



SF 2355 – Iowa Communications Network Audit and Appraisal (LSB5180SV.1)
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Fiscal Note Version – As amended and passed by the Senate

Description

[Senate File 2355](#), as amended and passed by the Senate, directs the Office of the Auditor of State (AOS) or an independent third party selected by the State Auditor to conduct a comprehensive audit and accounting of the Iowa Communications Network (ICN). The audit and accounting are to include the following components:

- A complete financial audit of the ICN for the time period beginning July 1, 2015, and ending July 1, 2018. The audit is to identify the revenues and expenses of the Network, verifying that existing authorized Network users were charged and booked properly;
- A complete inventory audit of all components of the Network, including telecommunications-related and non-telecommunications-related property and equipment. [Senate File 2355](#), as amended, requires that this audit also include verification of physical connections to existing authorized users, and identify the age and condition of property and equipment purchased or leased by the Commission for the operation of the Network;
- Information identifying and quantifying the amounts billed to current authorized users for services performed by the Network;
- Information identifying all current authorized users and business units of the Network;
- Information identifying the duration, terms, and conditions of all third-party contracts and leases entered into by the Network, including but not limited to any obligations of the State that may survive a sale, lease, or transfer of any Network assets or services.

Upon completion of the audit, the Iowa Telecommunications and Technology Commission (ITTC) is required to select an independent appraisal firm to conduct an appraisal of the Network and determine the current market value of the assets identified in the audit and accounting. [Senate File 2355](#), as amended, requires that the independent appraisal firm be selected through a competitive bidding process not associated with the ICN or any of its vendors.

The audit, accounting, and appraisal of the ICN are to be completed no later than December 21, 2018. Results of the audit, accounting, and appraisal are to be made available to the general public via an Internet site maintained by the ITTC.

Background

Established in 1989, the ICN offers voice, full-motion video, video over IP, data, Wide Area Network (WAN) connections, and high-speed Internet via a network of State-owned and leased fiber optic lines. Per Iowa Code section [8D.9](#), a private or public agency other than a State agency, local school district or nonpublic school, city or county library, Judicial Branch, judicial district department of correctional services, agency of the federal government, hospital or physician clinic, or post office is authorized to be offered access to the ICN and become a “certified user.” Initially, after its establishment, the General Assembly created this class of “certified users” for the ICN, requiring that such users use the Network for all video, data, and voice requirements. Over time, the Network established a waiver process for certified users

who can acquire similar services at a lower cost. To date, no waiver has been denied, and all noncertified users are free to choose other provider options without requiring a waiver. Per administrative rules, the ICN provides telephone services to all buildings on the Capitol Complex. Currently, the ICN administers over 3,300 miles of State-owned fiber optic lines and has a point of presence in each of Iowa's 99 counties.

The General Assembly previously initiated a Request for Proposal (RFP) for the sale or lease of the ICN pursuant to 2011 Iowa Acts, [ch. 122](#), section 8, as amended by 2011 Iowa Acts, [ch. 127](#), section 55. The 2011 Act required the ITTC to implement an RFP process to determine if there was an interest in selling or leasing the ICN, as well as to establish an RFP Implementation Team (RIT) to develop and execute a project plan and ensure the completion of the RFP by June 30, 2013. Upon completion of the bidding process and scoring and reviewing of potential vendors, the ITTC was tasked with reporting to the Governor and General Assembly for a final conclusion and potential legislation by January 2014. The RFP process was completed on May 30, 2013, and the analysis documents were presented to the Governor on June 28, 2013. The ITTC recommended the rejection of two evaluated offers, stating that the sale of the ICN would pose significant public safety risks, low estimated purchase prices, and a violation of the prohibition of the use of public funds pursuant to 2011 Iowa Acts, [ch. 127](#), section 55. Governor Branstad concurred with the analysis of the ITTC and accepted the recommendation to reject the two bid proposals for the sale or lease of the ICN in August 2013.

Assumptions

In determining the potential cost for a full appraisal of the ICN and the current market value of its assets, several assumptions are made:

- There are three common approaches to completing an appraisal: cost, market, and income. An appraisal of the ICN and the current market value will primarily utilize the cost approach, which surmises that the price a buyer will be willing to pay for an asset or group of assets should equal the cost to construct and develop a similar asset or group of assets. This type of approach adjusts market prices for depreciation.
- A complete appraisal would include an analysis of all underlying assets, including outside infrastructure, optical networks, Internet protocol (IP) networks, and other data assets.
- In order to facilitate the gathering and analysis of data done by both the AOS and the independent appraisal firm, the ICN assumes it will need to hire 1.0 additional full-time equivalent (FTE) position.
- The AOS does not have the in-house expertise to conduct a complete inventory audit as well as identify and quantify the value of services provided by the ICN and its current authorized users, nor can it identify all such current users and business units. The AOS assumes that it will need to hire an outside auditing firm to assist in this process, and that costs incurred from this process are estimated to increase by 30.0% when compared to a similar audit pursuant to 2012 Iowa Acts, [ch. 1140](#), section 5.

Fiscal Impact

The fiscal impact of [Senate File 2355](#), as amended and passed by the Senate, is estimated to cost approximately \$1.4 million in FY 2019. Total fiscal impact is grouped by Department/State agency and summarized in **Table 1** below.

Table 1: Fiscal Impact Summary, [SF 2355](#) as amended as passed by the Senate

<u>Department/State Agency</u>	<u>Estimated Cost</u>
Iowa Communications Network (ICN)	
FTE Position	\$ 75,000
Independent Appraisal	50,000 - 70,000
Auditor of State (AOS)	
Inventory/Asset Value Audit	581,300
Financial Audit	650,000
Total	1,356,300
	to
	\$ <u>1,376,300</u>

Iowa Communications Network

[Senate File 2355](#), as amended and passed by the Senate, requires an independent appraisal firm to conduct an appraisal of the ICN to determine the current market value of its assets as listed in the audit and accounting requirements described earlier in this **Fiscal Note**. According to preliminary research conducted by the ICN, such an appraisal is estimated to cost between \$50,000 and \$70,000, depending on the extensiveness of the analysis of various asset types, such as outside infrastructure, IP networks, optical networks, and other data transfer and storage resources.

Additionally, the ICN intends to work closely with the independent appraisal firm and the AOS to assist in facilitating the data collection required by the audit, appraisal, and accounting measures established in the Bill. The ICN estimates it will need to hire 1.0 additional FTE position to coordinate such data collection, totaling \$75,000 for hiring and training costs in FY 2019.

Auditor of State

The AOS estimates the cost of hiring an outside audit firm to assist with the inventory audit, quantifying the value of services provided to current authorized users, and identifying such users and business associations to total approximately \$650,000. This estimate is based on the assumption that the initial audit cost of \$500,000 pursuant to 2012 Iowa Acts, [ch. 1140](#), section 5, will have increased by 30.0%.

Additionally, the AOS estimates that the required financial audit of the ICN will require over 65.0% of the Office’s annual appropriation to execute, totaling an estimated \$581,300. No additional funds are provided in the Bill. This will result in a reduction of over 7,500 hours of audit effort at nonbillable State agencies. In order to complete statutorily required audit duties and fulfill the mandate pursuant to [SF 2355](#), as amended and passed by the Senate, the AOS indicates that the Office would require an additional appropriation.

Sources

Iowa Communications Network (ICN)
Iowa Telecommunications and Technology Commission (ITTC)
Auditor of State (AOS)
Legislative Services Agency analysis

/s/ Holly M. Lyons

March 13, 2018

The fiscal note for this Bill was prepared pursuant to Joint Rule 17 and the Iowa Code. Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.
