Universal Service Administrative Company

Financial Statements as of and for the Years ended December 31, 2018 and 2017, Additional Supplemental Schedules as of and for the Years ended December 31, 2018 and 2017, and Report of Independent Auditors in Accordance with Government Auditing Standards

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY

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Report of Independent Auditors

To the Board of Directors of Universal Service Administrative Company:

Report on the Financial Statements

We have audited the accompanying financial statements of Universal Service Administrative Company (the "Company"), which comprise the statements of financial position as of December 31, 2018 and 2017, and the related statements of operations and change in unrestricted net assets and cash flows for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 an opinion on the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and in accordance with 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 our 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, we consider internal control relevant to the Company'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 Company'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 opinion.

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and its operations and change in unrestricted net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other matter

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The additional combining supplemental schedules of financial position applicable to the Federal USF, of changes in net assets applicable to the Federal USF, and of cash flows applicable to the Federal USF are presented for the purposes of additional analysis and are not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we also have issued a report dated June 6, 2019 on our consideration of the Company's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the year ended December 31, 2018. 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 the Company's internal control over financial reporting and compliance and other matters.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
McLean, Virginia
June 6, 2019

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31, 2018 AND 2017
(In thousands)

	2018	2017
ASSETS		
CURRENT ASSETS:		
Cash	$ 6,401	$ 8,975
Receivable from Federal USF	11,623	4,056
Prepaid expenses and other current assets	8,728	9,798
Assets held for the Federal USF (Note 3)	7,086,215	4,969,559
Total Current Assets	7,112,967	4,992,388
Fixed Assets, net, held for Federal USF (Note 4)	35,478	42,754
Other Assets	3,716	433
Assets held for the Federal USF (Note 3)	-	2,550,314
TOTAL ASSETS	$ 7,152,161	$ 7,585,889
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	$ 24,165	$ 22,429
Advance from the Federal USF	18,024	13,024
Deferred revenue	3,014	10,783
Liabilities related to assets held for the Federal USF	7,086,215	4,969,559
Total Current Liabilities	7,131,418	5,015,795
Deferred Rent	20,743	19,780
Liabilities related to assets held for the Federal USF	-	2,550,314
Commitments and contingencies (Note 7)	-	-
TOTAL LIABILITIES	$ 7,152,161	$ 7,585,889
NET ASSETS		
Unrestricted net assets	-	-
TOTAL NET ASSETS	$ -	$ -
TOTAL LIABILITIES AND NET ASSETS	$ 7,152,161	$ 7,585,889

The accompanying notes are an integral part of these financial statements.

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
STATEMENTS OF OPERATIONS AND CHANGE IN UNRESTRICTED NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2018 AND 2017
(In thousands)

	2018	2017
REVENUE	$ 204,991	$ 196,730
OPERATING EXPENSES:		
Contractual expenses	53,972	45,856
Personnel and related expenses	72,537	69,917
General and administrative expenses	62,449	67,825
Depreciation, amortization and loss on retirements	16,033	13,132
Total Operating Expenses	204,991	196,730
CHANGE IN NET ASSETS	-	-
NET ASSETS - Beginning of year	-	-
NET ASSETS - End of year	$ -	$ -

The accompanying notes are an integral part of these financial statements.

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017
(In thousands)

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from the Federal USF and other parties	$ 194,640	$ 202,824
Cash paid for operating expenses and employees	(184,738)	(178,686)
Cash received from interest	15	7
Net cash provided by operating activities	9,917	24,145
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(12,491)	(22,568)
INCREASE (DECREASE) IN CASH	(2,574)	1,577
CASH - Beginning of year	8,975	7,398
CASH - End of year	$ 6,401	$ 8,975
RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES		
Change in net assets	$ -	$ -
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	15,984	13,132
Loss on retirement of fixed assets	49	-
Amortization of deferred rent	963	6,891
Changes in operating assets and liabilities:		
(Increase) Decrease in prepaid expense and other assets	(2,213)	(1,152)
(Increase) Decrease in assets held for the Federal USF	433,658	1,161,701
(Increase) Decrease in receivable from the Federal USF	(7,567)	1,570
Increase (Decrease) in accounts payable and accrued liabilities	5,470	(827)
Increase (Decrease) in advance from the Federal USF	5,000	-
Increase (Decrease) in deferred revenue	(7,769)	4,531
Increase (Decrease) in liabilities related to assets held for the Federal USF	(433,658)	(1,161,701)
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 9,917	$ 24,145
Supplemental disclosure of non-cash information:		
Capital expenditures included in accounts payable	$ 912	$ 4,646

The accompanying notes are an integral part of these financial statements.

1. ORGANIZATION AND BASIS OF PRESENTATION

The Universal Service Administrative Company ("USAC" or the "Company") was incorporated, effective September 17, 1997, as a not-for-profit, independent, wholly-owned subsidiary of the National Exchange Carrier Association, Inc. ("NECA"), and appointed by the Federal Communications Commission ("FCC") to administer the Universal Service Fund ("USF") and the universal service support mechanisms. USAC's Board of Directors consists of directors representing a cross-section of stakeholders in the USF and the universal support mechanisms. Pursuant to 47 C.F.R. § 54.703(a), USAC's Board of Directors is separate from NECA's Board of Directors and NECA is prohibited from participating in USAC's functions.

The FCC, in its Report and Order in CC Docket Nos. 96-45 and 97-21 ("Universal Service Order") released May 8, 1997 and November 20, 1998, respectively, determined that USAC should serve as the permanent administrator of the High Cost, Lifeline, Rural Health Care, and Schools and Libraries Universal Service Support Mechanisms, collectively referred to herein as the "Programs," established pursuant to Section 254 of the Communications Act of 1934, as amended.

USAC, as the administrator of the USF, performs billing, collection, and disbursement functions. It also collects information regarding contributing entities' and end-user telecommunications revenues, and submits projections of demand, administrative expenses for the Programs, and quarterly universal service contribution data to the FCC.

The functions of USAC as the administrator of the USF also include, but are not limited to, development of applications and associated instructions as needed for the Programs, administering the application process consistent with applicable FCC rules and related operational infrastructure for such processes, performing outreach and public education functions, performing audits of contributing telecommunications carriers reporting information to USAC as required under 47 C.F.R. § 54.707(a), performing audits of telecommunications carriers receiving High Cost and/or Lifeline Program benefits, and schools, libraries, and rural health care providers and beneficiaries receiving Schools and Libraries or Rural Health Care Program benefits, and development and implementation of other functions unique to the Programs.

Funds collected by USAC from telecommunications carriers required to contribute to the USF pursuant to 47 U.S.C. § 254 and 47 C.F.R. § 54.706 are restricted as to their intended use related to the Programs described above. The cash and other financial assets USAC holds and administers for the benefit of the USF are reported at fair value in the Statements of Financial Position as assets held for the Federal USF, with an equal amount recorded as liabilities related to assets held for the Federal USF. Activities related to the USF are not presented in USAC's Statements of Operations and Change in Unrestricted Net Assets or Statements of Cash Flows.

NECA, a related party to USAC, performs data collection functions for the High Cost Program pursuant to FCC rules and bills USAC for the associated costs. NECA is compensated by USAC in accordance with NECA's Cost Accounting and Procedures Manual. For the years ended December 31, 2018 and 2017, the expense recognized for services rendered by NECA was $489,501 and $449,534, respectively. These expenses are included in contractual expenses in the accompanying Statements of Operations and Change in Unrestricted Net Assets. At December 31, 2018 and 2017, amounts due to NECA were $73,500 and $29,000, respectively.

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting, in conformity with the accounting principles generally accepted in the United States of America (GAAP). Net assets are those assets not subject to restrictions. Due to the nature of its operations, USAC has no permanently restricted or temporarily restricted net assets. The accompanying supplemental schedules are unaudited and not presented in accordance with GAAP. Such supplemental schedules are presented for purposes of additional analysis of the financial statements and are not required as a part of the basic financial statements.

Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, Leases (Topic 842), which requires lessees to recognize right-of-use assets and lease liabilities on the balance sheet. ASU 2016-02 will be effective for the company beginning on January 1, 2020. Early adoption is permitted. The company is currently evaluating the impact of adopting this standard on its financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES

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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fixed Assets – Fixed assets consist of office furniture, office equipment, computer hardware, internal use computer software and leasehold improvements. These assets are carried at cost, net of accumulated depreciation and amortization. If an asset acquired has a cost exceeding $3,500 and a useful life exceeding one year, it is capitalized. Bulk purchases made in a single transaction are capitalized when a quantity of similar items individually cost $500 or more and less than $3,500 and where the total acquisition cost is greater than $18,000. Capitalizable bulk purchase items include furniture and fixtures and exclude personal computers. Depreciation of office furniture and equipment is calculated on a straight-line basis over the seven-year estimated useful lives of those assets. Depreciation and amortization of hardware and software are calculated on a straight-line basis over the three-year estimated lives of those assets. Amortization of leasehold improvements is calculated on a straight-line basis over the shorter of the remaining period of the respective leases or estimated useful lives of the improvements. Maintenance and repairs are expensed to operations as incurred.

Projects in progress consist primarily of development costs of internal use software. USAC capitalizes costs of software developed or obtained for internal use once the preliminary project stage has been completed, management commits to funding the project and it is probable that the project will be completed and the software will be used to perform the function intended.

Receivable from the Federal USF – USAC bills the USF on the basis of net cash disbursements. Collections against the receivable are collected in full from the USF by USAC.

Advance from the Federal USF – Represents cash advanced by the USF that allows USAC to make operating disbursements without placing USAC in a negative cash position. The amount is subject to adjustment to account for expected increases or decreases in cash-flow requirements.

Deferred Rent – USAC entered into a 13 year lease for office space commencing in July 2016. The deferred rent balance relates to lease and operating expense abatements as well as tenant improvement allowances associated with the operating lease of the new office space. Rent expense is being recognized on a straight-line basis over the life of the lease. The difference between rent expense recognized and rent payments due to the abatements, as stipulated in the lease, is reflected as deferred rent within statement of financial position. In addition, the tenant improvement allowance is also being amortized over the life of the lease.

Deferred Revenue – Represents the portion of revenues billed and/or collected through the Receivable from the Federal USF process where the corresponding expense is being recognized on the accrual basis and lags behind the cash disbursement used to bill the USF and record revenue. Deferred revenue is typically generated by capital or prepaid disbursements in excess of year end accruals.

Revenue – USAC, as the administrator of the USF, recognizes revenue when services are rendered. Revenues are equal to the cost of providing administrative support to the USF and the Programs, and to other FCC fund administrators. Such costs are paid by USF and by the other FCC fund administrators to USAC. These transactions are considered exchange transactions in accordance with the AICPA's *Audit and Accounting Guide for Not-for-Profit Entities*. The other FCC fund administrators provide administrative support for the Telecommunications Relay Services ("TRS"), North American Numbering Plan ("NANP"), and Local Number Portability ("LNP") programs. USAC invoices these administrators for direct and indirect charges it incurs each month for the data collection and management functions on their behalf.

Concentration of Credit Risk – Financial instruments that potentially subject USAC, as the administrator of the USF, to concentration of credit risk consist principally of cash, cash equivalents, short-term and long-term investments, and receivables from contributors. USAC, as the administrator of the USF, places its cash, cash equivalents, and short-term and long-term investments with high quality credit institution. USAC maintains portions of cash and cash equivalents with a financial institution which are federally insured under the Federal Depository Insurance Corporation Act ("FDIC"). The total deposits at these institutions are generally in excess of federally insured amounts. Deposits in excess of federally insured amounts are fully collateralized. Collateral assets consist of financial instruments issued and fully insured or guaranteed by the United States Government. In the normal course of business, USAC also has invested portions of cash held for the benefit of the USF in U.S. Treasury securities, which are classified as Assets held for the Federal USF on the Statements of Financial Position. On May 18, 2018, at the direction of the FCC, USAC began transferring USF cash from the private banking institutions to the U.S. Treasury. The transfer of cash will continue through August 2019 as securities held by the private institutions mature.

Income taxes – Income taxes are accounted for under the asset and liability method of accounting. Deferred income taxes are provided on the liability method, whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences between the amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when it is more likely than not that some portion of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax law and rates on the date of enactment.

USAC has not taken any uncertain tax positions that require adjustment to the consolidated financial statements. With few exceptions, USAC is subject to income tax examinations by US federal, state, and local authorities for tax years 2013 and after.

3. ACTIVITIES RELATED TO THE FEDERAL USF

As discussed in Note 1, the cash and other financial assets of the USF, which USAC administers and acts as an intermediary for, are reported at fair value in the Statements of Financial Position as assets held for the Federal USF, with an equal amount recorded as liabilities related to assets held for the Federal USF. The summary of assets applicable to the USF included below provides additional detail with respect to these amounts.

	December 31			
(In thousands)		2018		2017
ASSETS:				
CURRENT ASSETS:				
Cash and cash equivalents	$	3,786,324	$	913,734
Investments		2,569,279		3,333,107
Accounts receivable		1,177,893		1,108,553
Allowance for doubful accounts		(453,588)		(396,657)
Interest receivable		6,307		10,822
Total Current Assets held for the Federal USF		7,086,215		4,969,559
Fixed assets		35,478		42,754
Investments		-		2,550,314
Total Assets Held for Federal USF	$	7,121,693	$	7,562,627

Cash and Cash Equivalents – USAC, as the administrator of the USF, considers all highly liquid securities with an original maturity of three months or less as of the financial statement date to be cash equivalents. These also may include cash balances held by the U.S. Treasury on behalf of the USF.

Short-Term Investments – USAC, as the administrator of the USF, considers all securities purchased with an original maturity of greater than three months and a current maturity of less than or equal to one year to be short-term investments. Short-term investments consist solely of United States Treasury securities with readily determinable fair values. USAC, as the administrator of the USF, accounts for its investments in accordance with investment accounting standards for not-for-profit organizations.

Long-Term Investments - USAC, as the administrator of the USF, considers all securities purchased with a current maturity of greater than one year to be long-term investments. These investments are accounted for in accordance with fair value measurement accounting standards. Long-term investments consist solely of United States Treasury debt securities with readily determinable fair values, none of which have maturities greater than three years. On May 18, 2018, at the direction fo the FCC, as the result of the transfer of cash to U.S. Treasury, USAC no longer holds any long-term investments.

Accounts Receivable and Allowance for Doubtful Accounts – USAC, as the administrator of the USF, recognizes accounts receivable arising from amounts billed to contributors and the recovery of funds from service providers and beneficiaries, which remain unpaid. Accounts receivable are recorded at invoiced amounts and generally do not bear interest. Based on the Debt Collection Improvement Act ("DCIA"), all receivables over 90-days delinquent are transferred to the United States Treasury for collection, except for receivables where the debtor has appealed the validity of the amount owed or the debtor has sought protection under Chapter 7 or 11 of the United States Bankruptcy Code. The DCIA receivable balances transferred to the Treasury remain as USF receivables. All receipts of DCIA transferred receivables are held by USAC for the benefit of the USF.

Gross receivables are reduced to net realizable value by the allowance for doubtful accounts, which reflects the Company's estimate of exposure to risk of nonpayment of billed balances, determined principally on the basis of its historical collection experience. The allowance includes reserves for amounts on appeal, identified bankruptcies, identified inactive contributors, delinquent amounts that are referred to the United States Treasury for collection, and other items. Management periodically reviews such estimates and management's assessment of recoverability may change based on actual results. Accounts receivable write-offs are periodically submitted by USAC to the FCC for approval.

4. FIXED ASSETS

Fixed Assets as of December 31, 2018 and 2017 are as follows:

	December 31	
(In thousands)	**2018**	**2017**
FIXED ASSETS:		
Office furniture and equipment	$ 3,049	$ 2,586
Computer hardware	8,725	9,484
Computer software	76,983	66,004
Leasehold improvements	8,839	8,829
Projects in progress	3,803	6,975
Total Fixed Assets	101,399	93,878
Less accumulated depreciation	(65,921)	(51,124)
	$ 35,478	$ 42,754

Depreciation and amortization expense was $15.98 million and $13.13 million for the years ended December 31, 2018 and 2017, respectively.

5. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value of assets and liabilities, the following hierarchy is used in selecting inputs, with the highest priority given to Level 1, as these are the most transparent or reliable:

Level 1 – Quoted prices for identical instruments in active markets.
Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets.
Level 3 – Valuations derived using one or more significant inputs that are not observable.

USAC utilizes the best information available in measuring fair value, and financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement.

The following table summarizes the valuation of the investments held by USAC for the USF according to the fair value measurement classifications as of December 31, 2018:

(In thousands)	**Total**	**Active Markets for Identical Assets (Level 1)**	**Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**
US Treasuries	$ 2,569,279	$ 2,569,279	$ -	$ -

The following table summarizes the valuation of the investments according to the fair value measurement classifications as of December 31, 2017:

(In thousands)	**Total**	**Active Markets for Identical Assets (Level 1)**	**Observable Inputs (Level 2)**	**Unobservable Inputs (Level 3)**
US Treasuries	$ 5,883,421	$ 5,883,421	$ -	$ -

6. INCOME TAXES

USAC is a not-for-profit corporation subject to income taxes, including those that arise from the permanent and temporary differences between financial and tax accounting, such as those related to meals and entertainment expense, compensated absences, depreciation, and certain lease incentives.

For the twelve months ended December 31, 2018, USAC recorded $1.1 million and $0.4 million for federal and state income tax expense, respectively, and corresponding revenue of $1.5 million in that USAC's income tax payments are funded from the USF. For the twelve months ended December 31, 2017, USAC recorded $3.6 million and $1.0 million for federal and state income tax expense, respectively. Income taxes are included as a component of general and administrative expenses.

As of December 31, 2018, USAC has recorded deferred tax assets of $4.5 million, which are fully offset by a valuation allowance. FASB Accounting Standards Codification Topic ASC 740, Income Taxes, requires that a valuation allowance be established for deferred tax assets if it is more likely than not that the deferred tax asset will not be realized. Management assesses the available positive and negative evidence to estimate whether sufficient future taxable income will be generated on a more likely than not basis to permit use of its existing deferred tax assets. On the basis of this evaluation, USAC has concluded that it is more likely than not its deferred tax assets will not be realized and a full valuation allowance has been established.

On December 22, 2017, the Tax Cuts and Jobs Acts (the "TCJA") was enacted into law. The TCJA contains several key tax provisions including the reduction of the corporate income tax rate from 35% to 21% effective January 1, 2018, as well as a variety of other changes, including the limitation of the tax deductibility of interest expense, acceleration of expensing of certain business assets and reductions in the amount of executive pay that can qualify as a tax deduction. ASC 740 requires the Company to recognize the effect of the tax law changes in the period of enactment. The Company re-measured certain of its U.S. deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future. The tax expense recorded in 2017 related to the re-measurement of the deferred tax balance was $1.6 million, which was offset by the related valuation allowance. Guidance issued by the Securities Exchange Commission ("SEC") and approved by the FASB for private companies provides for a measurement period of one year from the enactment date to finalize the accounting for effects of the Tax Cuts and Jobs Act.

Additionally, on December 22, 2017, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 118, or SAB 118, to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the Tax Act. Specifically, SAB 118 provides a measurement period for companies to evaluate the impacts of the Tax Act on their financial statements. We completed the accounting for the tax effects of the Tax Act during 2018 and no change to the provisional estimate from $1.6 million was recorded.

7. COMMITMENTS AND CONTINGENCIES

Fixed Contract Commitments

MAXIMUS Agreement – MAXIMUS Federal Services, Inc. provides to USAC contracted program operations services for the Schools and Libraries Program. On October 16, 2018, USAC entered into a contract with MAXIMUS for a period ending December 31, 2019 with four 1 year options. The contractual required payments for the period January 1, 2019 through December 31, 2019, under the Agreement for the Schools and Libraries Program is $6.4 million. In addition, USAC expects to pay variable fees up to $14.9 million.

Solix Agreement – Solix, Inc. provides to USAC contracted program operations BPO services for the Schools and Libraries Program. The existing agreement expired on December 31, 2017. On November 14, 2017, USAC entered into a contract extension with Solix for a period of twelve months ending December 31, 2018. Solix contractual payments were $30.8 million and $37.5 million for the years ended December 31, 2018 and 2017, respectively.

Lease Commitments – USAC leases its current office space under a thirteen year operating lease agreement expiring in 2028. The lease commenced in July 2016 and included a full abatement of rent and operating costs for the first 22 months of the lease term. The initial lease agreement provided USAC with a tenant improvement allowance in the amount of $10.2 million for leasehold improvements. An amendment to the lease was signed in December 2016 which increased the total TIA to $11.7 million.

At December 31, 2018, the future minimum rental and operating cost payments under the terms of the lease are as follows (in thousands):

2019	$	7,916
2020		7,256
2021		7,995
2022		8,570
2023		8,708
2024 and beyond		43,343
	$	83,788

Rent expenses under operating leases were $6.4 million and $6.0 million for the years ended December 31, 2018 and 2017, respectively.

Legal Disputes

USAC is involved in various legal proceedings and claims incidental to the normal conduct of its business. USAC reports matters herein where the value of a claim asserted by or against USAC exceeds $450,000 or more for an individual matter, or for matters relating to the same plaintiff or defendant that in the aggregate amount to $450,000 or more. During 2018, USAC was not involved in any legal proceedings and did not have a claim asserted by or against USAC that exceeded the above thresholds. USAC is currently not a party to any other lawsuit or proceeding that, in the opinion of management, is reasonably possible to have a material adverse effect on its financial position, results of operations, or cash flows.

8. RETIREMENT PLANS

USAC has a 401(k) Retirement Savings Plan covering all USAC employees. The plan is both contributory and noncontributory and all contributions are subject to certain limitations as prescribed by the plan document and government regulations. Employees are immediately vested in the employer contribution, which is funded on a current basis. Employer contributions charged to operations were $5.5 million and $5.4 million for the twelve months ended December 31, 2018 and 2017 respectively.

9. SUBSEQUENT EVENTS

USAC has performed an evaluation of subsequent events through June 6, 2019, which is the date the financial statements were available to be issued.

SUPPLEMENTAL SCHEDULES

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
COMBINING SUPPLEMENTAL SCHEDULES OF CHANGES IN NET ASSETS APPLICABLE TO THE FEDERAL USF (UNAUDITED)
AS OF DECEMBER 31, 2018

(In thousands)

	2018					
	Schools and Libraries	**High Cost**	**Lifeline**	**Rural Health Care**	**Shared Costs**	**Total USF**
ASSETS						
Cash and cash equivalents	1,371,142	1,658,953	113,059	643,150	21	3,786,324
Investments	2,585,147	-	-	-	-	2,585,147
Receivables	196,732	68,681	18,521	7,701	886,257	1,177,893
Allowance for doubtful accounts	(190,226)	(59,366)	(16,837)	(6,543)	(180,616)	(453,588)
Interest receivable	-	-	-	-	6,307	6,307
Assets held for the Federal USF	$ 3,962,795	$ 1,668,269	$ 114,743	$ 644,307	$ 711,968	$ 7,102,082
Receivable from USAC	5,750	8,678	3,180	416	-	18,024
Receivable from Programs	-	-	-	-	-	-
Other Assets(net)	-	-	-	-	27,949	27,949
TOTAL ASSETS	**3,968,544**	**1,676,947**	**117,923**	**644,724**	**739,918**	**7,148,055**
LIABILITIES						
Payable to service providers	(9,959)	(255,602)	(342)	(454)	0	(266,357)
Accrued liabilities	(5,008)	(205,955)	(106,119)	(2,404)	0	(319,486)
USAC Admin Payable	0			0	(11,623)	(11,623)
TOTAL Liabilities	$ (14,967)	$ (461,557)	$ (106,462)	$ (2,858)	$ (11,623)	$ (597,466)
Net Position	3,886,142	1,257,500	(30,381)	516,848	920,480	6,550,589
TOTAL LIABILITIES & NET POSITION	**3,901,109**	**1,719,057**	**76,080**	**519,706**	**932,103**	**7,148,055**

	2017					
	Schools and Libraries	**High Cost**	**Lifeline**	**Rural Health Care**	**Shared Costs**	**Total USF**
ASSETS						
Cash and cash equivalents	(1,617,410)	1,960,277	82,687	488,162	19	913,735
Investments	5,918,076	-	-	-	-	5,918,076
Receivables	165,334	41,697	17,736	7,547	876,239	1,108,553
Allowance for doubtful accounts	(161,034)	(40,102)	(14,160)	(6,544)	(174,816)	(396,656)
Interest receivable	-	-	-	-	10,821	10,821
Assets held for the Federal USF	$ 4,304,966	$ 1,961,872	$ 86,263	$ 489,165	$ 712,263	$ 7,554,529
Receivable from USAC	3,569	6,983	2,290	182	-	13,024
Receivable from Programs	-	43,852	-	-	-	43,852
Other Assets(net)	-	-	-	-	31,347	31,347
TOTAL ASSETS	**4,308,535**	**2,012,707**	**88,553**	**489,347**	**743,610**	**7,642,752**
LIABILITIES						
Payable to service providers	(1,439)	(242,046)	(209)	(121)	-	(243,815)
Accrued liabilities	(12,763)	(193,243)	(118,725)	(5,561)	-	(330,292)
USAC Admin Payable					(4,058)	(4,058)
TOTAL Liabilities	$ (14,202)	$ (435,289)	$ (118,934)	$ (5,682)	$ (4,058)	$ (578,165)
Net Position	4,294,333	1,577,418	(30,381)	483,665	739,552	7,064,587
TOTAL LIABILITIES & NET POSITION	**4,308,535**	**2,012,707**	**88,553**	**489,347**	**743,610**	**7,642,752**

Note: This schedule represents assets and liabilities of the Federal USF at December 31, 2018 and 2017 for each of the support programs.

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
COMBINING SUPPLEMENTAL SCHEDULES OF CHANGES IN NET ASSETS APPLICABLE TO THE FEDERAL USF (UNAUDITED)
AS OF DECEMBER 31, 2018
(In thousands)

	Current Calendar Year total at 12/31/18						Prior Calendar Year total at 12/31/17					
	Schools and Libraries	High Cost	LifeLine	Rural Health Care	Shared Costs	Total	Schools and Libraries	High Cost	LifeLine	Rural Health Care	Shared Costs	Total
ADDITIONS:												
Amounts billed to contributors	1,852,784	4,607,617	1,223,121	485,913	-	8,169,435	1,775,110	4,479,844	1,284,449	300,783	-	7,840,186
Non exchange revenue bad debt	(1,351)	(3,236)	(873)	(340)	-	(5,800)	(1,627)	(4,521)	(1,439)	(459)	-	(8,046)
Interest income	27,589	12,538	856	3,133	-	44,117	44,060	18,805	1,538	3,764	-	68,167
Total additions	$ 1,879,022	$ 4,616,920	$ 1,223,104	$ 488,707	$ -	$ 8,207,752	$ 1,817,543	$ 4,494,128	$ 1,284,548	$ 304,088	$ -	$ 7,900,307
DEDUCTIONS:												
Amount paid and due to service providers	2,153,030	4,873,066	1,147,145	297,009	0	8,470,250	2,587,279	4,659,108	1,275,371	254,670	0	8,776,428
Bad debt expenses	29,192	19,263	2,677	0	0	51,132	30,583	3,393	11	5,973	0	39,960
Operating expenses	104,989	44,507	40,098	10,768	0	200,363	103,864	42,199	31,454	10,846	0	188,363
Unrealized/realized gain or loss	3	2	1	0	0	6	114	78	36	14	0	242
Non-expenditure financing (FCC transfer)	0	0	0	0	0	0		0	0	0	0	0
Total deductions	$ 2,287,214	$ 4,936,838	$ 1,189,921	$ 307,778		$ 8,721,750	$ 2,721,840	$ 4,704,778	$ 1,306,872	$ 271,503	$ -	$ 9,004,993
CHANGES IN NET ASSETS	(408,192)	(319,918)		33,183	180,928	(513,998)	(904,297)	(210,650)	(22,324)	32,585	-	(1,104,686)
NET POSITION BEGINNING BALANCE	$ 4,294,333	$ 1,577,418	$ (30,381)	$ 483,665	$ 739,552	$ 7,064,587	$ 5,198,630	$ 1,788,068	$ (8,058)	$ 451,081	$ 739,552	$ 8,169,273
NET POSITION ENDING BALANCE	$ 3,886,142	$ 1,257,500	$ (30,381)	$ 516,848	$ 920,480	$ 6,550,589	$ 4,294,333	$ 1,577,418	$ (30,381)	$ 483,665	$ 739,552	$ 7,064,587

Note: This schedule reflects the changes in net assets of the Federal USF for the years ended December 31, 2018 and 2017 for each of the support programs.

UNIVERSAL SERVICE ADMINISTRATIVE COMPANY
COMBINING SUPPLEMENTAL SCHEDULES OF CASH FLOWS APPLICABLE TO THE FEDERAL USF (UNAUDITED)
AS OF DECEMBER 31, 2018

(In thousands)

	2018							2017						
	Schools and Libraries	High Cost	High Cost Broadband	Lifeline	Rural Health	Shared Costs	Total (Sum)	Schools and Libraries	High Cost	High Cost Broadband	Lifeline	Rural Health Care	Shared Costs	Total (Sum)
CASH FLOWS FROM OPERATING ACTIVITIES														
Cash received from contributors	1,884,526	4,526,270	-	1,228,024	461,275	2	8,100,096	1,714,286	4,455,528	-	1,338,779	304,200	19	7,812,812
Interest received	21,948	15,166	-	1,468	3,546	0	42,129	44,959	20,868	-	2,060	3,958	0	71,845
Cash paid to service providers	(2,152,265)	(4,802,945)	-	(1,159,618)	(299,834)	-	(8,414,662)	(2,581,852)	(4,682,283)	-	(1,290,546)	(251,901)	-	(8,806,582)
Cash paid for administrative costs	(105,082)	(39,815)	-	(39,502)	(10,000)	-	(194,398)	(107,283)	(50,046)	-	(33,439)	(11,584)	-	(202,352)
Net cash provided by (used in) operating activities	(350,872)	(301,324)	-	30,372	154,988	2	(466,835)	(929,890)	(255,933)	-	16,854	44,673	19	(1,124,277)
CASH FLOWS FROM INVESTING ACTIVITIES														
Redemption of investments	13,665,426	-	-	-	-	-	13,665,426	2,402,701	-	-	-	-	-	2,402,701
Purchase of investments	(10,326,000)	-	-	-	-	-	(10,326,000)	(2,048,600)	-	-	-	-	-	(2,048,600)
Loss on investments	(2)						(2)	(615)						(615)
Net cash provided by investing activities	3,339,424	-	-	-	-	-	3,339,424	353,486	-	-	-	-	-	353,486
INCREASE (DECREASE) IN CASH EQUIVALENTS	2,988,552	(301,324)	-	30,372	154,988	2	2,872,589	(576,404)	(255,933)	-	16,854	44,673	19	(770,791)
CASH AND CASH EQUIVALENTS														
Beg of year	(1,617,410)	1,960,277	-	82,687	488,162	19	913,735	(1,041,006)	2,216,210	-	65,833	443,489	-	1,684,526
End of year	1,371,142	1,658,953	-	113,059	643,150	21	3,786,324	(1,617,410)	1,960,277	-	82,687	488,162	19	913,735
RECONCILIATION OF CHANGES IN NET ASSETS PROVIDED BY (USED IN) CASH FROM OPERATING ACTIVITIES														
Change in net assets	(408,192)	(319,918)		33,183	180,928		(513,998)	(904,297)	(210,650)		(22,324)	32,585		(1,104,686)
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:														
(Gain)/Loss on Disposition	3	2	-	1	0	-	6	114	78	-	36	15	-	243
Amortization	(6,500)						(6,500)							
Changes in operating assets and liabilities:							-							-
Decrease (increase) in interest receivable	859	2,630	-	612	413		4,514	899	2,063	-	522	194		3,678
Decrease (increase) in accounts receivable	(3,007)	(10,181)	-	1,320	(539)	-	(12,408)	836	1,999	-	18,751	(725)	-	20,861
Decrease (increase) in receivable from programs		43,852					43,852		(43,852)					(43,852)
Decrease (increase) in accounts receivable from USAC	(2,181)	(1,695)	-	(891)	(234)	-	(5,001)							
Increase (decrease) in liabilities	765	26,268	-	(12,473)	(2,824)	-	11,736	5,427	20,677	-	(15,175)	2,769	-	13,698
Increase (decrease) in Admin Payable	1,441	4,408	-	1,026	692	-	7,567	(384)	(881)	-	(223)	(83)	-	(1,571)
Increase in Other Assets	647	1,980	-	461	311		3,398	(3,035)	(6,967)	-	(1,762)	(656)		(12,420)
Adjustment due to allocation factor	65,294	(48,670)	-	7,133	(23,758)	2	0	(29,450)	(18,400)	-	37,029	10,574	19	(228)
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(350,872)	(301,324)	-	30,372	154,988	2	(466,835)	(929,890)	(255,933)	-	16,854	44,673	19	(1,124,277)

Note: This schedule represents the cash flows of the Federal USF for the years ended December 31, 2018 and 2017 for each of the support programs.

Report of Independent Auditors 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*

To the Board of Directors of Universal Service Administrative Company:

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 Universal Service Administrative Company (the "Company"), which comprise the statement of financial position as of December 31, 2018, and the related statements of operations and change in unrestricted 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 June 6, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Company's internal control 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 the Company's internal control. Accordingly, we do not express an opinion on the effectiveness of the Company's 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 Company'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.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
McLean, Virginia
June 6, 2019