of the Staff's investigation as directed by the Commission in Case No. TO-2005-0237.

Rebecca Malcolm (formerly known as Rebecca Matzdorff) is still Senior Vice President, Operations for LEC, LLC. According to her employment contract her duties include overseeing commercial operations and administration for LEC, LLC and its affiliates. LEC, LLC is the general partner of Cass County Telephone. Further, Ms Malcolm (Matzdorff) is the Vice President of Administration for New Florence Telephone Company.

The Staff explore all options to eliminate the role of LEC LLC regarding the ownership, financing, operation and financial affairs of Cass County Telephone Company LP and New Florence Telephone Company.

The Staff, through the Commission's General Counsel, contacted the Missouri Attorney General's Office regarding the feasibility of initiating a statutory receivership proceeding for Cass County Telephone. At this time, the Missouri Attorney General is reviewing the situation. The Staff already has filed a complaint case in pursuit of this recommendation and may bring others as its investigation continues.

The Staff initiate management audits of both Cass County Telephone Company and New Florence Telephone Company, to include but not be limited to: 1) quality of service, 2) the operations of the business office, and 3) related party transactions safeguards and controls.

This recommendation was incorporated into Case No. TO-2005-0237.

Update of the Engineering and Management Services Department:

Reviewed content of 9 notebooks of data request responses regarding quality of service and operations of the business office delivered to the PSC on March 14, 2005.

Made on-site visit to Cass County Telephone on April 14, 2005 and interviewed Scott Smith of GVNW.

Topics addressed with Mr. Smith included the following:

- Organizational Structure and Reporting Relationships of LEC, LLC and Cass County Telephone

- Contract with GVNW

- Operating Performance of GVNW

- Immediate and Long Term Goals and Objectives of GVNW for Cass County Telephone

- Job Documentation

- Billing and Payment Remittance Process

- Credit and Collections

- Martin System (Billing Software)

- Customer Contact

Staff is presently drafting some conclusions and potential recommendations for Cass County Telephone and continues to review data request responses received from the Company.

Staff plans to interview representatives from New Florence Telephone in the near future.

The Staff ensure that Century Tel and Spectra have in place an audit program and overall internal controls sufficient to detect possible wrongdoing and report the results of these efforts.

Staff has no new information to report regarding this area at this time.

The Staff explore Joint Audit option(s) with NECA, Federal Communications Commission, Universal Service Administrator Company, and other interested entities to minimize duplication of effort and improve overall knowledge of the audits and investigations of these matters.

The Kansas Corporation Commission (KCC) Staff submitted a joint KCC – MoPSC non-disclosure agreement to Cass County Telephone and LEC, LLC for consideration. The Staff received from KCC Staff on Friday, May 13, 2005 a counterproposal agreement made by Cass County Telephone and LEC, LLC that same day. The Staff is reviewing the counterproposal.

In its April status report, Staff noted the FCC is completing an audit of the Cass County Telephone Company high cost loop support for 2004 and that, while the full report cannot be released, the FCC indicated its willingness to share the findings and conclusions with Staff upon the receipt of the proper confidentiality agreement. Staff submitted a request for the findings and conclusions and the confidentiality agreement the FCC would require.

In the previous status report, Staff also indicated it, along with staff of the Kansas Corporation Commission, contacted the Universal Service Administrator (USAC) to discuss the possibility of sharing data between USAC and the state commissions. USAC was to discuss this possibility internally and respond back to both KCC staff and the Commission's Staff with its determinations.

On April 13, 2005, Staff was contacted by the FCC about the previous discussions with FCC staff and USAC staff. Because of the recent changes at the FCC, the FCC staff is reviewing the Missouri and Kansas statutes and/or rules and the confidentiality agreement to determine if sharing of data and findings and conclusions with the state commissions will be properly protected. As of April 26, 2005, the FCC still had not completed its review of the state protective order procedures. The Staff anticipates that the FCC will make its decision soon.

The Staff depose Kenneth Matzdorff, Rebecca Matzdorff and Controller Debi Long regarding the scope of their non-Missouri regulated telephone company activities, current Cass County operations, relationship and operation of LEC LLC, relationship and operation of Haug Construction, relationship and operation of Local Exchange Carriers, LLC, relationship and operation of the other firms identified in Section 5, and identification of other firms related to Mr. Matzdorff that have not yet been identified.

The Staff is collecting and reviewing data in preparation for these depositions. Data collection has been delayed by discovery disputes with LEC, LLC. The lack of the ability to have informal access to LEC, LLC employees due to restrictions dictated by LEC, LLC's management will require far more depositions than originally planned. General Counsel's Office attorneys are considering the applicability of section 386.470 RSMo, which requires parties to provide information and provides witnesses immunity from criminal prosecution for that information.

The Staff initiate discussions with Missouri LECs and Missouri Telephone Industry Association (MTIA) regarding development of a whistleblower program for Missouri telecommunications activities.

Staff has no further information to report at this time.

The Staff initiate discussions with interested parties to develop an affiliate transaction rule for small Missouri telephone companies.

Staff has no further information to report at this time.

The Staff modify the Missouri telephone company annual report format to include identification of related party transactions above a specified threshold and the amount of the transaction.

Staff has no further information to report at this time.

The Staff continue to work with federal agencies involved in the investigation of these matters.

The Staff is still working with USAC, the FCC and the U.S. Attorney's Office for the Western District of Missouri.

Case No. TO-2005-0237 – An Investigation of the Fiscal and Operational Reliability of Cass County Telephone Company and New Florence Telephone Company, and Related Matters of Illegal Activity

Network/Provisioning Quality

1. Information Requests: Staff has submitted data requests designed to obtain information necessary to conduct portions of the reviews and analyses listed below. These requests seek information on the following topics: Basic Service Orders Installed within 5 days; Installation Commitments; Operator Assisted Calls; Customer Assisted Calls; Originated Switch Calls; Local Exchanged Switched Calls; InterExchange Switched Calls; Customer Trouble Report Rate; Clearing Time Out of Service Trouble in < 24 hours; Repair Commitments; Held Service Order Logs; Directory Publication requirements and Consumer Bill Requirements. The information received will be used to perform the reviews in step 2 (Compliance with Commission Rules) and 3 (Analyze Outside Plant). ***Information was requested 05/02/2005 for New Florence. Information has been received and reviewed for Cass County.***

2. Review Compliance with Commission Rules: Staff is reviewing how the company tracks and tabulates its quarterly quality of service report. This review will reveal if the company's quality of service results are accurate and a true reflection of compliance with the Commission's service objectives for quality of service. In addition Staff will review compliance with other Commission rules. Staff conducted its ***initial on-site visit for CassTel on 03/29/2005. Visit regarding New Florence is scheduled 05/24/2005.***

3. Analyze Outside Plant: Staff is analyzing the condition of the company's outside plant facilities. This analysis consists of field investigations of various components of the company's outside plant facilities. Compliance with requirements contained in 4 CSR 240.32.60 and 4 CSR 240.18 will be specifically investigated. Staff will attempt to rate or score the overall condition of the company's outside plant facilities based on set criteria. **Cass County field investigation has been completed. Analysis is in progress. New Florence's field investigation began 05/16/2005.**

4. Analyze Central Office Facilities: Staff is analyzing the condition of the company's Central Office and Remote facilities, including digital line carriers located in the field. Compliance with requirements contained in 4 CSR 240.32.60 and 4CSR 240.18 will be specifically investigated. Staff will attempt to rate or score the overall condition of the company's switching facilities based on set criteria. **The Cass County inspection began 05/11/05 and the New Florence inspection is planned to begin 05/24/2005.**

5. Contractor Administrative Review: The Telecommunications Department is providing the Commission auditors assistance in their analysis of capital

improvement expenditures for Cass County and New Florence Telephone Companies. **Three (3) fiber plant design orders have been field reviewed at Cass County. Current copper and buried wire work orders are pending. New Florence field review began 05/16/2005.**

Receipt and Disbursement of Universal Service Funds

Data requests (21) have been issued in accordance the work plan.

Work has started to recreate the plant investment of Cass County Telephone and New Florence Telephone from the time the change in ownership took place from GTE to present. This approach will include but not be limited to validating and verifying the approvals, authorizations and payment process for plant investment, retirements and operation and maintenance of utility property.

A number of Cass County's Continuing Property Records ("CPRs") have been selected for testing. The construction projects have been and will continue to be located and field inspected to determine if the project was completed and providing service to the customer. Additionally, the legitimacy of the expenditures is being scrutinized.

Quality of the Books & Records

Staff has received a number of additional data request responses that are currently being reviewed.

Staff has conducted fieldwork in Peculiar, MO on a limited basis during April. More fieldwork time in Peculiar will be necessary during May as data request responses are being provided only onsite and it is anticipated that subpoena information will also be made available in Peculiar only.

The Staff is creating a spreadsheet to analyze Haug Construction invoices to Cass County Telephone Company during the years 1996 through 2004. The work orders recorded on the invoices will be cross checked against Continuing Property Records (CPRs). The posting of expenditures as repair and maintenance expenses versus asset additions are being verified. Payment of the invoices will be traced through the check register and bank statements. A comparison of unit pricing will be completed to determine if affiliate transactions are in compliance with FCC rule.

Copies of LEC, LLC invoices for 2003 have been traced back through the 2003 Cass County Telephone Company general ledger to verify their inclusion in expenses. This work has created the need for further inquiry related to general

ledger postings as preliminary audit results have found entries not supported by an invoice provided previously to Staff in earlier data requests.

The Staff is compiling information to cross check annual report submissions with audited financial statements. An analysis of LEC, LLC charges posted to various expense accounts by year has been completed. This work allows the Staff to determine the annual proportion of CassTel's expenses that consist of LEC, LLC charges by separate expense account.

Both New Florence Telephone Company and Cass County Telephone Company have submitted amended 2003 annual reports to the Commission. The GCO has requested amended 1996-2002 annual reports based upon admissions from LEC, LLC's president, Kenneth Matzdorff, that invoices were falsified.

The Staff has completed an analysis of Cass County Telephone Company and New Florence Telephone Company check registers for the years 2002 through 2004 for all checks issued over \$1,000. A list of affiliated companies has been compiled and it is updated as new information is discovered. Invoice payments have been verified through analysis of corresponding bank statements. Additional inquiry of transactions appearing on bank statements has is outstanding. Further analysis of the 1996 through 2001 check registers is ongoing.

The Staff has requested a sample of vendor invoices for years prior to 2002 similar to those requested 2002-2004. This material will be reviewed in Peculiar, MO.

Staff reviewed the Martin software manual used by LEC, LLC for accounting functions. This analysis will assist Staff in determining the internal control procedures of LEC, LLC in order to develop a conclusion regarding their effectiveness.

Staff's work has been severely delayed by the lack of access to the documents *subpoenaed* from LEC, LLC. The LEC, LLC costs appear to be Cass County's largest expenditures and directly affect this investigation and Cass County's cost of service. As indicated by pleadings filed with the Commission LEC, LLC is providing access to documents requested. The documents to which access will be provided are reflected in attachments A and B. On Friday, May 13, 2005 the Staff first received documents requested in the *subpoenas*. Additional documents requested in the *subpoenas* first became available for review by the Staff on May 17, 2005 at LEC, LLC's headquarters in Peculiar, Missouri.

As stated in last month's status report, Staff's work has been slowed due to the Cass County and New Florence objections to the Staff's review of their external auditors' work papers and access to LEC, LLC employees. The financial statements of Cass County and New Florence have been significantly changed. The Staff has been unable to understand the basis for certain of the changes and the related quantification. Further, conclusions regarding the quality of the books and records have been hindered by LEC, LLC's denial of access to the underlying supporting audit tests conducted by the external auditor.

Ongoing Fiscal Reliability

Data requests have been submitted requesting indenture information for any loans outstanding at Cass County or LEC, LLC. Staff is awaiting Cass County's 2004 audited financial statements to identify the amount of outstanding debt and evaluate the Company's standing in relation to this debt through ratio analyses and other various financial measures.