



**PENNSYLVANIA UNIVERSAL
SERVICE FUND**

Financial Statements

December 31, 2011 and 2010

With Independent Auditors' Report

Pennsylvania Universal Service Fund
Table of Contents
December 31, 2011 and 2010

| | Page(s) |
|---|----------------|
| Independent Auditors' Report | 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 |
| Financial Statements | |
| 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, 2011 and 2010, 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 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 the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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, 2011 and 2010, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 15, 2012, 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 considered in assessing the results of our audits.

The Management's Discussions and Analysis on page 2, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. 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.

Withum Smith + Brown, PC

June 15, 2012

PENNSYLVANIA UNIVERSAL SERVICE FUND

MANAGEMENT'S DISCUSSION AND ANALYSIS

PERIODS ENDED DECEMBER 31, 2011 AND 2010

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, 2011 and 2010 were \$1.9 million and \$1.7 million, respectively.
- The PUSF's unrestricted net assets increased by approximately \$146 thousand during the period January 1, 2011 through December 31, 2011.
- The PUSF's unrestricted net assets decreased by approximately \$81 thousand during the period January 1, 2010 through December 31, 2010.

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, 2011, the PUSF had net receivables of \$6 thousand comprised of accounts receivables – assessments of \$91 thousand, deferred revenues of \$62 thousand, and accounts payable and accrued expenses of \$23 thousand.

As of December 31, 2010, the PUSF had net receivables of \$7 thousand comprised of accounts receivables – assessments of \$49 thousand, accounts payable – assessments of \$1 thousand, deferred revenues of \$18 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 2011 and 2010.



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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 and for the years ended December 31, 2011 and 2010, and have issued our report thereon dated June 15, 2012. 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 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.

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 deficiencies, 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.

Witham Smith + Brown, PC

June 15, 2012

Pennsylvania Universal Service Fund
Balance Sheets
December 31, 2011 and 2010

| | 2011 | 2010 |
|--|---------------------|---------------------|
| Assets | | |
| Cash and cash equivalents | \$ 1,882,658 | \$ 1,735,842 |
| Accounts receivable - assessments, net | 91,335 | 48,621 |
| Interest receivable | <u>56</u> | <u>120</u> |
| | <u>\$ 1,974,049</u> | <u>\$ 1,784,583</u> |
| Liabilities and Fund Net Assets | | |
| Accounts payable - assessments | \$ -- | \$ 1,210 |
| Deferred revenue | 62,486 | 17,662 |
| Administrative costs payable | <u>23,400</u> | <u>23,400</u> |
| | 85,886 | 42,272 |
| Fund net assets - unrestricted | <u>1,888,163</u> | <u>1,742,311</u> |
| | <u>\$ 1,974,049</u> | <u>\$ 1,784,583</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, 2011 and 2010

| | 2011 | 2010 |
|--|---------------------|---------------------|
| Operating revenue | | |
| Assessments | \$ 33,929,172 | \$ 33,677,557 |
| Operating expenses | | |
| Amounts paid and due to service providers | 33,612,315 | 33,599,004 |
| Bad debt expense | 19,823 | 10,101 |
| Administrative costs | 154,128 | 154,071 |
| | <u>33,786,266</u> | <u>33,763,176</u> |
| Operating income (loss) | 142,906 | (85,619) |
| Non-operating income | | |
| Interest income | <u>2,946</u> | <u>4,857</u> |
| Net change in unrestricted fund net assets | 145,852 | (80,762) |
| Fund net assets - unrestricted | | |
| Beginning of period | <u>1,742,311</u> | <u>1,823,073</u> |
| End of period | <u>\$ 1,888,163</u> | <u>\$ 1,742,311</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, 2011 and 2010

| | 2011 | 2010 |
|--|---------------------|---------------------|
| Cash flows from operating activities | | |
| Receipts from assessments and service providers | \$ 33,911,459 | \$ 33,590,739 |
| Cash paid to service providers | (33,613,525) | (33,597,943) |
| Cash paid for administrative costs | <u>(154,128)</u> | <u>(154,071)</u> |
| Net cash provided by (used in) operating activities | 143,806 | (161,275) |
| Cash flows from investing activities | | |
| Interest income | <u>3,010</u> | <u>4,774</u> |
| Change in cash and cash equivalents | 146,816 | (156,501) |
| Cash and cash equivalents | | |
| Beginning of period | <u>1,735,842</u> | <u>1,892,343</u> |
| End of period | <u>\$ 1,882,658</u> | <u>\$ 1,735,842</u> |
| Reconciliation of net cash provided by (used in) operating activities | | |
| Operating income (loss) | \$ 142,906 | \$ (85,619) |
| Changes in assets and liabilities | | |
| Increase in accounts receivable - assessments | (42,714) | (5,631) |
| Increase (decrease) in accounts payable - assessments | (1,210) | 1,061 |
| Increase (decrease) in deferred revenue | <u>44,824</u> | <u>(71,086)</u> |
| Net cash provided by (used in) operating activities | <u>\$ 143,806</u> | <u>\$ (161,275)</u> |

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

Pennsylvania Universal Service Fund

Notes to Financial Statements

December 31, 2011 and 2010

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 extended by the PPUC through June 30, 2012, per contract amendment dated and signed February 12, 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, 2011 and 2010, 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.

3. Cash and Cash Equivalents

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, 2011 and 2010 averaged 0.10% and 0.16%, respectively.

Pennsylvania Universal Service Fund
Notes to Financial Statements
December 31, 2011 and 2010

4. Allowance for Doubtful Accounts

Allowance for doubtful accounts amounted to \$19,056 and \$4,479 at December 31, 2011 and 2010, respectively, to provide for anticipated uncollectible amounts from certain carriers. Uncollectible contributions of \$5,246 and \$11,049 were written off during the years ended December 31, 2011 and 2010, 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, 2011 and 2010 was 1.25 and 1.17 percent, respectively. The gross assessment totaled \$33,929,172 and \$33,677,557 for the years ending December 31, 2011 and 2010, 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, 2011 and 2010 the PUSF determined that \$33,612,315 and \$33,599,004, 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, 2011 and 2010 was \$130,778 and \$130,778, respectively. Solix is under contract as the administrator of the PUSF through December 31, 2011. For the year ended December 31, 2011, the PUSF will pay administrative fees of \$130,778 to Solix.

The administrative costs were as follows:

| | 2011 | 2010 |
|---------------------|-------------------|-------------------|
| Administrative fees | \$ 130,778 | \$ 130,778 |
| External audit fees | <u>23,350</u> | <u>23,293</u> |
| | <u>\$ 154,128</u> | <u>\$ 154,071</u> |

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.

Pennsylvania Universal Service Fund
Notes to Financial Statements
December 31, 2011 and 2010

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 43% and 44% of operating revenue assessments for the years ended December 31, 2011 and 2010, respectively. One carrier represents 75% and 69% of the accounts receivable – assessments at December 31, 2011 and 2010, respectively.

10. Subsequent Events

Management has evaluated subsequent events occurring after the balance sheet date through the date of June 15, 2012, 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.