

AN AUDIT

Universal Service Fund

Public Service Commission

00-15

December 2000

1999-2000 Joint Legislative Audit Committee Members

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December 13, 2000

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

Dear Senator George and Representative Kelso:

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, 2000 and 1999.

The Universal Service Fund is funded through assessments of telecommunications providers, which totaled \$14.1 million in fiscal year 1999-2000. The largest program funded by the Universal Service Fund is the Educational Telecommunications Access Program, which is administered by the Technology for Educational Achievement (TEACH) Board. During fiscal year 1999-2000, \$8.8 million, which is 67 percent of total fund expenditures, was expended on subsidies and grants for data lines and video links for schools, libraries, and others under this program.

As noted in our prior audits, expenditures for the Universal Service Fund programs operated by the PSC continued to be significantly less than budgeted levels. However, the Legislature and the PSC recently added a number of new programs to be funded from the Universal Service Fund, which are likely to affect its funding needs in the future.

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,

Janice Mueller
State Auditor

JM/DA/ao

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 (FYs) 1999-2000 and 1998-99.

The Universal Service Fund is funded by assessments paid by telecommunications providers, which totaled \$14.1 million in FY 1999-2000 and \$14.2 million in FY 1998-99, 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 \$13.0 million in FY 1999-2000 and \$15.7 million in FY 1998-99. Since the Fund's establishment in 1996 through June 30, 2000, a total of \$38.9 million in assessments has been assessed and \$36.2 million has been spent on the Fund's programs. The fund balance as of June 30, 2000 was \$4.0 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 1999-2000, 67 percent of the Fund's total expenditures, or \$8.8 million, supported the Educational Telecommunications Access 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.

Most of the other programs supported by the Fund were established and are operated by the PSC. The Universal Service Fund programs operated by the PSC help people with disabilities acquire special telecommunications equipment, lessen the financial effect of rate increases on users, and serve low-income individuals. However since 1996, when the PSC began to establish and operate these programs, their expenditures have been significantly less than the \$8.0 million that was budgeted for them annually. Most recently, expenditures for PSC-operated programs and administrative expenditures totaled only \$2.7 million in FY 1999-2000.

1999 Wisconsin Act 9 made a number of programmatic changes to the PSC-operated Universal Service Fund programs, including modifications to existing programs and authorizations for new activities. In addition, the PSC added new programs to those already supported by the Universal Service Fund and expanded the provisions of existing programs as part of administrative rule changes that became effective in May 2000. As a result of these recent actions by the Legislature and the PSC, the future

funding needs of PSC-operated programs supported by the Universal Service Fund will likely change. The PSC has budgeted \$6.9 million to support the existing and new Universal Service Fund programs it is operating during FY 2000-01.

In contrast to the PSC-operated programs that have not met spending expectations, the Educational Telecommunications Access Program, which is administered by the TEACH Board, has required additional expenditure authority. The Governor requested an increase of \$10,528,700 from the Universal Service Fund for the TEACH program in the 1999-01 biennial budget.

The expenditure levels of both PSC-operated Universal Service Fund programs and TEACH's Educational Telecommunications Access Program are closely monitored by the Joint Committee on Finance. For FY 2000-01, the Legislature placed \$8.0 million for the PSC-operated programs in reserve in the Joint Committee on Finance's supplemental appropriation and required a detailed expenditure plan from the PSC before release of the funds. In the case of the Educational Telecommunications Access Program, the Legislature placed one-half of the recommended \$10,528,700 increase for the 1999-01 biennium in the supplemental appropriation. However, the Joint Committee on Finance did not approve the TEACH Board's request for release of \$1,997,300 of those funds in May 2000. Another request for release of funds held in the Committee's reserve is currently pending.

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 \$14.1 million in fiscal year (FY) 1999-2000 and \$14.2 million in FY 1998-99. While telecommunications providers may 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 has been 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 these 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 assessed the fair presentation of the Fund's financial statements for FYs 1999-2000 and 1998-99.

Programs Funded

Most of the 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 expanded uses of the Fund to support programs operated by other state agencies. Descriptions, expenditures, and budget information for each of the specific programs supported by the Universal Service Fund are provided in Appendix I.

Initially, the Universal Service Fund supported telecommunications service and access programs that the PSC established, as directed under 1993 Wisconsin Act 496. The PSC programs that were supported by the Fund during FYs 1999-2000 and 1998-99 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 Institutional Discount Program, which enables qualified public libraries, nonprofit schools, and nonprofit hospitals to receive discounted rates for new specialized telecommunications services and has been discontinued, except for payments on commitments already made in the program; and
- the Lifeline and Link-up America programs, which provide support for low-income individuals to establish and receive basic telephone services.

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 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, the Universal Service Fund:

- provides funding for four University of Wisconsin campuses to receive voice, data, and video services through BadgerNet, the State's voice, data, and video telecommunications infrastructure;
- beginning in FY 1999-2000, pays 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
- funds 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 sight-impaired individuals.

Public Service Commission–Operated 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.

Expenditures for PSC-operated programs were significantly less than the \$8.0 million budgeted for them in FY 1999-2000.

In May 1996, the PSC first promulgated rules that formally established the programs it operates. Since these programs were established, expenditures for them have been significantly less than the \$8.0 million budgeted annually. For example, in FY 1999-2000, expenditures for PSC-operated programs and administrative expenditures totaled only \$2.7 million. In response to the lower expenditure levels, 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.

Recent actions by the Legislature and the PSC are likely to affect future funding needs for these programs. For example, 1999 Wisconsin Act 9 modified existing programs and authorized a new medical telecommunications equipment purchase program that will provide grants to nonprofit medical clinics and health agencies. In addition, the PSC added its own programs and expanded existing programs as part of administrative rule changes that became effective in May 2000. For example, the PSC established a program to help nonprofit groups fund access programs or projects, as well as an outreach program to increase awareness and participation in the Universal Service Fund's low-income support programs.

The Joint Committee on Finance has required the PSC to submit a detailed expenditure plan for its programs.

To address concerns with the differences between budgeted and actual expenditures for PSC-operated Universal Service Fund programs, the Legislature also enacted budgetary changes as part of Act 9. For the second year of the 1999-2001 biennial budget, \$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 as part of its future biennial budget requests, the PSC submit a budget for each Universal Service Fund program, including budgeted expenditure levels for each program by fiscal year.

The PSC submitted a \$6.9 million expenditure plan for FY 2000-01 that listed proposed expenditure levels for each of its existing and new Universal Service Fund programs. As part of the budget, the PSC

included \$650,000 for promotion and outreach, in an effort to increase awareness and use of the programs. In July 2000, the Joint Committee on Finance approved the release of the \$6.9 million for FY 2000-01. As of October 31, 2000, the PSC has expended an estimated \$0.8 million for FY 2000-01.

Educational Telecommunications Access Program

\$8.8 million was spent for the Educational Telecommunications Access Program in FY 1999-2000.

In FY 1999-2000, a total of \$8.8 million was spent on the TEACH-administered Educational Telecommunications Access Program, which is the largest program currently funded by the Universal Service Fund. The Educational Telecommunications Access 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 the 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 TEACH Board has financed its video link costs through the State's master lease program; its outstanding master lease obligation as of June 30, 2000, was \$20.3 million, which will be paid in semi-annual payments through 2005.

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. The grants for existing data line and video link contracts are limited to the amount of the subsidy an entity would receive under the new data line or video link component of the Educational Telecommunications Access Program, but existing contract grants may not be greater than the contract costs in effect on 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 is scheduled to sunset on June 30, 2002.

Subsidies and grants have been provided for 788 data lines and video links.

As of June 30, 2000, TEACH has provided subsidies for 145 new video links and 515 new data lines under the Educational Telecommunications Access Program. In addition, TEACH provided grants for 117 video links and 11 data lines that were in existence as of October 14, 1997.

The Educational Telecommunications Access Program has received continued legislative attention since its creation because of requests for increased funds. As part of the 1999-2001 biennial budget process, the Governor recommended that funding from the Universal Service Fund for the program be increased by \$10,528,700 for the biennium. In order to have more information on the actual costs of the program before providing the full amount of additional expenditure authority, the Legislature transferred one-half of the proposed annual funding increase to the Joint Committee on Finance's supplemental appropriation.

In May 2000, the Joint Committee on Finance did not approve the TEACH Board's request to release \$1,997,300 from the Committee's appropriation for FY 1999-2000. The requested amount was intended to cover projected cost increases in the Educational Telecommunications Access Program for the remainder of FY 1999-2000. A large part of the requested amount, \$1.8 million, was for the installation of gateways for two distance education networks.

Gateways are used to allow video networks with different technology to connect. Concerns of the Committee were that gateways previously had not been funded by the Educational Telecommunications Access Program and cost estimates for the gateways had increased approximately 680 percent over a period of seven months. The TEACH Board made another request in November 2000 for release of reserved funds to help fund the gateways. This request is currently pending.

The federal E-Rate discount program also provides discounts on telecommunications services.

Another area of interest to the Committee in considering the TEACH Board's request was whether federal funds that TEACH receives for telecommunications access services would be available to fund a portion of the Educational Telecommunications Access Program's costs. A federal universal service fund also has a program to assist in providing eligible schools and libraries affordable access to telecommunications services through discounts of 20 to 90 percent on telecommunications services, Internet access, and internal connections. Like the State's program, this federal program, which is popularly known as the "E-Rate" discount program, funds the discounts through assessments on the telecommunications industry. E-Rate discounts are based on the number of students eligible for the National Free Lunch Program. Schools and libraries in low-income urban communities and rural areas qualify for the highest discounts.

TEACH staff are taking steps to ensure the E-Rate discounts are being considered in the context of the services provided through the State's Educational Telecommunications Access Program. However, because of confusion regarding eligibility, only 110 of the schools and libraries that were participating in the State's Educational Telecommunications Access Program applied for and received the E-Rate discounts during FY 1998-99, which was the first year the discounts were available. Most of these schools and libraries were receiving state funds

under the existing contract grants component of the Educational Telecommunications Access Program. To adjust for the payments that these schools and libraries had received for FY 1998-99, TEACH staff recalculated the grants and subsidized payments based on the E-Rate discounts and collected \$345,000 back from the entities. These excess payments were deposited into the Universal Service Fund and recorded as a reduction of FY 1998-99 program costs. For FY 1999-2000, TEACH staff took the approved E-Rate discounts into account when initially determining grants for existing contracts by reducing payments and, therefore, did not need to collect these funds from the entities with existing contracts.

TEACH received \$2.8 million in E-rate funds under the Educational Telecommunications Access Program during FY 1999-2000.

As the purchaser of telecommunications services under the Educational Telecommunications Access Program, the TEACH Board applied for \$3.9 million and received \$2.8 million of E-Rate discounts for FY 1999-2000 as a statewide consortium on behalf of the eligible educational agencies for which it was providing new data lines and video links. TEACH deposited the \$2.8 million into its federal appropriation. In addition, during FY 1999-2000 TEACH received and deposited into its federal appropriation another \$55,000 of E-Rate funds for collections that related to FY 1998-99.

During 1999-2001 biennial budget deliberations, the Legislature approved provisions specifying that E-Rate funds be used to offset Universal Service Fund spending for the Educational Telecommunications Access Program, and therefore reduce the amount of assessments needed to fund the program. Although the Governor vetoed the provisions, in his veto message he directed the TEACH Board to offset state spending on telecommunications access subsidies to the extent possible.

Of the \$2.8 million in E-Rate funds received for entities participating in the Educational Telecommunications Access Program, \$3,000 has been spent to assist in the initial development costs for a Web site developed by the Department of Public Instruction to collect and display free and reduced-price school lunch statistics for the E-Rate program. Currently, the TEACH Board is also considering using the funds to help fund gateways; to prepay master lease payments for video links financed by the Educational Telecommunications Access Program; and for new initiatives, such as a portal Web site that would provide Wisconsin teachers access to educational technology-based best practices and resources.

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, 2000 and 1999, 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 audit.

We conducted our audit in accordance with generally accepted auditing standards 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 audit provides 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, 2000 and 1999, and the results of its operations and changes in fund balance for the years then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2000 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.

LEGISLATIVE AUDIT BUREAU

December 4, 2000

by

Diann Allsen
Audit Director

Universal Service Fund
Balance Sheet
June 30, 2000 and 1999

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
Assets		
Cash and Cash Equivalents (Note 2C)	\$ 5,304,475	\$ 3,737,555
Assessments Receivable	887,151	337,451
Educational Telecommunications Access Program Receivable	264,658	383,569
Other Receivables	<u>5,840</u>	<u>4,600</u>
Total Assets	<u>\$ 6,462,124</u>	<u>\$ 4,463,175</u>
Liabilities and Fund Balance		
Liabilities		
Program liabilities:		
Educational Telecommunications Access Program	\$ 1,149,944	\$ 293,199
University of Wisconsin BadgerNet access	773,000	864,000
Rate Ceiling Credit Program	209,228	179,438
Lifeline Program	117,982	135,165
Link-up America Program	88,997	99,819
Institutional Discount Program	71,920	95,018
Telecommunications Equipment Purchase Program	66,404	41,988
Accounts payable	<u>14,672</u>	<u>29,265</u>
Total Liabilities	<u>2,492,147</u>	<u>1,737,892</u>
Fund Balance		
Reserved for encumbrances (Note 6)	709,000	297,800
Unreserved	<u>3,260,977</u>	<u>2,427,483</u>
Total Fund Balance	<u>3,969,977</u>	<u>2,725,283</u>
Total Liabilities and Fund Balance	<u>\$ 6,462,124</u>	<u>\$ 4,463,175</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, 2000 and 1999

	<u>Year Ended June 30, 2000</u>	<u>Year Ended June 30, 1999</u>
Revenues		
Telecommunications Providers Assessments (Note 2D) for:		
Educational Telecommunications Access Program	\$ 12,263,961	\$ 12,283,333
University of Wisconsin BadgerNet access	863,875	1,867,240
BadgerLink Program	934,444	0
Total Telecommunications Providers Assessments	14,062,280	14,150,573
Investment Income	212,380	224,585
Other Revenue	45,327	24,452
Total Revenues	<u>14,319,987</u>	<u>14,399,610</u>
Expenditures		
Program Expenditures (Note 2E):		
Educational Telecommunications Access Program	8,750,186	12,232,143
Rate Ceiling Credit Program	1,247,650	1,246,492
BadgerLink Program	835,150	0
University of Wisconsin BadgerNet access	773,000	864,000
Telecommunications Equipment Purchase Program	643,453	490,399
Lifeline Program	321,645	299,651
Link-up America Program	210,951	207,280
Institutional Discount Program	64,743	194,755
Total Program Expenditures	12,846,778	15,534,720
Administrative Expenditures	142,276	118,980
Other Expenditures	42,739	40,919
Total Expenditures	<u>13,031,793</u>	<u>15,694,619</u>
Excess of Revenues Over Expenditures	1,288,194	(1,295,009)
Other Financing Uses		
Operating Transfer to the State of Wisconsin General Fund (Note 4)	43,500	35,000
Excess of Revenues Over Expenditures and Other Financing Uses	1,244,694	(1,330,009)
Fund Balance		
Fund Balance, Beginning of Year	2,725,283	4,055,292
Fund Balance, End of Year	<u>\$ 3,969,977</u>	<u>\$ 2,725,283</u>

The accompanying notes are an integral part of this statement.

NOTES TO THE FINANCIAL STATEMENTS

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 should 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 statutes, 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) 1999-2000 and 1998-99:

- 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. 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.

- C. BadgerLink Program - 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.
- D. 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. 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 for payment.
- F. 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.

- G. 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.
- H. 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-related 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.

- E. Program Expenditures - The recognition of program expenditures depends on the nature of the program:

Educational Telecommunications Access Program - Expenditures are recognized in the same fiscal year in which the expenditures are charged in accordance with the State's budgetary accounting policies. Master lease payments are recorded as expenditures in the fiscal year in which the obligations are due.

Rate Ceiling Credit Program - Expenditures are paid monthly, based on invoices submitted by approved telecommunications providers. A liability is established and expenditures are recognized for any unpaid invoices as of June 30.

BadgerLink and BadgerNet - As annual appropriations, expenditures are recognized in the same fiscal year in which the expenditures are charged in accordance with the State's budgetary accounting policies.

Telecommunications Equipment Purchase Program - Expenditures are recognized when vendors submit vouchers to the Universal Service Fund for payment. Vouchers that have been issued to disabled persons but not yet presented to vendors are reported as encumbrances, which are a reservation of fund balance.

Lifeline Program and Link-up America Program - Expenditures are recorded when invoices are received from telecommunications providers. A liability is established and expenditures are recognized for an estimate of credits that have been issued by the telecommunications providers but not yet paid as of June 30.

Institutional Discount Program - Expenditures are recorded monthly, based on approved applications. The approved institutions generally submit invoices annually in May, and the Universal Service Fund pays the institutions in June based on the submitted invoices. The financial statements reflect a liability for the expenditures accrued for the month of June, as well as an estimate for those approved institutions that have not submitted their annual invoices as of June 30.

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 the cash in the bank, plus cash in transit to or from the bank. As of June 30, 2000, the carrying amount of the bank account was \$767, while the bank balance was \$83,980. As of June 30, 1999, the carrying amount of the bank account was \$8,278, while the bank balance was \$32,421. 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, 2000 and June 30, 1999 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 approximates fair value, was \$5,249,000 as of June 30, 2000, and \$3,722,000 as of June 30, 1999. 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 sight-impaired individuals.

5. Master Lease Commitments

The TEACH Board has financed subsidized video link costs totaling \$30.7 million and data line costs totaling \$0.2 million through the State's master lease program. The Universal Service Fund's expenditures for the program include master lease payments of \$3.9 million during FY 1999-2000 and \$7.7 million during FY 1998-99, which included \$0.8 million for interest and \$0.2 million for issuance costs. The outstanding balance on the master lease for the Educational Telecommunications Access Program as of June 30, 2000, was \$20.3 million. The following presents the future lease payments as of June 30, 2000:

<u>Fiscal Year</u> <u>Ended June 30</u>	<u>Total</u>
2001	\$ 4,402,532
2002	4,405,080
2003	4,401,182
2004	4,401,301
2005	4,402,922
Thereafter	<u>2,200,412</u>
Total future payments	24,213,429
Less: Interest	<u>(3,920,000)</u>
Present value of minimum lease payments	\$20,293,429

6. Future Program Commitments

The Universal Service Fund is committed to make future payments related to the Telecommunications Equipment Purchase Program and the Institutional Discount Program.

- A. 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, 2000 and 1999, the amounts reserved for Telecommunications Equipment Purchase Program encumbrances were \$571,100 and \$297,800, respectively.
- B. Institutional Discount Program - Under this program, the Fund will pay eligible institutions a portion of the cost of certain monthly telecommunications service fees. Institutions will be reimbursed for 30 percent of the fees for the first year, 20 percent of the fees for the second year, and 10 percent of the fees for the third year, with a maximum total reimbursement of \$7,200 for each institution. In addition to the amounts reported as expenditures for the Fund's share of these costs through June 30, 2000, the Fund is committed to pay an additional \$19,121 in June 2001, \$3,465 in June 2002, and \$15 in June 2003 related to the Institutional Discount Program.
- C. Other Commitments - As of June 30, 2000, amounts reserved for the Educational Telecommunications Access Program and UW BadgerNet access were \$46,900 and \$91,000, respectively.

7. **E-Rate Discounts**

A federal universal service fund also has a program, the E-Rate discount program, to assist in providing affordable access to telecommunications services for eligible schools and libraries through discounts ranging from 20 to 90 percent on telecommunications services, Internet access, and internal connections. Similar to the State's program, funding for the discounts comes from assessments of the telecommunications industry.

A total of 110 entities participating in the Educational Telecommunications Access Program received E-Rate discounts during FY 1998-99. Most of these received existing contract grants. For these entities, TEACH staff recalculated the grants based on the E-Rate discounts and collected \$345,000 back from the entities, which was deposited into the Universal Service Fund and recorded as a reduction of program expenditures. For FY 1999-2000, TEACH staff took the approved E-Rate discounts into account when initially determining grants for existing contracts by reducing payments and, therefore, did not need to collect these funds from the entities with existing contracts.

As the purchaser of the telecommunications services under the Educational Telecommunications Access Program, the TEACH Board applied for \$3.9 million, and for FY 1999-2000 received \$2.8 million, of E-Rate discounts as a statewide consortium on behalf of the eligible entities for which it was providing new data lines and video links. These funds were not deposited into the Universal Service Fund, but rather were deposited into TEACH's federal

appropriation in the General Fund. In addition, during FY 1999-2000 TEACH received and recorded in its federal appropriation another \$55,000 of E-rate funds for collections that related to FY 1998-99.

8. Subsequent Events

Recent actions by the Legislature and the PSC are likely to affect future funding needs for Universal Service Fund programs operated by the PSC. 1999 Wisconsin Act 9 made programmatic changes to the PSC programs, including modifications to existing programs and authorizations for new activities. In addition, the PSC modified and created new programs as part of administrative rule changes that became effective in May 2000, which added new programs and expanded existing programs. Among the new programs expected to be implemented in FY 2000-01 are Outreach for Low-Income Programs, Nonprofit Groups Access Programs or Projects, Medical Telecommunications Equipment, and Public Interest Payphones.

9. Lawsuit

The TEACH Board is currently in the process of resolving a lawsuit brought against it by the Freedom From Religion Foundation regarding the eligibility of private schools and colleges with a religious affiliation to participate in the State's existing contract grants component of the Educational Telecommunications Access Program. The TEACH Board appealed the court decision that found the eligibility of private schools with a religious affiliation for the existing contract grant program to be unconstitutional. A decision from the Seventh Circuit Court is expected to be made in summer 2001. The plaintiffs sought only declaratory and injunctive relief and nonmonetary damages. The TEACH Board currently is not providing grants to private schools but is continuing to include private schools in its cost projections until a decision on the appeal is made.

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, 2000 and 1999, and have issued our report thereon dated December 4, 2000. We conducted our audit in accordance with generally accepted auditing standards 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 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's Joint Legislative Audit Committee. This restriction is not intended to limit the distribution of this report, which, upon submission to the Joint Legislative Audit Committee, is a matter of public record. 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 those specified parties.

LEGISLATIVE AUDIT BUREAU

December 4, 2000

by

Diann Allsen
Audit Director

APPENDIX

Universal Service Fund Programs

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures Through 6/30/00</u>	<u>FY 2000-01 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	\$6,170,781	\$1,400,000
Telecommunications Equipment Purchase	Provides financial assistance to help persons with disabilities in acquiring special telecommunications equipment.	1996	1,893,432	1,550,000
Lifeline	Provides support to low-income individuals for rates in excess of \$15 per month for basic telephone services.	1997	1,256,778	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	793,045	450,000
Institutional Discount	Provides qualified institutions, such as public libraries, nonprofit schools, and nonprofit hospitals, with discounted rates for new specialized telecommunications services.	1996	737,075	75,000
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 6/30/00</u>	<u>FY 2000-01 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.	1996	\$ 0	\$ 20,000
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
Nonprofit Groups—Access Programs or Projects	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	0	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	0	500,000
Outreach for Low-Income Programs	Provides grants to fund collaborative efforts between community-based organizations and telecommunications providers to increase awareness and participation in the Fund's low-income support programs.	2000	0	250,000

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures Through 6/30/00</u>	<u>FY 2000-01 Budget</u>
Public Interest Pay Phones	Provides payments from the Fund to pay phone operators where it is determined that the public health, safety, and welfare is jeopardized without the availability of public pay phone services.	2000	\$ 0	\$ 100,000
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	10,000
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			11,562,299	6,605,000
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	20,982,329	10,268,600

<u>Program Name</u>	<u>Description</u>	<u>Year Initiated</u>	<u>Expenditures Through 6/30/00</u>	<u>FY 2000-01 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	\$ 189,500	\$ 45,500
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	835,150	1,700,000
UW System Program:				
UW System BadgerNet access	Provides support to provide BadgerNet access for four UW campuses.	1997	2,645,000	864,000
Total of All Programs			\$36,214,278	\$19,483,100