

**Martin Matson**  
Comptroller

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**Glenn Steinbrecher, CPA**  
Special Deputy Comptroller

**Toni Biscobing**  
Special Deputy Comptroller

**Office of the Comptroller**

October 22, 2013

Mr. Jim Owczarski  
City Clerk  
200 E. Wells St, Room 205  
Milwaukee, WI 53202

Re: AT&T Video Service Provider Fees

Dear Mr. Owczarski:

The attached report summarizes the results of the review of Video Service Provider Fee payments to the City from AT&T. The City contracted with the University of Wisconsin to conduct this review for both Time Warner Cable and AT&T. This review for AT&T was conducted for the fees paid to the City for calendar years 2007 through 2009.

As the attached report indicates from the professor who conducted the review, AT&T did provide a lot of the information for a lengthy amount of time resulting in this late completion of the review. The result of the review indicates that AT&T overpaid the City for this time frame of 2007 through 2009 of \$11,153.98. AT&T is requesting this refund as you will find in their accompanying letter attached.

If there are any questions related to this matter, please contact the Audit Manager, Aycha Sirvanci at 286-2347.

Sincerely,

Handwritten signature of Martin Matson in cursive.

Martin Matson  
Comptroller

Handwritten signature of Aycha Sirvanci in cursive.

Aycha Sirvanci, CPA  
Audit Manager



**Review of  
License Fees/Video Service Provider Fees  
Paid By AT&T To  
The City of Milwaukee, Wisconsin**

**Period Reviewed: January 1, 2007 – December 31, 2009**

**August 23, 2013**

**Dr. Barry Orton  
UW-Madison  
Madison, Wisconsin**



August 23, 2013

Office of the Comptroller  
City of Milwaukee  
ATT: Aycha Sirvanci  
200 E. Wells St Room 401  
Milwaukee, WI 53202

Dear Ms. Sirvanci:

Attached find my report reviewing the License Fees/Video Service Provider Fees paid the City of Milwaukee by AT&T for 2007 – 2009.

The review found overpayment of \$11,153.98. The explanation for this estimate is found in the attached report.

As you know, it took AT&T almost a year to agree to a Non-Disclosure Agreement for this review, and almost two additional years to provide full data as to the License Fees/Video Service Provider Fees it paid the City.

It was impossible to independently verify the AT&T revenues on which the License Fees/Video Service Provider Fees were based.

Sincerely,

Barry Orton  
professor of telecommunications

Division of Continuing Studies

## INTRODUCTION

Pursuant to the request of the City of Milwaukee, Dr. Barry Orton performed a review of License Fees/Video Service Provider Fees paid to the City by AT&T for the period from January 1, 2007 to December 31, 2009.

AT&T provided documentation of its revenues and payments to the City from 1Q 2007 through 4Q 2009 and the City provided documentation of its License Fees/Video Service Provider Fees receipts for the same period.

## REQUIREMENTS

The regulations under which AT&T paid License Fees/Video Service Provider Fees to the City changed with the 2007 passage of Wisconsin Act 42, which took oversight of cable television away from municipalities and vested it with the State, specifically the Department of Financial Institutions. As a consequence, as of 6/1/08 the "License Fee" specified in Section 6 ("Compensation") of the 2007 Agreement with AT&T providing a grant of authority to provide cable service in the City was replaced with "Video Service Provider Fees" and the Agreement's definition of "Gross Revenue" was replaced with the statute's narrower definition of "Gross Receipts."

The definition of "Gross Revenue" in the Agreement (Section 1.3) is very inclusive. "Gross Revenue means all revenue derived by AT&T Wisconsin from the operation of its System specifically to provide U-verse services, whether such revenue is received by AT&T Wisconsin, its affiliates, or by any other entity that is an operator of the network or services directly or indirectly. Gross revenue includes, by way of illustration and not limitation, amounts charged for basic service, optional premium, per-channel, per-program services, channel guide subscriptions, installation, disconnection, re-connection and changes-in-service; equipment rentals, leased channel fees; late fees and administrative charges of any type; and consideration received from programmers. Gross revenue also includes a pro rata portion of all revenue generated by AT&T Wisconsin's network pursuant to compensation arrangements for advertising derived from the operation of AT&T Wisconsin's network to provide U-verse TV services within the City. The allocation shall be based on the number of subscribers in the City divided by the total number of subscribers in relation to the relevant regional or national compensation arrangement. The provision of U-verse TV services to customers at no charge however, including the provision of U-verse TV services to public institutions without charge, is not derived revenue unless bundled with other services for which a charge is collected in accordance with 6.2."

The City's definition further stipulates: "Gross revenue shall not include:

1.3.1 Bad debt except to the extent that bad debts are recovered.

1.3.2. The revenue of any person including, without limitation, a supplier of programming to AT&T Wisconsin to the extent that said revenue is also included in gross revenue of AT&T Wisconsin.

1.3.3 Pass-through payments received by AT&T Wisconsin from third-party programmers to purchase services from entities other than AT&T Wisconsin, which services benefit only the third-party programmers and for which AT&T Wisconsin neither received nor provides any consideration.

1.3.4 Any taxes on services furnished by AT&T Wisconsin which are imposed directly on any subscriber or user by the state, the city or other governmental unit and which are collected by AT&T Wisconsin on behalf of said governmental unit. The License fee in Section 6 is not such a tax."

1.3.5 Refunds, rebates, credits or discounts to subscribers or City to the extent not already offset and to the extent such refund, rebate, credit or discount is attributable to U-verse TV services;

1.3.6 Any revenues received by AT&T Wisconsin or its affiliates from the provision or capabilities other than U-verse TV services, including telecommunications services, information services, and services, capabilities, and applications that may be sold as part of a package or bundle, or functionally integrated, with U-verse TV services;

1.3.7 Any revenues received by AT&T Wisconsin or its affiliates for the provision of directory or Internet advertising, including yellow pages, white pages, banner advertisement, including advertising on the U-verse TV program guide, and electronic publishing;

1.3.8 Reimbursement by programmers of marketing costs actually incurred by AT&T Wisconsin for the marketing of programming; and

1.3.9 Any revenues received by AT&T Wisconsin for maintenance charges or sales of capital assets or equipment.

The Wisconsin statute's Gross receipts definition is very similar, but with two changes in exclusions:

(66.0420 (2) (j)) 1. "Gross receipts" means all revenues received by and paid to a video service provider by subscribers residing within a municipality for video

service, or received from advertisers, including all of the following:

- a. Recurring charges for video service.
- b. Event-based charges for video service, including pay-per-view and video-on-demand charges.
- c. Rental of set top boxes and other video service equipment.
- d. Service charges related to the provision of video service, including activation, installation, repair, and maintenance charges.
- e. Administrative charges related to the provision of video service, including service order and service termination charges.
- f. Revenues received from the provision of home shopping or similar programming.
- g. All revenue, except for refunds, rebates, and discounts, derived by the video service provider for advertising over its video service network to subscribers within a municipality. If such revenue is derived under a regional or national compensation contract or arrangement between the video service provider and one or more advertisers or advertising representatives, the amount of revenue derived for a municipality shall be determined by multiplying the total revenue derived under the contract or arrangement by the percentage resulting from dividing the number of subscribers in the municipality by the total number of regional or national subscribers that potentially receive the advertising under the contract or arrangement."

The statute somewhat changes the exclusions from those on the City Agreement's list:

2. Notwithstanding subd. 1., "Gross receipts" does not include any of the following:
  - a. Discounts, refunds, and other price adjustments that reduce the amount of compensation received by a video service provider.
  - b. Uncollectible fees, except that any uncollectible fees that are written off as bad debt but subsequently collected shall be included as gross receipts in the period collected, less the expenses of collection.
  - c. Late payment charges.
  - e. Amounts billed to video service subscribers to recover taxes, fees, surcharges or assessments of general applicability or otherwise collected by a video service provider from video service subscribers for pass through to any federal, state, or local government agency, including video service provider fees and regulatory fees paid to the FCC under 47 USC 159.
  - f. Revenue from the sale of capital assets or surplus equipment not used by the purchaser to receive video service from the seller of those assets or surplus equipment.
  - g. Charges, other than those described in subd. 1., that are aggregated or bundled with amounts described in subd. 1., including but not limited to any revenues received by a video service provider or its affiliates for telecommunications services, information services, or the provision of directory or Internet advertising, including yellow pages, white pages, banner

advertisement, and electronic publishing, if a video service provider can reasonably identify such charges on books and records kept in the regular course of business or by other reasonable means.”

In summary, the statute eliminated two not insignificant categories of revenue from Milwaukee's Agreement with AT&T: late fees and franchise or License fees (the so-called "fee-on-fee"). The late fees specifically included in the Agreement's Section 1.3 were excluded in the statute's Section 66.0420 (2) (j) (2) (c) and the License fee specified as not being excluded in the Agreement's Section 1.3.4 is specifically excluded in the statute's Section 66.0420 (2) (j) (2) (e).

Because AT&T's U-Verse service only began in 1Q 2007, and these changes took effect as of 3Q 2008, the changes in Milwaukee's License Fee/Video Service Provider Fee receipts as a result of these definitional changes were not significant in relation to the whole of the payments, particularly since AT&T did not charge or waived late fees for the first year or so while introducing its U-Verse service in the Milwaukee area.

## **REVIEW PROCESS**

The primary review task was to compile and compare the primary data of quarterly License Fee/Video Service Provider Fee payments with the accrual worksheets AT&T used to calculate its License Fee/Video Service Provider Fee payments from monthly revenues and the actual payments to the City. The payments were to be based on gross revenues as defined above, with the AT&T Agreement's definition used from 1Q/2007 through 2Q/2008, and the statute's definition used from 3Q/2008 forward.

Table 1 shows the quarterly License Fees/Video Service Provider Fees paid to the City for the January 1, 2007 to December 31, 2009 period, based on the City's records and AT&T's data.

Table 1

<u>Period</u>	<u>License/ Video Service Provider Fees</u>
1Q/2007	\$178 (paid \$189 -overpaid \$11)
2Q/2007	\$3,050
3Q/2007	\$14,495
4Q/2007	\$39,039
1Q/2008	\$37,042
2Q/2008	\$60,938
3Q/2008	\$85,807
4Q/2008	\$122,870
1Q/2009	\$142,504
2Q/2009	\$174,563
3Q/2009	\$180,002
4Q/2009	\$211,134

Each quarter from 1Q 2007 to 4Q 2009 was checked against License/Video Service Provider Fees reported by AT&T and total License Fees/Video Service Provider Fee receipts reported by the City. The quarterly totals checked out for every quarter compared.

AT&T also paid a total of \$174,089 to support Public, Educational and Government (PEG) programming pursuant to Section 66.0420(7)(em) of Wisconsin Statutes. A March 25, 2008 letter to AT&T from City Clerk Ronald D. Leonhardt verified the calculation of the payment, which was made on April 15, 2008. AT&T recovered the \$174,089 from its subscribers in monthly surcharges that ran from 2Q/2008 to 4Q/2008. AT&T's payment reports to the City reflected these recoveries.

## **ANALYSIS**

Unlike Time Warner Cable, the AT&T data does not clearly reflect the impact of the state statute on revenues beginning with June 2008 when the two categories that were eliminated from the definition of gross revenues by the statute: late fees, and License/franchise fees ("fee-on-fee") were removed from the revenue streams included in the License/Video Service Provider Fee calculation. The reason there was no visible impact from these statute changes is that AT&T did not charge late fees in the early ramp-up stages of their growth, and License/Video Service Provider Fees were not split out from other revenues in its reports.



The stepwise increases in License Fees/Video Service Provider Fees over the period reviewed were generally consistent with strong subscriber growth patterns for the introduction of U-verse, a new service that was heavily marketed by AT&T.

As far as can be determined from the License/Video Service Provider Fee spreadsheets AT&T provided, all revenue source categories that should be included in the revenue totals were included. These sources include premium, pay-per-view, digital and specialized programming, advertising, installation fees, remote and converter rentals, program guides, carriage incentives, and home shopping. As explained above, as of June 2008, due to Wisconsin Act 42, late fees and License/Video Service Provider Fees were zeroed out from the revenue streams included in the License/Video Service Provider Fee calculation.

One issue that surfaced involved the PEG support surcharges that AT&T imposed in 4Q/2008 to recover the \$174,089 it paid Milwaukee on April 15, 2008. The report AT&T filed with its normal 5% License/Video Service Provider Fee payment of \$27,884.96 shows an additional payment of \$11,153.98, which was an additional 2% of that quarter's gross revenues of \$557,699. Subsequent reports show the recovery surcharge revenues were calculated as 2% of each period's gross revenues, but that amount was not added to the 5% payment to the City for any period beyond 4Q/2008. My discussions with AT&T's Lead Tax Accountant, Cathy Candelario, confirmed this error. Therefore, it is my conclusion that AT&T overpaid the City of Milwaukee by \$11,153.98.

The review found no other instances of underpayment, missing revenues or miscalculation. In total, AT&T paid \$1,071,622 in License Fees/Video Service Provider Fees to the City for the period from January 1, 2007 to December 31, 2009. My opinion is that AT&T has paid all the License Fees/Video Service Provider Fees due the City for 2007 - 2009.

The City should note that it was impossible to independently verify the AT&T revenues beyond the data provided by AT&T itself.

**CONCLUSION**

For the period January 1, 2007 to December 31, 2009, AT&T overpaid the City of Milwaukee by the amount of \$11,153.98 by including its 2% PEG support recovery surcharge revenues with its normal 5% License Fee/Video Service Provider Fee payment.



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October 21, 2013

City of Milwaukee  
Office of the Comptroller  
Attn: Aycha Sirvanci  
200 E. Wells St., Rm. 401  
Milwaukee, WI 53202

RE: License Fee/Video Service Provider Fee Audit Results

Dear Ms. Sirvanci,

The audit conducted on AT&T Wisconsin's (AT&T) Uverse activity for compliance with the City of Milwaukee ordinance and the State of Wisconsin Statute 66.0420 by Barry Orton, Professor of Telecommunications of the University of Wisconsin-Madison was completed on August 23, 2013. The results of the audit showed that AT&T over paid the City by \$11,153.98. The reason for the over payment was due to AT&T remitting the customer billed PEG Fee to the City when it should have been used as a recovery of the PEG Fees AT&T paid to the City of Milwaukee in advance as agreed to in the Milwaukee ordinance.

AT&T respectfully requests that the City reimburse AT&T for the over payment.

Regards,

A handwritten signature in cursive script that reads "Cathy A. Candelario".

Cathy A. Candelario  
Lead Tax Accountant