

## UW System's Role in WiscNet and Grant-Funded Networks

December 2012

# Report Highlights ■

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***WiscNet is funded primarily by fees charged to its members.***

***Inadequate documentation prevented us from determining whether all payments made between WiscNet and UW System institutions were sufficient and appropriate.***

***Most UW System institutions and other WiscNet members use BadgerNet to obtain connections to WiscNet's network.***

***2011 Wisconsin Act 32 made statutory changes affecting the involvement of UW System in WiscNet and grant-funded networks.***

WiscNet is a private, membership-based nonprofit association of public and private organizations that provides internet service and other services to its members for research and educational purposes. As of June 2012, WiscNet membership totaled 483 organizations, including University of Wisconsin (UW) System institutions, state technical colleges, public library systems, counties, municipalities, private colleges, hospitals, and three-fourths of Wisconsin's public school districts. In addition, UW System has been involved in obtaining \$35.0 million in federal grant funds to support the construction of broadband networks, which include the infrastructure needed to transport large amounts of data.

Some have questioned whether UW System's involvement in WiscNet and the grant-funded networks resulted in financial subsidies or other benefits that provided WiscNet with a competitive advantage over commercial providers. 2011 Wisconsin Act 32, the 2011-13 Biennial Budget Act, directed the Legislative Audit Bureau to evaluate UW System's use of broadband services and its relationship with WiscNet. In completing our work, we reviewed:

- the creation, governance, and operations of WiscNet;
- the services WiscNet provides to its members;
- price comparisons between WiscNet and commercial providers;
- UW System's acquisition and use of network infrastructure, including its role in obtaining federal funding for construction of new grant-funded networks; and
- the future role of UW System in WiscNet and grant-funded networks.

## Key Facts and Findings

*In June 2012, 64.6 percent of WiscNet's 483 members were public school districts.*

*WiscNet paid the salary and fringe benefit costs of its staff, who are all employees of UW System institutions.*

*We question \$2.3 million in payments made by UW System Administration to WiscNet as compensation for future services.*

*Management practices and inadequate documentation prevented us from determining whether WiscNet has adequately reimbursed UW System institutions for certain goods and services.*

*In FY 2011-12, WiscNet fees were substantially lower than published commercial prices for high-bandwidth service.*

*Starting in 2003, UW System entered into lease agreements with public and private entities to develop its own network.*

*UW System institutions are collaborating with other entities to establish grant-funded community area networks.*

## WiscNet Operations

WiscNet is funded primarily by fees charged to its members. These fees accounted for \$7.5 million, or 93.6 percent, of WiscNet's total FY 2010-11 revenue. Primary and secondary schools provided 47.6 percent of WiscNet's fee revenue.

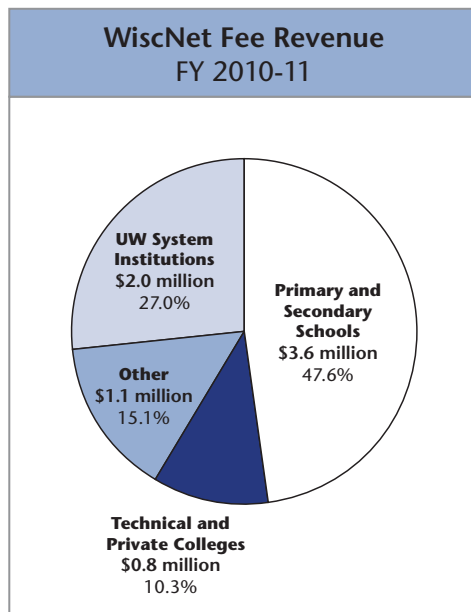
In FY 2010-11, WiscNet paid UW System institutions \$1.4 million for goods and services, including network engineering and monitoring services and network infrastructure needed for WiscNet to provide internet service to its members. UW-Madison served as WiscNet's fiscal agent, which involved processing financial transactions, as well as providing accounting, billing, purchasing, and human resources services. Although WiscNet paid the salary and fringe benefit costs of its employees, all WiscNet staff are employed by UW System institutions.

UW System Administration makes payments to WiscNet to cover a portion of the fees WiscNet charges to UW System institutions. In June of three consecutive fiscal years, UW System Administration made a total of \$2.3 million in additional payments to WiscNet in excess of the cost of services UW System institutions received, which officials indicate were prepayments for WiscNet services to be provided in future years. We question these excess payments because they are noncompliant with statutes that generally prohibit state agencies, including UW System, from using funds allocated through annual appropriations to pay for services to be provided in future years.

## Price Comparisons

WiscNet offers internet service at prices that are generally lower than commercial providers. Based on estimates provided to us by 32 WiscNet members, they would have paid commercial providers an average of \$1,161 per month in FY 2011-12 to obtain bandwidth comparable to that which they received through WiscNet. This is more than twice the \$497 per month these members paid, on average, in internet service and membership fees through WiscNet.

We identified several factors that likely contribute to WiscNet's ability to charge lower fees. For example, WiscNet does not incur all of the operating costs that many commercial providers do, including fees paid to transmit data across other



networks and advertising expenses. As a nonprofit entity, WiscNet also does not need to generate a profit and is exempt from paying income taxes.

In addition, the lack of sufficient written agreements between UW-Madison and WiscNet for the provision of goods and services and imprecise estimates of the actual costs of those goods and services lead us to question the adequacy of reimbursements.

For example, a 1999 agreement did not specify the amount UW-Madison would charge WiscNet for network engineering services, and the costs UW-Madison incurred in providing additional network engineering services to WiscNet under a 2007 agreement, which continues to guide the provision of these services, consistently exceeded the amount specified under the agreement. UW-Madison officials stated that they have not attempted to renegotiate the price of engineering services under the 2007 agreement because they believe that the amount WiscNet paid for the use of UW System's network infrastructure was sufficient to offset UW-Madison's unreimbursed costs.

## **Providing Connections to the Internet**

In order to obtain internet service, WiscNet's members must obtain their own connections to its network. Most UW System institutions and other WiscNet members obtain these

connections through BadgerNet, a state-supported network operated by a consortium of private telecommunications companies. Although most UW System institutions have historically used BadgerNet in connecting to the internet, UW System has determined that it is less costly to lease infrastructure to develop its own network. Since FY 2010-11, the expansion of UW System's network has increased bandwidth capacity at six of its institutions while reducing annual connection expenses by an estimated \$370,000.

In 2010, UW-Madison and UW-Extension were awarded federal grants totaling \$35.0 million to support the construction of network infrastructure in the Chippewa Valley, Platteville, Superior, Wausau, and the Madison area. These projects are intended to create community area networks to provide internet connections for UW System institutions, public school districts, local governments, and health care organizations.

Prices anticipated to be charged for internet connections from these networks are lower than the prices charged by BadgerNet or other providers. This is possible, in part, because significant network costs, such as equipment and construction, will be paid with federal grant funds.

UW System institutions are overseeing the construction of the grant-funded networks and also plan to participate in their governance. Plans for UW System to own a portion of the network

infrastructure, and for UW System institutions to provide technical support to grant-funded networks, are viewed by officials as extensions of UW System's mission. However, those roles may be viewed by some as conflicting with a statutory prohibition on UW System providing telecommunications services.

## **UW System's Future Role**

Act 32 made statutory changes affecting the involvement of UW System in WiscNet and the grant-funded networks, some of which first take effect on July 1, 2013. To comply with Act 32, UW System institutions plan to discontinue their WiscNet memberships and make alternative arrangements to obtain internet service.

One such arrangement, which would achieve compliance with statutory prohibitions on offering, reselling, or providing telecommunications services to entities outside of UW System, is for UW System to provide internet services directly and exclusively to its own institutions. However, UW System officials do not view this as a preferred option, in part because they believe it would likely result in increased costs for UW System institutions and may adversely affect their connections with other research and education networks.

Alternatively, UW System could contract with a vendor to provide internet services to its institutions. UW System officials indicate they may consider issuing a request for

proposals to serve its institutions that also assesses the vendor's willingness to provide services to all WiscNet members at comparable prices. However, if a vendor provides services to all WiscNet members and if UW System allows a vendor to access UW System's infrastructure and network monitoring services, the resulting arrangement could be comparable to the existing relationship between UW System and WiscNet.

Because UW System's future plans for obtaining internet services and its future role in the grant-funded networks have not been finalized, we could not assess its compliance with Act 32 at the present time. Therefore, continued monitoring will be necessary.

## Recommendations

We recommend UW System Administration:

- ☑ recover by June 30, 2013, any balance remaining from the \$2.3 million in excess payments it made to WiscNet and, in compliance with state law, lapse the amount recovered to the General Fund as a refund of expenditures (p. 20);

- ☑ report to the Joint Legislative Audit Committee by July 1, 2013, on its plans for obtaining internet services, including the identification of any vendors selected to provide services and the use of UW System resources by vendors or outside entities (p. 58); and
- ☑ report to the Joint Legislative Audit Committee by October 1, 2013, on the extent to which UW System institutions provide support to the grant-funded networks, own network infrastructure, or have transferred, or plan to transfer, infrastructure ownership to any other entity (p. 61).

We also recommend that UW-Madison:

- ☑ seek reimbursement from WiscNet for unbilled fringe benefit costs related to services it provided to WiscNet (p. 32); and
- ☑ improve the procedures it uses when entering into fixed-price agreements (p. 34).

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## Additional Information

For a copy of report 12-18, which includes a response from UW System, call (608) 266-2818 or visit our website:



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