

AN AUDIT

Universal Service Fund

Public Service Commission

02-14

August 2002

2001-2002 Joint Legislative Audit Committee Members

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August 21, 2002

Senator Gary R. George and
Representative Joseph K. Leibham, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator George and Representative Leibham:

As requested by the Public Service Commission (PSC), we have completed a financial audit of the Universal Service Fund, which was established to ensure that all state residents receive essential telecommunications services and have access to advanced telecommunications capabilities. Our audit report contains our unqualified opinion on the Fund's financial statements and related notes for the fiscal years ending June 30, 2001 and 2000.

The Universal Service Fund is funded through assessments of telecommunications providers, which totaled \$19.6 million in fiscal year (FY) 2000-01. The largest program supported by the Fund is the Educational Telecommunications Access Program, which is administered by the Technology for Educational Achievement (TEACH) Board. During FY 2000-01, \$10.5 million, or 59.4 percent of total fund expenditures, was spent on subsidies and grants for data lines and video links for schools, libraries, and others under this program.

Other programs supported by the Fund are operated by the PSC. Historically, expenditures for these programs have been significantly less than annual program budgets. For example, in FY 1999-2000, the budget for PSC-operated programs was \$8.0 million, but expenditures totaled only \$2.7 million. Although expenditures increased 69.3 percent during FY 2000-01 as the result of the implementation of new programs, modification of existing programs, and increased outreach efforts, PSC expenditures and outstanding encumbrances totaling \$5.8 million were less than the budget of \$6.9 million during FY 2000-01. As the result of recent legislation, the PSC may not assess more than \$5.0 million in FY 2003-04, and \$6.0 million in FY 2004-05 and each year thereafter for PSC-operated programs.

We appreciate the courtesy and cooperation extended to us by the staff at the PSC, TEACH, and the Fund's administrator, Williams Young, LLC, during the audit.

Respectfully submitted,

A handwritten signature in cursive script that reads 'Janice Mueller'.

Janice Mueller
State Auditor

JM/DA/ss

Summary

We have completed a financial audit of the Universal Service Fund, which was established under 1993 Wisconsin Act 496 to ensure that all state residents receive essential telecommunications services and have access to advanced telecommunications capabilities. The audit was requested by the Public Service Commission (PSC), which oversees the Fund, to fulfill its audit requirements under s. 196.218(2)(d), Wis. Stats. Our report includes our unqualified opinion on the Fund's financial statements and notes for fiscal years (FY) 2000-01 and 1999-2000.

The Universal Service Fund is funded by assessments paid by telecommunications providers, which totaled \$19.6 million in FY 2000-01, as well as interest earnings on cash balances. It supports telecommunications services and access that are provided by several state agencies, including the PSC, the Technology for Educational Achievement (TEACH) Board, the University of Wisconsin System, and the Department of Public Instruction. Expenditures from the Fund totaled \$17.7 million in FY 2000-01. From the Fund's establishment in 1996 through June 30, 2001, assessments have totaled \$58.5 million, and \$53.6 million has been spent on the Fund's programs. The fund balance as of June 30, 2001, was \$6.5 million.

The largest program supported by the Fund is the Educational Telecommunications Access Program, which is operated and administered by the TEACH Board. In FY 2000-01, 59.4 percent of the Fund's total expenditures, or \$10.5 million, supported the program, which helps to fund direct access to the Internet and two-way interactive video capabilities for public and private K-12 schools; private, tribal, and technical colleges; public libraries; and the Wisconsin School for the Deaf and the Wisconsin Center for the Blind and Visually Impaired. The FY 2000-01 expenditure level represented a 19.8 percent increase from FY 1999-2000.

Several of the other programs supported by the Fund were established and are operated by the PSC. These programs help people with disabilities acquire special telecommunications equipment, lessen the financial effect of rate increases on users, serve low-income individuals, help fund the purchase of medical telecommunications equipment, maintain selected public pay telephones, and help nonprofit groups facilitate affordable access to telecommunications and information services.

Since the PSC began managing these programs in 1996, their expenditures have been significantly less than their annual budgets. For example, in FY 1999-2000, the budget for PSC-operated programs and administrative expenses was \$8.0 million, but expenditures totaled only \$2.7 million. However, expenditures increased 69.3 percent during FY 2000-01, as the result of the implementation of new programs, modifications to existing programs, and increased outreach efforts. Despite this increase, PSC expenditures and outstanding encumbrances totaling \$5.8 million were less than the budget of \$6.9 million during FY 2000-01.

The Legislature requires the PSC to submit a budget for each of its programs. In addition, as part of 2001 Wisconsin Act 16, the Legislature capped the amount of assessments that could be collected from telecommunications providers to support the PSC-operated programs. As a result of this legislation, the PSC may not assess more than \$5.0 million in FY 2003-04, and \$6.0 million in FY 2004-05 and each year thereafter for PSC-operated programs.

In addition to the assessment and expenditure levels for the PSC-operated programs, the assessment of commercial mobile radio service providers, including wireless and cellular providers, has been an area of increasing legislative interest. The PSC promulgated an administrative rule and, in August 2000, began to assess these providers. However, in response to concerns that the assessments imposed an undue hardship on the developing industry, the Legislature's Joint Committee for Review of Administrative Rules suspended the portion of the rule that contained the effective date for the wireless and cellular providers' participation in fund assessments. Subsequently, the Legislature enacted a provision that would make wireless and cellular providers subject to contributions to the Fund only if the PSC promulgates rules designating such providers as eligible to receive funding under both federal and state Universal Service Fund programs. The PSC plans to further consider the issue of wireless and cellular assessments in its biennial review of Universal Service Fund rules.

Universal Service Fund Programs

The Universal Service Fund is funded through assessments paid by telecommunications providers.

The Universal Service Fund was established under 1993 Wisconsin Act 496 to ensure that all state residents receive essential telecommunications services and have access to advanced telecommunications capabilities. The Fund supports telecommunications services and access programs that are provided by several state agencies, including the Public Service Commission (PSC), the Technology for Educational Achievement (TEACH) Board, the University of Wisconsin System, and the Department of Public Instruction. The Universal Service Fund is funded through assessments paid by telecommunications providers, which totaled \$19.6 million in fiscal year (FY) 2000-01. While telecommunications providers are allowed to recover assessment costs from their customers, they may not establish a separate surcharge on bills to recover those costs.

The PSC is responsible for the overall policies and procedures related to the Fund but is directed by statute to contract with a private firm to administer the Fund. The PSC has contracted with Williams Young, LLC, a public accounting firm, for administrative services. At the request of the PSC, we completed a financial audit of the Universal Service Fund to fulfill the agency's audit requirements under s. 196.218(2)(d), Wis. Stats. As necessary parts of the financial audit, we reviewed controls over telecommunications provider assessments and expenditures of the programs financed through the Fund, and we assessed the fair presentation of the Fund's financial statements for FYs 2000-01 and 1999-2000.

Programs Funded

Most programs supported by the Universal Service Fund are operated by the PSC.

Most of the programs supported by the Universal Service Fund are operated by the PSC. However, in recent years the Legislature has made the Fund available to support programs operated by other state agencies. Descriptions, expenditures, and budget information for each of the programs supported by the Universal Service Fund are provided in the appendix.

The PSC programs that were supported by the Fund during FYs 2000-01 and 1999-2000 were:

- the Telecommunications Equipment Purchase Program, which provides financial assistance to help persons with disabilities in acquiring special telecommunications equipment;

- the Rate Ceiling Credit Program, which lessens the financial effects of rapid rate increases on users;
- the Lifeline and Link-up America programs, which provide support for low-income individuals to establish and receive basic telephone services;
- the Access Program or Project by Nonprofit Groups program, which provides grants to nonprofit groups for programs or projects that facilitate affordable access to telecommunications and information services;
- the Medical Telecommunications Equipment Program, which awards grants on a competitive basis to nonprofit medical clinics or public health agencies for the purchase of medical telecommunications equipment;
- the Public Interest Pay Telephone Program, which ensures that pay telephones remain or are installed at locations where there is a public need; and
- the Institutional Discount Program, which enables qualified public libraries, nonprofit schools, and nonprofit hospitals to receive discounted rates for new specialized telecommunications services, and which has been discontinued except for payments on commitments already made.

Under 1997 Wisconsin Act 27 and 1999 Wisconsin Act 9, the Legislature designated funding from the Universal Service Fund for several other programs that help provide telecommunications access to educational entities and that provide statewide Internet access to reference information. The largest of these programs is the Educational Telecommunications Access Program operated by the TEACH Board. In addition, during FY 2000-01, the Universal Service Fund provided:

- \$955,000 for four University of Wisconsin campuses to receive voice, data, and video services through BadgerNet, the State's voice, data, and video telecommunications infrastructure;
- \$1,692,767 for contracts with vendors that provide statewide access to reference databases of magazines and newspapers through BadgerLink, which is administered by the Department of Public Instruction; and

- \$45,500 for a contract with the National Federation of the Blind for *Newsline*, an electronic information service that provides dial-up access to audio versions of major national and regional newspapers for blind or visually impaired individuals.

Public Service Commission Programs

The PSC was authorized by 1993 Wisconsin Act 496 to promulgate, by administrative rule, universal telecommunications service programs to be funded from the Universal Service Fund. The PSC was also authorized to appoint a Universal Service Fund Council to advise it on the creation and implementation of these PSC programs. The Council consists of representatives of telecommunications providers and consumers of telecommunications services. Statutes require that a majority of its members be representatives of telecommunications consumers. Two areas of continuing legislative interest have been the expenditure levels for PSC-operated programs and the applicability of assessment provisions to commercial mobile radio service providers, including wireless and cellular providers.

Expenditure Levels

Expenditures for PSC-operated programs have been significantly less than budgeted.

In May 1996, the PSC first promulgated rules that formally established the programs it operates. During their first four years, PSC-operated programs' expenditures were significantly less than the \$8.0 million budgeted annually for them. For example, in FY 1999-2000, expenditures for PSC-operated programs and administration totaled only \$2.7 million. In response to the lower expenditure levels and increasing fund balance, the assessments through which telecommunications providers were required to fund PSC-operated programs were suspended from January 1998 through July 2000. In August 2000, these assessments were reinstated.

The Joint Committee on Finance requires the PSC to submit detailed expenditure plans for its programs.

To address concerns with the differences between budgeted and actual expenditures for PSC-operated Universal Service Fund programs, the Legislature enacted budgetary changes as part of 1999 Wisconsin Act 9. For FY 2000-01, \$8.0 million was placed in reserve in the Joint Committee on Finance's supplemental appropriation, to be released under s. 13.10, Wis. Stats., upon the Committee's approval of a detailed expenditure plan from the PSC. In addition, Act 9 required that the PSC submit a budget for each Universal Service Fund program, including budgeted expenditure levels by fiscal year, as part of its future biennial budget requests.

Expenditures for PSC-operated programs increased 69.3 percent during FY 2000-01.

The PSC submitted a \$6.9 million expenditure plan for FY 2000-01 that listed proposed expenditure levels for each of its Universal Service Fund programs. In July 2000, the Joint Committee on Finance approved the release of funds for this plan. Actual FY 2000-01 expenditures for PSC-operated programs and administration totaled \$4,525,676, which was 69.3 percent greater than the \$2,673,457 million spent in FY 1999-2000. In addition, \$1,230,803 of encumbrances were outstanding as of June 30, 2001.

1999 Act 9 both modified existing programs and authorized a program that provides grants to nonprofit medical clinics and health agencies to purchase medical telecommunications equipment. During FY 2000-01, the PSC expended \$357,359 and encumbered an additional \$139,272 for grants to seven medical clinics and health agencies under this new program.

The PSC also added its own programs and expanded existing programs as part of administrative rule changes that became effective in May 2000. For example, the Telecommunications Equipment Purchase Program, which provides financial assistance to help persons with disabilities acquire special telecommunications equipment, was expanded to allow the issuance of multiple vouchers to a single household to cover multiple qualified participants. In the past, households had been limited to one voucher regardless of the number of qualified recipients residing in the household. As shown in Table 1, expenditures for the Telecommunications Equipment Purchase Program increased 151.2 percent during FY 2000-01. The PSC also increased its outreach efforts to develop awareness of and participation in the Universal Service Fund's low-income support programs, such as Lifeline and Link-up America. As a result, expenditures for these programs also increased markedly during FY 2000-01.

Table 1

Increase in Expenditures for Selected PSC Programs

<u>Program</u>	<u>FY 1999-2000</u>	<u>FY 2000-01</u>	<u>Percentage Increase</u>
Telecommunications Equipment Purchase Program	\$643,453	\$1,616,067	151.2%
Lifeline Program	321,645	942,714	193.1
Link-up America Program	210,951	585,482	177.5

The Legislature capped the amount of future assessments that could be collected to support PSC-operated programs.

Even with increased program activity, FY 2000-01 expenditures and outstanding encumbrances were 16.6 percent less than the \$6.9 million included in the PSC's expenditure plan. In response to the lower program activity and expenditure levels, the Legislature enacted 2001 Wisconsin Act 16, which limits the amount of assessments on telecommunications providers to support the PSC-operated programs. As a result of this legislation, the PSC may not assess more than \$5.0 million in FY 2003-04, and \$6.0 million in FY 2004-05 and each year thereafter for PSC-operated programs.

Wireless and Cellular Providers

The assessment of wireless and cellular providers has also been an area of legislative interest. When the PSC undertook efforts to revise its administrative rules pertaining to Universal Service Fund programs, standing legislative committees requested modifications so that wireless and cellular providers would be subject to participation in the Universal Service Fund for the first time. In response, the PSC promulgated an administrative rule and, in August 2000, began to assess these providers.

Wireless and cellular providers objected to participation in the Universal Service Fund.

The wireless and cellular providers objected to participating in the Universal Service Fund and wished to have the ability to include a surcharge on customer bills for contributions to the Universal Service Fund that they would be required to pay. After a public hearing in October 2000, the Legislature's Joint Committee for Review of Administrative Rules voted to suspend the portion of the administrative rule establishing the effective date for the assessments, reasoning that the assessments imposed an undue hardship on an industry that is sensitive to rate increases and could negatively affect the development of competition, consumer choice, and infrastructure development. In November 2000, the PSC issued an order temporarily suspending the assessment of wireless and cellular providers until January 2002.

Bills that would have allowed either wireless and cellular providers or all providers to establish a surcharge that would bill customers for the contributions that providers are required to make to the Universal Service Fund were introduced in the 2001 legislative session, but failed to pass. In their place, the Legislature included a provision in 2001 Wisconsin Act 16 that wireless and cellular providers would be subject to contributions to the Universal Service Fund only if the PSC promulgates rules designating such providers as eligible to receive funding under both federal and state Universal Service Fund programs.

At the end of 2001, the PSC considered its options in response to both the suspension of assessments of wireless and cellular providers set to expire in January 2002, and 2001 Wisconsin Act 16. In December 2001, the PSC concluded that it was in the public interest to extend the suspension while it gives further consideration to the issue in its biennial review of Universal Service Fund rules.

Educational Telecommunications Access Program

**In FY 2000-01,
\$10.5 million was
spent for the Educational
Telecommunications
Access Program.**

In FY 2000-01, a total of \$10.5 million was spent on the TEACH-administered Educational Telecommunications Access Program, which is the largest program currently funded by the Universal Service Fund. This program provides subsidized access to new data lines for direct Internet access, as well as two-way interactive video links that also allow participants to view and respond to instructional presentations from off-site locations. Eligible entities, which include public and private K-12 schools; private, tribal, and technical colleges; public libraries; and the Wisconsin School for the Deaf and the Wisconsin Center for the Blind and Visually Impaired, are charged a maximum of either \$100 or \$250 per month, depending on the speed of their Internet data line or video link.

The program pays for equipment, for installation costs of the data lines and video links, and for ongoing costs in excess of the monthly charges paid by the eligible institutions. The actual access to a data line or video link is provided by telecommunications providers under contract with the Department of Administration. The telecommunications services are part of the State's voice, data, and video network known as BadgerNet. The State leases the network from the Wisconsin BadgerNet Access Alliance (WBAA), which is a consortium of private telephone companies and other telecommunications firms led by Ameritech, Inc. In 1998, the Department of Administration signed three contracts with WBAA, one each for voice, data, and video services, with the goal of obtaining a single rate for telecommunications services for the State and other participating Wisconsin agencies. The contracts for video links and data lines will expire in December 2005. The TEACH Board has financed its video link costs through the State's master lease program; its outstanding master lease obligation as of June 30, 2001, was \$23.0 million, which will be paid semiannually through 2006.

In addition to subsidizing new data lines and video links, the Educational Telecommunications Access Program also provides grants for data lines and video links that were in existence on or before October 14, 1997. Entities receiving funding for existing contracts may not also receive support for new data lines or video links. The existing contract grants component of the Educational Telecommunications Access Program, which was originally scheduled to sunset June 30, 2002, was extended through December 31, 2005 by the Legislature.

Subsidies and grants have been provided for 765 data lines and video links.

As of June 30, 2001, TEACH has provided subsidies for 161 new video links and 486 new data lines under the Educational Telecommunications Access Program. In addition, TEACH provided grants for 115 video links and 3 data lines that were in existence as of October 14, 1997.

For the 1999-2001 biennial budget, Educational Telecommunications Access Program funding was increased by \$10,528,700. In order to have more information on the demand and actual costs of the program before providing the full amount of additional expenditure authority, the Legislature transferred one-half of the funding increase to the Joint Committee on Finance's supplemental appropriation.

In January 2001, the Joint Committee on Finance approved a TEACH Board request to release \$2,035,000 from the Committee's appropriation for FY 2000-01. The requested amount was intended to cover projected cost increases in the Educational Telecommunications Access Program for the remainder of FY 2000-01. A large part of the requested amount, \$1.2 million, was to cover one-half the cost of three gateways for distance education networks. Gateways are used to allow video networks with different technology to connect.

In addition to funding from the Universal Service Fund, federal funding is also available for telecommunications access services through the federal E-rate program. The E-rate program consists of discounts applied to telecommunications services such as basic and long-distance telephone services, Internet access, and equipment to provide internal telecommunications connections. As a purchaser of telecommunications services, the TEACH Board applies for and receives the federal E-rate funds on behalf of school districts and libraries with TEACH-provided video links and data lines. In FY 2000-01, the TEACH Board applied \$1.5 million in federal E-rate funds to the Educational Telecommunications Access Program's outstanding balance in the State's master lease program. Federal E-rate funds have been used to support numerous other programs administered by the TEACH Board. Subsequently, in 2001 Wisconsin Act 16, the Legislature specified that E-rate funds would be expended for TEACH block grants and would offset general purpose revenue for the program. The Legislature estimated a general purpose revenue lapse of \$7.4 million over the 2001-2003 biennium as the result of using E-rate funds for the block grants.

Independent Auditor's Report on the Financial Statements of the State of Wisconsin Universal Service Fund

We have audited the accompanying balance sheet of the State of Wisconsin Universal Service Fund as of June 30, 2001 and 2000, and the related statement of revenues, expenditures, and changes in fund balance for the years then ended. These financial statements are the responsibility of the management of the Universal Service Fund. Our responsibility is to express an opinion on these financial statements based on our audits.


We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 2, the financial statements of the Universal Service Fund are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the State of Wisconsin that is attributable to the transactions of the Fund. The statements are not intended to present fairly the financial position of the State of Wisconsin and the results of its operations and changes in financial position.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Universal Service Fund as of June 30, 2001 and 2000, and the results of its operations and changes in fund balance for the years then ended in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 12, 2002, on our consideration of the Universal Service Fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, and contracts. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

August 12, 2002

LEGISLATIVE AUDIT BUREAU
by 
Diann Allsen
Audit Director

**Universal Service Fund
Balance Sheet
June 30, 2001 and 2000**

	<u>June 30, 2001</u>	<u>June 30, 2000</u>
Assets		
Cash and Cash Equivalents (Note 2C)	\$ 7,402,768	\$ 5,304,475
Assessments Receivable	1,434,970	887,151
Educational Telecommunications Access Program Receivable	26,257	264,658
Other Receivables	11,100	5,840
Prepaid Items	9,000	0
Total Assets	<u>\$ 8,884,095</u>	<u>\$ 6,462,124</u>
Liabilities and Fund Balance		
Liabilities		
Program liabilities:		
University of Wisconsin BadgerNet Access	\$ 875,188	\$ 773,000
Educational Telecommunications Access Program	754,798	1,149,944
Lifeline Program	221,470	117,982
Medical Telecommunications Equipment Program	154,335	0
Link-up America Program	130,839	88,997
Telecommunications Equipment Purchase Program	93,871	66,404
Institutional Discount Program	72,603	71,920
Rate Ceiling Credit Program	18,116	209,228
Access Program or Project by Nonprofit Groups	7,691	0
Public Interest Pay Telephone Program	5,624	0
Accounts payable	92,803	14,672
Total Liabilities	<u>2,427,338</u>	<u>2,492,147</u>
Fund Balance		
Reserved for encumbrances (Note 6)	2,374,803	709,000
Reserved for prepaids	9,000	0
Unreserved	4,072,954	3,260,977
Total Fund Balance	<u>6,456,757</u>	<u>3,969,977</u>
Total Liabilities and Fund Balance	<u>\$ 8,884,095</u>	<u>\$ 6,462,124</u>

The accompanying notes are an integral part of this statement.

Universal Service Fund
Statement of Revenues, Expenditures, and Changes in Fund Balance
for the Years Ended June 30, 2001 and 2000

Revenues	<u>Year Ended June 30, 2001</u>	<u>Year Ended June 30, 2000</u>
Telecommunications Providers Assessments (Note 2D) for:		
Educational Telecommunications Access Program	\$ 10,325,484	\$ 12,263,961
Public Service Commission programs	6,790,216	0
BadgerLink program	1,612,054	934,444
University of Wisconsin BadgerNet Access	<u>867,559</u>	<u>863,875</u>
Total Telecommunications Providers Assessments	19,595,313	14,062,280
Investment Income	407,630	212,380
Other Revenue	<u>183,278</u>	<u>45,327</u>
Total Revenues	<u>20,186,221</u>	<u>14,319,987</u>
Expenditures		
Program Expenditures:		
Educational Telecommunications Access Program	10,480,498	8,750,186
BadgerLink program	1,692,767	835,150
Telecommunications Equipment Purchase Program	1,616,067	643,453
University of Wisconsin BadgerNet Access	955,000	773,000
Lifeline Program	942,714	321,645
Rate Ceiling Credit Program	607,683	1,247,650
Link-up America Program	585,482	210,951
Medical Telecommunications Equipment Program	357,359	0
Access Program or Project by Nonprofit Groups	88,422	0
Public Interest Pay Telephone Program	32,212	0
Institutional Discount Program	<u>(3,178)</u>	<u>64,743</u>
Total Program Expenditures	17,355,026	12,846,778
Administrative Expenditures	233,308	142,276
Other Expenditures	<u>65,607</u>	<u>42,739</u>
Total Expenditures	<u>17,653,941</u>	<u>13,031,793</u>
Excess of Revenues over Expenditures	2,532,280	1,288,194
Other Financing Uses		
Operating Transfer to the State of Wisconsin General Fund (Note 4)	<u>45,500</u>	<u>43,500</u>
Excess of Revenues over Expenditures and Other Financing Uses	2,486,780	1,244,694
Fund Balance		
Fund Balance, Beginning of Year	<u>3,969,977</u>	<u>2,725,283</u>
Fund Balance, End of Year	<u>\$ 6,456,757</u>	<u>\$ 3,969,977</u>

The accompanying notes are an integral part of this statement.

1. Description of the Universal Service Fund

The Wisconsin Public Service Commission (PSC) established the State of Wisconsin Universal Service Fund, as directed by 1993 Wisconsin Act 496, to ensure that all residents of Wisconsin receive essential telecommunications services and have access to advanced telecommunications service capabilities. Act 496 directed the PSC to create and appoint the members of the Universal Service Fund Council, the majority of whom are to be representatives of consumers of telecommunications services, to advise the PSC concerning the administration of the Fund. Act 496 also directed the PSC to contract with a private firm to administer the Fund. The PSC has contracted with Williams Young, LLC, a public accounting firm, for these services.

As allowed by statute, the PSC requires telecommunications providers to contribute to the Universal Service Fund in amounts sufficient to support the Fund's programs and operations. The Fund supports funding for telecommunications services and access that are provided through several state agencies, including the PSC, the Technology for Educational Achievement (TEACH) Board, the University of Wisconsin (UW) System, and the Department of Public Instruction (DPI).

Presented below is a description of each of the programs under which the Universal Service Fund incurred expenditures during fiscal years (FYs) 2000-01 and 1999-2000:

- A. Educational Telecommunications Access Program - This program, which is administered by the TEACH Board, was implemented in February 1998 to provide educational entities with subsidized access to new data lines for direct Internet access and video links, which also provide for two-way interactive video that allows participants to view and respond to instructional presentations from off-site locations. In addition, the program provides grants for data lines and video links in existence prior to or on October 14, 1997.
- B. BadgerLink - Beginning in FY 1999-2000, the Universal Service Fund pays for contracts with vendors that provide statewide access to reference databases of magazines and newspapers through BadgerLink, which is a program administered by DPI to provide access to information resources using existing telecommunications networks and Internet connections.

- C. Telecommunications Equipment Purchase Program - This program, which was implemented in May 1996, assists persons with disabilities in acquiring special telecommunications equipment. Six categories of disabilities qualify for the program: hard of hearing, deaf, speech impaired, mobility/motion impaired, deaf and low vision, and deaf and blind. For each disability, the PSC has established a maximum dollar amount that the Universal Service Fund will pay toward the purchase of special telecommunications equipment. Participants in this program are required to contribute \$100 toward the cost of the special equipment, plus any amount in excess of the maximum amount that the Fund will pay, although beginning in May 2000, hard of hearing participants are not required to contribute \$100. The Fund issues vouchers to approved eligible disabled persons, who present them to vendors when equipment is purchased. Vendors subsequently submit the vouchers to the Fund administrator for payment.
- D. University of Wisconsin BadgerNet Access - BadgerNet is the State's telecommunications infrastructure of voice, data, and video networks and communication services provided by the Department of Administration to Wisconsin state agencies, local governments, UW campuses, technical colleges, public and private schools, and other eligible users. Beginning in FY 1997-98, the Legislature appropriated funds from the Universal Service Fund to provide BadgerNet access for UW-River Falls, UW-Stout, UW-Superior, and UW-Whitewater in a manner equivalent to the access provided through other funding sources for the other nine four-year campuses.
- E. Lifeline and Link-up America Programs - These are separate but similar programs that were implemented in June 1997, with retroactive assistance to May 1996. Certain low-income individuals are eligible to participate in these programs. The Lifeline Program is based on a maximum rate of \$15 per month for certain basic services consisting of single-party residential touch-tone service, including "911" emergency service. When the actual approved rate for these services exceeds \$15 per month, low-income customers may receive support for the difference. Until May 1, 2000, the Universal Service Fund paid for 25 percent of this difference; beginning May 1, 2000, the Fund pays 100 percent of the difference that is in excess of the amount that is eligible for reimbursement from federal Lifeline Program funds. The Link-up America Program provides a waiver of certain regulated service charges when low-income residential customers initiate or move telephone service. For both of these programs, telecommunications providers establish eligibility and request reimbursement from the Fund for its share of these costs.
- F. Rate Ceiling Credit Program - This program was implemented in May 1996 to lessen the financial effects of rapid increases in approved telecommunications rates charged to users. Under the program, telecommunications providers issue credits to residential customers when the telecommunications rates approved by the PSC exceed certain levels

that are based on the median household income level for which the rates apply. Monthly, the Universal Service Fund reimburses telecommunications providers the value of the credits issued.

- G. Medical Telecommunications Equipment Program - This program, which was implemented in FY 2000-01, provides grants to nonprofit medical clinics and public health agencies to purchase medical telecommunications equipment that will promote technologically advanced medical services or will enhance access to medical care.
- H. Access Program or Project by Nonprofit Groups - This program, which was implemented in FY 2000-01, provides grants to nonprofit groups for partial funding of programs or projects that will facilitate affordable access to telecommunications and information services.
- I. Public Interest Pay Telephone Program - This program, which was implemented in FY 2000-01, provides funding to ensure that pay telephones remain or are installed at locations where there is a public need, even though revenues generated by use of the telephones are not sufficient to have providers willing to maintain or install these telephones.
- J. Institutional Discount Program - This program, which was implemented in May 1996, is designed to enable qualified institutions, such as public libraries, nonprofit schools, and nonprofit hospitals, to receive discounted rates for new specialized telecommunications services, including direct Internet access, high-speed data transfer capability, two-way interactive video, and toll call access to the Internet. The institutions are reimbursed 30 percent of their annual service costs their first year in the program, 20 percent in the second year, and 10 percent in the third year, with a cumulative limit of \$7,200. 1999 Wisconsin Act 9 authorized the phasing out and eventual elimination of this program in FY 2001-02 as the result of the similarity and use of the Educational Telecommunications Access Program.
- K. Newsline Electronic Information Service - Beginning with FY 1997-98, an annual transfer from the Universal Service Fund is made to the State of Wisconsin General Fund to fund a contract between DPI and the National Federation of the Blind to provide the *Newsline* electronic information service that provides dial-up access to audio versions of major national newspapers for sight-impaired individuals.

2. Summary of Significant Accounting Policies

- A. Basis of Presentation - The Universal Service Fund's financial statements have been prepared in conformity with generally accepted accounting principles for governments as prescribed by the Governmental Accounting Standards Board (GASB). The Universal Service Fund is a special revenue

fund of the State of Wisconsin. These statements present the financial position and results of operations of only the activity of the Fund, and are not intended to present the financial activity for the State of Wisconsin as a whole.

- B. Basis of Accounting - The Universal Service Fund is accounted for using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are included on the balance sheet. The operating statement presents revenues and expenditures that result in changes in net available financial resources.

The Fund is accounted for on the modified accrual basis of accounting, which recognizes revenues when they become measurable and available to pay current reporting period liabilities. Expenditures and related liabilities are recognized when obligations are incurred, with the exception that payments on master lease obligations are recorded as expenditures when due.

- C. Cash and Cash Equivalents - Cash and cash equivalents reported on the balance sheet include a demand deposit account at a commercial financial institution and cash deposited with the State Treasurer, where available balances beyond immediate needs are pooled in the State Investment Fund for short-term investment purposes. Balances pooled are restricted to legally stipulated investments valued consistent with GASB Statement No. 31, *Accounting and Financial Reporting for Investments and for External Investment Pools*.
- D. Telecommunications Providers' Assessments - Annually, the PSC estimates the amount of revenues needed to pay for the year's program and administrative costs. The PSC then assesses telecommunications providers their share of these costs based on intrastate revenues. Those telecommunications providers with intrastate gross telecommunications revenues of less than \$200,000 annually are exempt from this assessment. Generally, telecommunications providers pay one-twelfth of the assessed amount each month or one-fourth of the assessment each quarter, depending on the amount of the assessment. The Universal Service Fund recognizes telecommunications providers' assessments when due. Unpaid assessments as of June 30 are reported on the balance sheet as assessments receivable.

Effective January 1998, the PSC temporarily suspended assessments against telecommunications providers for the Universal Service Fund programs operated by the PSC, in order to reduce an accumulated balance in the Fund. Consequently, there were no assessments for PSC-operated programs during FYs 1999-2000 and 1998-99, although telecommunications providers were assessed for the estimated cost of other Universal Service Fund programs. The PSC reinstated assessments for PSC-related programs effective August 2000.

3. Deposits

The Universal Service Fund's administrator uses a bank account at a commercial financial institution to process payments under the telecommunications programs established by the PSC. Payments from this bank account are funded by periodic transfers from the State's bank account. For the Fund's bank account, the financial statements include cash in the bank, plus cash in transit to or from the bank. As of June 30, 2001, the amount of the bank account balance was \$70,200. As of June 30, 2000, the amount of the bank account balance was \$83,980. The Federal Deposit Insurance Corporation insures the Fund's deposits for losses up to \$100,000. Therefore, all of the Fund's cash deposits in the bank account as of June 30, 2001, and June 30, 2000, were insured and are categorized as risk category 1 in accordance with GASB Statement No. 3.

Cash deposited with the State of Wisconsin Treasurer is invested in the State Investment Fund (SIF), which is a short-term pool of state and local funds managed by the State of Wisconsin Investment Board with oversight by its Board of Trustees. The carrying amount of shares in the SIF, which is presented at fair value, was \$7,388,000 as of June 30, 2001, and \$5,249,000 as of June 30, 2000. Holdings of the SIF include certificates of deposit and investments consisting primarily of direct obligations of the federal government and the State, and unsecured notes of qualifying financial and industrial issuers. Shares in the SIF are not required to be categorized under GASB Statement No. 3. The SIF is not registered with the Securities and Exchange Commission.

4. Operating Transfer to the General Fund

An annual operating transfer from the Universal Service Fund is made to the State of Wisconsin General Fund appropriation created under s. 20.255(1)(ke), Wis. Stats., to fund a contract between DPI and the National Federation of the Blind for the *Newsline* electronic information service that provides dial-up access to audio versions of major national newspapers for blind and visually impaired individuals.

5. Master Lease Commitments

The TEACH Board has financed subsidized video link costs and data line costs using the State's master lease program. The Universal Service Fund's expenditures for the program include master lease payments of \$5.9 million during FY 2000-01 and \$3.9 million during FY 1999-2000, which included \$1.2 million and \$0.8 million for interest, respectively. The outstanding balance on the master lease for the Educational Telecommunications Access Program as of June 30, 2001, was \$23.0 million. The following presents the future lease payments as of June 30, 2001:

<u>Fiscal Year</u> <u>Ended June 30</u>	<u>Total</u>
2002	\$ 4,670,694
2003	6,373,582
2004	6,245,616
2005	6,245,116
2006	<u>3,089,254</u>
Total future payments	26,624,262
Less: Interest	<u>(3,657,419)</u>
Present value of minimum lease payments	\$22,966,843

6. Encumbrance Reserves

The Universal Service Fund is committed to make future payments related to the Telecommunications Equipment Purchase Program, the Educational Telecommunications Access Program, and various other programs.

- A. Educational Telecommunications Access Program - As of June 30, 2001, a purchase order was outstanding for the design and construction of three gateways in which \$1,144,000 was encumbered and expected to be paid during FY 2001-02.
- B. Telecommunications Equipment Purchase Program - Valid vouchers that have been issued to disabled persons for the purchase of special telecommunications equipment but have yet to be presented to the Fund for payment are reported as reserved for encumbrances. As of June 30, 2001, and June 30, 2000, the amounts reserved for Telecommunications Equipment Purchase Program encumbrances were \$728,200 and \$571,100, respectively.
- C. Other Encumbrances - As of June 30, 2001, the following encumbrance balances were outstanding for the various programs in which awards had been made to participants, but the appropriate invoices and supporting documentation have not yet been presented to the Fund for the release of funding to the recipient:

<u>Program</u>	<u>Encumbrances at</u> <u>June 30, 2001</u>
Access Program or Project by Nonprofit Groups	\$270,386
Medical Telecommunications Program	139,272
Public Interest Telephone Program	88,788
Other	4,157

As of June 30, 2000, the following encumbrance balances were outstanding:

<u>Program</u>	<u>Encumbrances at June 30, 2000</u>
Educational Telecommunications	
Access Program	\$46,900
UW BadgerNet	91,000

7. Subsequent Events

2001 Wisconsin Act 16 limits the amount of assessments on telecommunications providers to support the PSC-operated programs. The PSC may not assess more than \$5.0 million in FY 2003-04, and \$6.0 million in FY 2004-05 and each year thereafter for PSC-operated programs.

Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

We have audited the financial statements of the State of Wisconsin Universal Service Fund as of and for the years ended June 30, 2001 and 2000, and have issued our report thereon dated August 12, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the State of Wisconsin Universal Service Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control over Financial Reporting

In planning and performing our audits, we considered the State of Wisconsin Universal Service Fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements, and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This independent auditor's report is intended for the information of the agencies responsible for management of the Universal Service Fund and the various programs it funds, and the Wisconsin Legislature. This independent auditor's report, upon submission to the Joint Legislative Audit Committee, is a matter of public record and its distribution is not limited. However, because we do not express an opinion on compliance or provide assurance on internal control over financial reporting, this report is not intended to be used by anyone other than these specified parties.

LEGISLATIVE AUDIT BUREAU

August 12, 2002

by 
Diann Allsen
Audit Director

Appendix

Program Descriptions, Expenditures, and Budgets

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures through 6/30/01</u>	<u>FY 2001-02 Budget</u>
PSC Programs:				
Rate Ceiling Credit	Provides credits for a portion of local service rates when the rate charged for service exceeds levels set in administrative rule for this program.	1996	\$6,778,464	\$ 896,500
Telecommunications Equipment Purchase	Provides financial assistance to help persons with disabilities in acquiring special telecommunications equipment.	1996	3,509,499	1,800,000
Lifeline	Provides support to low-income individuals for rates in excess of \$15 per month for basic telephone services.	1997	2,199,492	1,750,000
Link-up America	Provides a waiver of certain regulated service charges when low-income residential customers establish or move their telephone service.	1997	1,378,527	705,000
Institutional Discount	Provides qualified institutions, such as public libraries, nonprofit schools, and nonprofit hospitals, with discounted rates for new specialized telecommunications services.	1996	733,897	0
Rate-Shock Mitigation	Provides rate credits for customers to temporarily mitigate the effect of large increases in authorized rates. The PSC specifies the individual rate cases where the credits apply.	1996	711,188	0

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures through 6/30/01</u>	<u>FY 2001-02 Budget</u>
Voice Mail for the Homeless	Compensates any voice mail provider that provides voice mail services to a social services agency, a job service agency, or other homeless shelter authority to be used for the benefit of the entity's homeless clients or residents. (The Governor deleted funding for the program as part of his veto provisions of the 2001-03 budget bill.)	1996	\$ 0	\$ 0
Provider of Last Resort	Provides compensation to an intraLATA toll service provider in the case where no provider is willing to be the provider of last resort and provide intraLATA toll service within a telephone exchange.	1996	0	0
Advanced Telecommunications Services	The PSC may undertake an investigation of the deployment of advanced telecommunications service to Wisconsin customers. Subsequently, the PSC may require the deployment of the services and determine whether the provider requires assistance from the Fund.	1996	0	0
Access Program or Project by Nonprofit Groups	Provides funding for nonprofit groups that will facilitate the provision of affordable access to telecommunications and information services that are consistent with the uses of the Fund.	2000	88,422	500,000
Medical Telecommunications Equipment	Awards grants on a competitive basis to nonprofit medical clinics and public health agencies for the purchase of telecommunications equipment.	2000	357,359	500,000

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures through 6/30/01</u>	<u>FY 2001-02 Budget</u>
Outreach for Low-Income	Provides grants to fund collaborative efforts between community-based organizations and telecommunications providers to increase awareness of and participation in the Fund's low-income support programs.	2000	\$ 0	\$ 250,000
Public Interest Pay Telephone	Provides payments from the Fund to pay phone operators where it is determined that public health, safety, and welfare is jeopardized without the availability of public pay phone services.	2000	32,212	155,000
Two-Line Voice Carryover	Waives any intrastate nonrecurring charge or monthly rate for a second telephone line used by hearing-impaired customers for teletype service.	2000	0	5,000
Eligible Telecommunications Carrier	Allows for reimbursement of a telecommunications provider in a service area where no other eligible telecommunications carrier is designated.	2000	0	0
Subtotal of PSC Programs			<u>15,789,060</u>	<u>6,561,500</u>
TEACH Program:				
Educational Telecommunications Access	Provides subsidized access to new data lines for direct Internet access and two-way interactive video links, and provides grants for data lines and video link contracts in existence before or on October 14, 1997.	1998	31,462,827	13,595,400

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures through 6/30/01</u>	<u>FY 2001-02 Budget</u>
DPI Programs:				
Newsline	Funds a contract with the National Federation of the Blind to provide <i>Newsline</i> electronic information service that provides dial-up access to audio versions of major national newspapers for sight-impaired individuals.	1997	\$ 235,000	\$ 68,500
BadgerLink	Funds a contract with vendors that provide statewide access to reference databases of magazines and newspapers through BadgerLink, which previously had been supported with federal funding.	1999	2,527,917	1,773,500
UW System Program:				
UW System BadgerNet Access	Provides support to provide BadgerNet access for four UW campuses.	1997	3,600,000	1,054,800
TOTAL OF ALL PROGRAMS			<u>\$53,614,804</u>	<u>\$23,053,700</u>