



**PENNSYLVANIA UNIVERSAL  
SERVICE FUND**

**Financial Statements**

**December 31, 2006 and 2005**

**With Independent Auditors' Report**

**Pennsylvania Universal Service Fund  
Table of Contents  
December 31, 2006 and 2005**

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	<b>Page(s)</b>
<b>Independent Auditors' Report</b> .....	1
Management's Discussion and Analysis .....	2
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 .....	3-4
<b>Financial Statements</b>	
Balance Sheets .....	5
Statements of Revenues, Expenses and Changes in Fund Net Assets.....	6
Statements of Cash Flows.....	7
Notes to Financial Statements.....	8-10



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## Independent Auditors' Report

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

We have audited the accompanying balance sheets as of December 31, 2006 and 2005, of the Pennsylvania Universal Service Fund (PUSF), a special revenue unit 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 for the years then ended. These financial statements are the responsibility of the Fund's management. 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 of America and 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.

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, 2006 and 2005, and the changes in fund net assets and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying required supplementary information such as Management's Discussions and Analysis on page 2 is not a required part of the basic financial statements but is supplementary information required by the Government Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 28, 2007 on our consideration of Solix as administrator for the PUSF's internal control structure over financial reporting and 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 of 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* and should be read in conjunction with this report in considering the results of our audits.

*Withum Smith + Brown* P.C.

June 28, 2007

## **PENNSYLVANIA UNIVERSAL SERVICE FUND**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

#### **PERIODS ENDED DECEMBER 31, 2006 AND 2005**

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, 2006 and December 31, 2005 was \$1,593,284 and \$1,876,759, respectively.
- The PUSF's unrestricted net assets decreased by \$283,475 during the year ended December 31, 2006.
- The PUSF's unrestricted net assets decreased by \$448,624 during the year ended December 31, 2005.

#### 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, 2006, the PUSF had net receivables of \$133,619 comprised of accounts receivables – assessments of \$182,978, interest receivable of \$3,755, accounts payable – assessments of \$15,063, deferred revenue of \$14,651, and accounts payable and accrued expenses of \$23,400.

As of December 31, 2005, the PUSF had net payables of \$17,053 comprised of accounts receivables – assessments of \$49,074, accounts payable – assessments of \$733, accounts payable – assessments of \$19,772, deferred revenue of \$23,688, and accounts payable and accrued expenses of \$23,400.

The PUSF maintained an adequate cash flow and balance of funds to satisfy all obligations during 2006 and 2005.



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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**

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

We have audited the financial statements of the Pennsylvania Universal Service Fund as of December 31, 2006 and 2005, and have issued our report thereon dated June 28, 2007. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Solix, Inc.'s (Solix') internal control, in its role as administrator for the Pennsylvania Universal Service Fund (PUSF) over financial reporting as a basis for designing our auditing procedures 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 over financial reporting, in its role as administrator for the PUSF. Accordingly, we do not express an opinion on the effectiveness of the Solix' internal control over financial reporting, in its role as administrator for the PUSF.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the PUSF's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the PUSF's financial statements that is more than inconsequential will not be prevented or detected by the PUSF's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material misstatement of the financial statements will not be prevented or detected by the PUSF's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as identified above.



Compliance and Other Matters

As part of obtaining reasonable assurance whether the PUSF's financial statements are free of material misstatement, we performed tests of compliance of Solix as administrator for the PUSF 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 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*.

This report is intended solely for the information and use of the Administrator, Contract Administrator, the Pennsylvania Public Utility Commission and State Auditor's Office of the State of Pennsylvania and is not intended to be and should not be used by anyone other than these specified parties.

*Withum Smith & Brown P.C.*

June 28, 2007

**Pennsylvania Universal Service Fund**  
**Balance Sheets**  
**December 31, 2006 and 2005**

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	<b>2006</b>	<b>2005</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 1,459,665	\$ 1,893,812
Accounts receivable - assessments	182,978	49,074
Interest receivable	<u>3,755</u>	<u>733</u>
	<u>\$ 1,646,398</u>	<u>\$ 1,943,619</u>
<b>Liabilities and Fund Net Assets</b>		
Accounts payable - assessments	\$ 15,063	\$ 19,772
Deferred revenue	14,651	23,688
Accounts payable and accrued expenses	<u>23,400</u>	<u>23,400</u>
	53,114	66,860
Fund net assets - unrestricted	<u>1,593,284</u>	<u>1,876,759</u>
	<u>\$ 1,646,398</u>	<u>\$ 1,943,619</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, 2006 and 2005**

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	<b>2006</b>	<b>2005</b>
Operating revenue		
Assessments	\$ 33,350,623	\$ 33,207,064
Operating expenses		
Amounts paid and due to service providers	33,565,234	33,565,271
Bad debt expense	70,275	43,657
Administrative costs	145,384	144,540
	<u>33,780,893</u>	<u>33,753,468</u>
Operating loss	(430,270)	(546,404)
Non-operating income		
Interest income	<u>146,795</u>	<u>97,780</u>
Net decrease in unrestricted fund net assets	(283,475)	(448,624)
<b>Fund net assets - unrestricted</b>		
Beginning of period	<u>1,876,759</u>	<u>2,325,383</u>
End of period	<u>\$ 1,593,284</u>	<u>\$ 1,876,759</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, 2006 and 2005**

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	<b>2006</b>	<b>2005</b>
<b>Cash flows from Operating activities</b>		
Receipts from assessments and service providers	\$ 33,137,407	\$ 33,238,203
Cash paid to service providers	(33,569,943)	(33,676,514)
Cash paid for administrative costs	<u>(145,384)</u>	<u>(144,540)</u>
Net cash used in operating activities	(577,920)	(582,851)
<b>Cash flows from investing activities</b>		
Interest income	<u>143,773</u>	<u>97,635</u>
<b>Decrease in cash and cash equivalents</b>	(434,147)	(485,216)
<b>Cash and cash equivalents</b>		
Beginning of period	<u>1,893,812</u>	<u>2,379,028</u>
End of period	<u>\$ 1,459,665</u>	<u>\$ 1,893,812</u>
<b>Reconciliation of net cash used in operating activities</b>		
Operating loss	\$ (430,270)	\$ (546,404)
Changes in assets and liabilities		
(Increase) decrease in accounts receivable - assessments	(133,904)	65,130
Increase (decrease) in accounts payable - assessments	(4,709)	15,981
Increase (decrease) in deferred revenue	(9,037)	9,666
Decrease in accounts payable and accrued expenses	<u>--</u>	<u>(127,224)</u>
Net cash used in operating activities	<u>\$ (577,920)</u>	<u>\$ (582,851)</u>

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

# **Pennsylvania Universal Service Fund**

## **Notes to Financial Statements**

### **December 31 2006 and 2005**

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#### **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). 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), which was selected by the PPUC to act as Administrator of the Fund through December 31, 2010. 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, 2006 and 2005 the PUSF had accounting transactions in the unrestricted fund net assets only. The PUSF's financial statement presentation follows the recommendation of GASB No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments" and amendments. GASB No. 34, 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.

##### **Receivables and Credit Policies**

Accounts receivable – assessments are due under normal terms requiring payment by the 15<sup>th</sup> of the month. Any accounts not paid by the 15<sup>th</sup> 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.

##### **Reclassification**

Certain amounts contained in the 2005 financial statements have been reclassified to conform to the 2006 presentation.

**Pennsylvania Universal Service Fund**  
**Notes to Financial Statements**  
**December 31, 2006 and 2005**

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**3. Cash and Cash Equivalents**

As part of its cash management program, Solix maintains a portfolio of daily valued mutual 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 Merrill Lynch and Mellon Bank. Interest is credited to the PUSF when earned and the interest rate for the years ended December 31, 2006 and 2005 averaged 4.80% and 3.07%, respectively.

**4. Allowance for Doubtful Accounts**

Allowance for doubtful accounts amounted to \$113,931 and \$43,656 at December 31, 2006 and 2005 to provide for anticipated uncollectible amounts from certain carriers. No uncollectible contributions were written off during the years ended December 31, 2006 and 2005.

**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, 2006 and 2005 was 1.02 and .99 percent, respectively. The gross assessment totaled \$33,350,623 and \$33,207,064 for the years ending December 31, 2006 and 2005, 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, 2006 and 2005 the PUSF determined that approximately \$33,565,234 and \$33,565,271, 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 year ended December 31, 2006 and 2005 was approximately \$121,440 and \$121,440, respectively. On May 31, 2007, the PPUC awarded the administrative duties to Solix through December 31, 2010. For the year ended December 31, 2007 the PUSF will pay administrative fees of approximately \$121,440 to Solix.

The administrative costs were as follows:

	<b>2006</b>	<b>2005</b>
Administrative fees	\$ 121,440	\$ 121,440
External audit fees	<u>23,944</u>	<u>23,100</u>
	<u>\$ 145,384</u>	<u>\$ 144,540</u>

**Pennsylvania Universal Service Fund**  
**Notes to Financial Statements**  
**December 31, 2006 and 2005**

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**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 unit 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**

The Fund maintains its cash and cash equivalents balances with financial institutions, which may at times exceed amounts insured by the Federal Deposit Insurance Corporation. 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 47% and 48% of operating revenue assessments for the years ended December 31, 2006 and 2005, respectively. One carrier represents 48% and -0% of the accounts receivable – assessments at December 31, 2006 and December 31, 2005, respectively.