



**PENNSYLVANIA UNIVERSAL
SERVICE FUND**

Financial Statements

December 31, 2013 and 2012

With Independent Auditors' Report

Pennsylvania Universal Service Fund
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December 31, 2013 and 2012

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Independent Auditors' Report

To the Pennsylvania Public Utility Commission
and the Board of Directors,
Solix, Inc.

Report on the Financial Statements

We have audited the accompanying balance sheets of the Pennsylvania Universal Service Fund (PUSF), a special revenue fund of the Commonwealth of Pennsylvania administered by Solix, Inc. (Solix), and the related statements of revenues, expenses and changes in fund net assets and cash flows as of December 31, 2013 and 2012 and for the years then ended, and the related notes to the financial statements, which collectively comprise the PUSF's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the PUSF administered by Solix as of December 31, 2013 and 2012, and the changes in fund net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that the Management's Discussions and Analysis on page 3 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 2, 2014 on our consideration of Solix as administrator for the PUSF's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Solix' internal control over financial reporting.

A handwritten signature in black ink that reads "Withum Smith & Brown PC". The signature is written in a cursive, flowing style.

July 2, 2014

PENNSYLVANIA UNIVERSAL SERVICE FUND

MANAGEMENT'S DISCUSSION AND ANALYSIS

PERIODS ENDED DECEMBER 31, 2013 AND 2012

This section of the Pennsylvania Universal Service Fund's financial report represents our discussion and analysis of the PUSF's financial performance during the period presented. It should be read in conjunction with the PUSF's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The PUSF's unrestricted fund balance as of December 31, 2013 and 2012 were approximately \$1.7 million and \$202 thousand, respectively.
- The PUSF's unrestricted net assets increased by approximately \$1.5 million during the period January 1, 2013 through December 31, 2013 primarily due to an increase in assessment rate of 1.51% from 1.26% effective January 1, 2013.
- The PUSF's unrestricted net assets decreased by approximately \$1.7 million during the period January 1, 2012 through December 31, 2012 primarily due to a decrease in assessments.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts – management's discussion and analysis and the basic financial statements. The basic financial statements also include notes that explain key information contained in the financial statements and provide further details on select data.

As of December 31, 2013, the PUSF had net payables of \$63 thousand comprised of accounts receivables – assessments of \$10 thousand, deferred revenues of \$49 thousand, and accounts payable and accrued expenses of \$24 thousand.

As of December 31, 2012, the PUSF had net payables of \$31 thousand comprised of accounts receivables – assessments of \$47 thousand, deferred revenues of \$55 thousand, and accounts payable and accrued expenses of \$23 thousand.

The PUSF maintained an adequate cash flow and balance of funds to satisfy all obligations during 2013 and 2012.



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Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditors' Report

Solix, Inc. as administrator for the
Pennsylvania Universal Service Fund

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Pennsylvania Universal Service Fund, which comprise the balance sheet as of December 31, 2013, and the related statements of revenues, expenses and changes in fund net assets and cash flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated July 2, 2014.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Solix, Inc.'s (Solix') internal control, in its role as administrator for the Pennsylvania Universal Service Fund (PUSF), over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Solix' internal control. Accordingly, we do not express an opinion on the effectiveness of Solix' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether the PUSF's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Withum Smith & Brown PC".

Princeton, NJ
July 2, 2014

Pennsylvania Universal Service Fund
Balance Sheets
December 31, 2013 and 2012

	2013	2012
Assets		
Cash and cash equivalents	\$ 1,761,331	\$ 233,512
Accounts receivable - assessments, net	10,452	47,333
Interest receivable	<u>33</u>	<u>61</u>
	<u>\$ 1,771,816</u>	<u>\$ 280,906</u>
Liabilities and Fund Net Assets		
Deferred revenue	\$ 49,546	\$ 55,260
Administrative costs payable	<u>24,205</u>	<u>23,400</u>
	73,751	78,660
Fund net assets - unrestricted	<u>1,698,065</u>	<u>202,246</u>
	<u>\$ 1,771,816</u>	<u>\$ 280,906</u>

The Notes to Financial Statements are an integral part of these statements.

Pennsylvania Universal Service Fund
Statements of Revenues, Expenses and Changes in Fund Net Assets
For the Years Ended December 31, 2013 and 2012

	2013	2012
Operating revenue		
Assessments	\$ 35,266,042	\$ 32,065,175
Operating expenses		
Amounts paid and due to service providers	33,613,469	33,613,202
Bad debt expense	38,497	4,530
Administrative costs	119,280	136,176
	<u>33,771,246</u>	<u>33,753,908</u>
Operating income (loss)	1,494,796	(1,688,733)
Non-operating income		
Interest income	<u>1,023</u>	<u>2,816</u>
Net change in unrestricted fund net assets	1,495,819	(1,685,917)
Fund net assets - unrestricted		
Beginning of period	<u>202,246</u>	<u>1,888,163</u>
End of period	<u>\$ 1,698,065</u>	<u>\$ 202,246</u>

The Notes to Financial Statements are an integral part of these statements.

Pennsylvania Universal Service Fund
Statements of Cash Flows
Years Ended December 31, 2013 and 2012

	2013	2012
Cash flows from operating activities		
Receipts from assessments and service providers	\$ 35,258,712	\$ 32,097,421
Cash paid to service providers	(33,613,469)	(33,613,202)
Cash paid for administrative costs	<u>(118,475)</u>	<u>(136,176)</u>
Net cash provided by (used in) operating activities	1,526,768	(1,651,957)
Cash flows from investing activities		
Interest income	<u>1,051</u>	<u>2,811</u>
Change in cash and cash equivalents	1,527,819	(1,649,146)
Cash and cash equivalents		
Beginning of period	<u>233,512</u>	<u>1,882,658</u>
End of period	<u>\$ 1,761,331</u>	<u>\$ 233,512</u>
Reconciliation of net cash provided by (used in) operating activities		
Operating income (loss)	\$ 1,494,796	\$ (1,688,733)
Changes in assets and liabilities		
Decrease in accounts receivable - assessments	36,881	44,002
Decrease in deferred revenue	(5,714)	(7,226)
Increase in administrative costs payable	<u>805</u>	<u>--</u>
Net cash provided by (used in) operating activities	<u>\$ 1,526,768</u>	<u>\$ (1,651,957)</u>

The Notes to Financial Statements are an integral part of these statements.

Pennsylvania Universal Service Fund

Notes to Financial Statements

December 31, 2013 and 2012

1. General

On September 30, 1999, the Pennsylvania Public Utility Commission (PPUC) issued an Order at Docket Nos. P-00991648 and P-00991649 (Global Order), as amended by the Order entered November 5, 1999, and as amended by the Proposed Order in Rulemaking Re: Establishing Universal Service Fund Regulations at 52 Pa.Code §§63.141-63.151, Docket No. L-00000148, (1/27/00), to create the Pennsylvania Universal Service Fund (PUSF). In addition, on March 22, 2001, the PPUC adopted a revised final rulemaking order establishing a universal service funding mechanism, implementing revenue-neutral rate reform and resolving interconnection issues in the telecommunications industry. The PUSF was established to both reduce and restructure access charges and further the opportunity for development of local competition. The PUSF is a means to reduce access and toll rates for the ultimate benefit of the end-user and to encourage greater toll competition, while enabling carriers to continue to preserve the affordability of local service rates.

The PUSF is funded by an assessment on all Pennsylvania telecommunications service providers that provide intrastate telecommunications services (excluding wireless carriers) and is paid, via a monthly remittance advice, to Solix, Inc. (Solix), whose contract to act as Administrator of the Fund was granted by the PPUC through June 30, 2016, with a possible one-year extension from July 1, 2016 through June 30, 2017, per contract dated and signed June 21, 2012. Carriers contribute a fixed monthly assessment amount based on company-specific revenues. Eligible recipients receive fixed monthly support payments from the PUSF as approved by the PPUC.

2. Summary of Significant Accounting Policies

Basis of Presentation

These statements have been prepared on the accrual basis in accordance with the Governmental Accounting Standards Board (GASB). For the years ended December 31, 2013 and 2012, the PUSF had accounting transactions in the unrestricted fund net assets only. The PUSF's financial statement presentation follows the accounting guidance related to Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments and amendments. This accounting guidance, as amended, establishes standards for financial reporting for state and local governments.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Revenue Recognition

Telecommunications companies doing business in the Commonwealth of Pennsylvania are required to pay into the PUSF a fixed monthly amount as determined in accordance with PPUC regulations. It is the PUSF's policy to record revenues in the period earned. Funds received in advance or prepayments are not recognized as revenues, but as deferred revenues.

Receivables and Credit Policies

Accounts receivable – assessments are due under normal terms requiring payment by the 15th of the month. Any accounts not paid by the 15th of the month plus a five day grace period are assessed a late payment charge of 18 percent per annum, adjusted to a daily percent. Late payment charges are recorded as assessments.

Special Revenue Fund

The PUSF is considered a special revenue fund of the State of Pennsylvania. The financial statements presented are not a reflection of the financial position or changes in financial position of the State of Pennsylvania.

Pennsylvania Universal Service Fund
Notes to Financial Statements
December 31, 2013 and 2012

3. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and highly liquid instruments with an original maturity of three months or less when purchased. As part of its cash management program, Solix maintains a portfolio of daily valued money market funds. The carrying value of such funds approximates market due to their short-term nature. Surplus funds of the PUSF are invested in two money market funds maintained by two national financial institutions. Interest is credited to the PUSF when earned and the interest rate for the years ended December 31, 2013 and 2012 averaged 0.04% and 0.12%, respectively.

4. Allowance for Doubtful Accounts

Allowance for doubtful accounts amounted to \$40,010 and \$9,459 at December 31, 2013 and 2012, respectively, to provide for anticipated uncollectible amounts from certain carriers. Uncollectible contributions of \$7,946 and \$14,127 were written off during the years ended December 31, 2013 and 2012, respectively.

5. Assessments

Identified carriers that are operating in the Commonwealth of Pennsylvania, excluding wireless service providers, provide assessments to the Fund. The PPUC notifies Solix when new carriers are certified to offer service in the Commonwealth of Pennsylvania. The carriers are assessed at a flat rate based on the intrastate revenue of two years prior. The assessment rate for the years ending December 31, 2013 and 2012 was 1.51 and 1.26 percent, respectively. The gross assessment totaled \$35,266,042 and \$32,065,175 for the years ending December 31, 2013 and 2012, respectively.

6. Amounts Paid and Due to Service Providers

Universal Service Support Payments to the qualified recipients are made by Solix as directed by the PPUC. The qualified recipients receive payments in order to neutralize the revenue deficits created by mandated decreases in toll and access charges. For the years ended December 31, 2013 and 2012 the PUSF determined that \$33,613,469 and \$33,613,202, respectively, in support payments were due to service providers.

7. Administrative Costs

As stated in the Contract, Solix is reimbursed a fixed amount each fiscal year plus any allowable variable costs, as defined. Such variable costs include customary, reasonable and necessary expenses incurred by Solix in performance of services, including payments to an independent accountant for an annual audit, extraordinary legal work provided by external counsel, taxes, application fees, licensing fees, and similar expenses.

The administrative fee for the years ended December 31, 2013 and 2012 was \$95,880 and \$112,789, respectively. For the year ended December 31, 2013, the PUSF will pay administrative fees of \$95,880 to Solix.

The administrative costs were as follows:

	2013	2012
Administrative fees	\$ 95,880	\$ 112,789
External audit fees	<u>23,400</u>	<u>23,387</u>
	<u>\$ 119,280</u>	<u>\$ 136,176</u>

Pennsylvania Universal Service Fund
Notes to Financial Statements
December 31, 2013 and 2012

8. Income Taxes

These financial statements present the activities of the PUSF. The activities of the PUSF are tax-exempt since the PUSF is a special revenue fund of the Commonwealth of Pennsylvania, and therefore not subject to federal or state income taxes or sales, use, gross receipts or other taxes. As such, no provision for such taxes has been reflected in the accompanying financial statements.

9. Concentration of Credit Risk

Solix maintains a portion of the PUSF's cash and cash equivalents at a financial institution and may at times exceed amounts insured by the Federal Deposit Insurance Corporation (FDIC). Additionally, the balance of the cash and cash equivalents of the Company was invested in money market funds. Since these are high quality financial institutions, management does not believe the Fund is exposed to any significant credit risk on its cash and cash equivalent balances.

One carrier represents approximately 40 percent and 41 percent of operating revenue assessments for the years ended December 31, 2013 and 2012, respectively. Three carriers represent 74 percent (27 percent, 27 percent and 20 percent, respectively) and one carrier represents 88 percent of the accounts receivable – assessments at December 31, 2013 and 2012, respectively.

10. Subsequent Events

Management has evaluated subsequent events occurring after the balance sheet date through the date of July 2, 2014, which is the date the financial statements were available to be issued. Based on this evaluation, Management has determined that no subsequent events have occurred which require disclosure in the financial statements.