

for free or reduced price school lunch receive a 90 percent discount on eligible services, and thus pay only 10 percent of the cost of those services, while schools and libraries where less than one percent of students are eligible to receive free or reduced price school lunch receive a 20 percent discount and must pay 80 percent of the cost.¹⁴² Schools and libraries located in rural areas also may receive an additional 5 to 10 percent discount compared to urban areas.¹⁴³ Funding for all priority one services, including telecommunications, advanced telecommunications, and Internet access, is committed first.¹⁴⁴ Beginning with schools and libraries eligible for a 90 percent discount, the remaining funds for internal connections are allocated to eligible applicants at each descending single discount percentage, e.g., 89 percent, 88 percent, and so on until the cap has been reached.¹⁴⁵

62. While the E-rate program has always been able to fund all priority one requests, the demand for internal connections has exceeded the E-rate program's \$2.25 billion cap in every year but one since the program's existence.¹⁴⁶ As a result, many requests for priority two services are denied, and over the years, the vast majority of requests for internal connections have gone unfunded.¹⁴⁷ This trend has held true throughout the duration of the program's history. In fact, since funding year 2000, with one exception, priority two funding has been available only for recipients where at least 50 percent of the students are eligible for free or reduced price school lunch.¹⁴⁸ As a consequence, the largest urban districts have received, on average, as much as \$50 to \$190 per student for internal connections, while smaller school districts across the country receive nothing.¹⁴⁹

63. In funding year 2007, for example, applicants requested more than \$2 billion for internal connections and basic maintenance of internal connections, but only \$600 million was authorized for funding.¹⁵⁰ Only schools or libraries at the 81 percent level or higher received priority two funding that

¹⁴² 47 C.F.R. § 54.505(c).

¹⁴³ 47 C.F.R. § 54.505(b)(3).

¹⁴⁴ 47 C.F.R. § 54.507(g)(1)(i).

¹⁴⁵ 47 C.F.R. § 54.507(g)(1)(iii).

¹⁴⁶ See USAC website, Automated Search of Commitments, available at <http://www.usac.org/sl/tools/commitments-search/Default.aspx> (last visited May 20, 2010) (USAC Automated Search of Commitments).

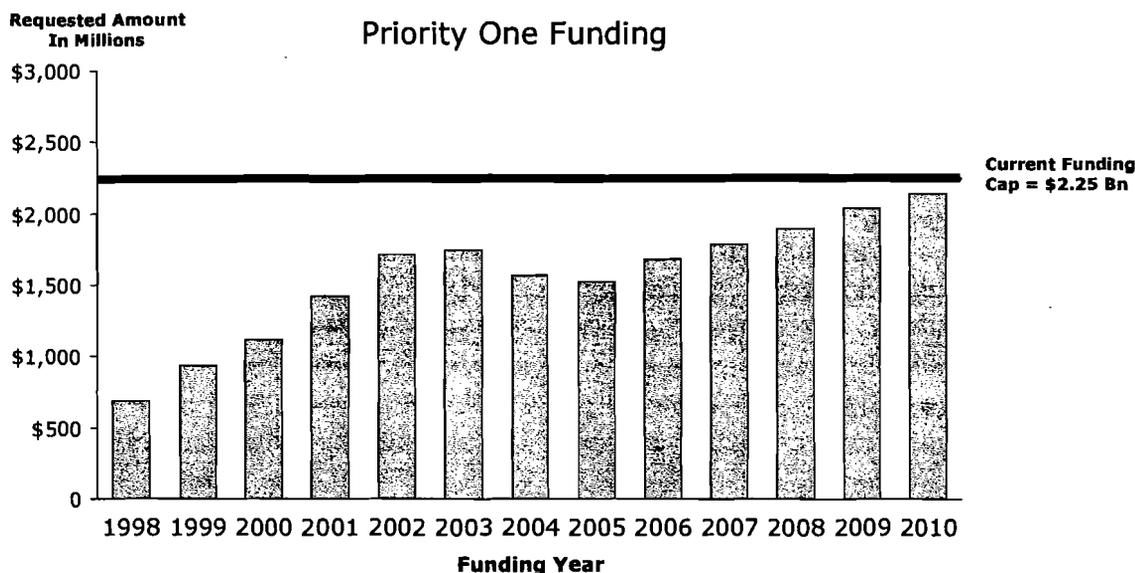
¹⁴⁷ In 2008 and 2009, for instance, schools and libraries sought more than \$4 billion in E-rate program services even though only \$2.25 billion was available. See USAC Automated Search of Commitments (demonstrating the lack of available internal connections funding for applicants in the 79 percent funding tier and below in every funding year since 2004).

¹⁴⁸ See, e.g., USAC website, Schools and Libraries, Schools and Libraries News Brief (dated Apr. 11, 2008), available at <http://www.usac.org/sl/tools/news-briefs/preview.aspx?id=155> (last visited May 20, 2010) (setting the funding year 2007 denial threshold); USAC website, Schools and Libraries, Schools and Libraries News Brief (dated July 6, 2007), available at <http://www.usac.org/sl/tools/news-briefs/preview.aspx?id=98> (last visited May 20, 2010) (setting the funding year 2006 priority two threshold). In funding year 2003, priority two funding was available at the 70 percent discount level due to a \$420 million rollover of unused E-rate funds. See *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26935, para. 57 (carrying forward funds that were projected to be unused in the first quarter of 2004 for use through June 30, 2004).

¹⁴⁹ See USAC Automated Search of Commitments.

¹⁵⁰ Funds for Learning NBP Public Notice #15 Comments at 12; see also Letter from Mel Blackwell, Schools and Libraries Division, USAC, to Thomas J. Navin, Chief, Wireline Competition Bureau (dated Mar. 8, 2007), available at <http://www.universalservice.org/res/documents/sl/pdf/FY2010%20Demand%20Estimate%20Letter.pdf> (last visited May 20, 2010) (noting that demand for priority two funding in funding year 2007 was estimated to be nearly \$2 billion).

year. In funding year 2008, there were insufficient funds to grant discounts to any priority two funding requests seeking 86 percent discounts or less.¹⁵¹ Most recently, for funding year 2010, approximately \$2 billion was requested just for priority one services.¹⁵² USAC projects that it will only be able to fund slightly more than the 90 percent applicants – meaning those applicants that have nearly 75 percent of their students eligible for free or reduced price lunch – for requested priority two services for funding year 2010 and only with significant rollover funding. The net result is that institutions that serve areas with significant poverty, with 30 or 50 percent of their population eligible to receive free or reduced-price lunch, are expected to receive no funding at all for internal connections this year.



64. The Commission has tried various strategies to expand the distribution of E-rate funding for internal connections. In 2003, the Commission adopted a rule limiting each eligible entity's receipt of discounts on internal connections to twice every five funding years.¹⁵³ The Commission also amended its rules to require that those E-rate funds identified as unused from prior years be used to increase the annual funding cap for the next E-rate funding year.¹⁵⁴ Since then, the Commission has carried forward unused E-rate funds for use in funding years 2003, 2004, 2007, 2008, and 2009.¹⁵⁵ Despite these efforts, most

¹⁵¹ See USAC website, Schools and Libraries, Schools and Libraries News Brief (Feb. 27, 2009), available at <http://www.universalservice.org/sl/tools/news-briefs/preview.aspx?id=213> (last visited May 18, 2010).

¹⁵² See Letter from Mel Blackwell, Schools and Libraries Division, USAC, to Sharon Gillett, Wireline Competition Bureau (dated Mar. 10, 2010), available at <http://www.universalservice.org/res/documents/sl/pdf/FY2010%20Demand%20Estimate%20Letter.pdf> (last visited May 20, 2010).

¹⁵³ *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26916-17, paras. 9, 11.

¹⁵⁴ *Id.* at 26935, para. 55.

¹⁵⁵ *Id.*; *Carryover of Unused Funds for Funding Year 2004*, CC Docket No. 02-6, Public Notice, 19 FCC Rcd 20420 (Wireline Comp. Bur. 2004); *Wireline Competition Bureau Announces Carryover of Unused Funds for Funding Year 2007*, CC Docket No. 02-6, Public Notice, 22 FCC Rcd 10795 (Wireline Comp. Bur. 2007); *Carryover of Unused Federal Universal Service Funds for Funding Year 2008*, CC Docket No. 02-6, Public Notice, 23 FCC Rcd (continued....)

applicants have never received E-rate funding for internal connections.¹⁵⁶ Indeed, many applicants do not even apply for priority two funding because they know from experience that the cap will be reached before many priority two requests are funded.¹⁵⁷ As shown below, in funding year 2008, most internal connections and basic maintenance funding was committed to recipients that had 75 percent or more eligible for free/reduced lunch, while applicants that had one-third or one-half of their students eligible received nothing.¹⁵⁸ In contrast, as demonstrated below, priority one funding is more evenly distributed among applicants in the various discount brackets.

Priority One Commitments Funding Year 2008

Discount Bracket	Percentage Eligible for Free/Reduced Lunch (Urban)	Percentage Eligible for Free/Reduced Lunch (Rural)	Internal Access	Internal Services	Percentage of Priority One Total
20-29%	Less than 1%	Less than 1% (starting at 25% Discount Level)	\$633,000	\$2,158,000	0.2%
30-39%	1% to 19%		\$1,101,000	\$7,072,000	0.6%
40-49%			\$26,367,000	\$106,687,000	8.3%
50-59%	20% to 34%	1% to 19%	\$30,842,000	\$141,140,000	11.0%
60-69%	35% to 49%	20% to 34%	\$52,973,000	\$221,920,000	17.3%
70-79%		35% to 49%	\$89,197,000	\$290,207,000	22.6%
80-89%	50% to 74%	50% to 74%	\$88,109,000	\$391,222,000	30.5%
90%	75% to 100%	75% to 100%	\$42,170,000	\$121,496,000	9.5%
TOTAL			\$331,391,000	\$1,281,902,000	100.0%

Priority Two Commitments Funding Year 2008

Discount Bracket	Percentage Eligible for Free/Reduced Lunch (Urban)	Percentage Eligible for Free/Reduced Lunch (Rural)	Internal Connections	Basic Maint. of Internal Connections	Percentage of Priority Two Total
20-29%	Less than 1%	Less than 1% (starting at 25% Discount Level)	\$0	\$0	0.0%
30-39%	1% to 19%		\$0	\$0	0.0%
40-49%			\$0	\$0	0.0%
50-59%	20% to 34%	1% to 19%	\$0	\$0	0.0%
60-69%	35% to 49%	20% to 34%	\$0	\$0	0.0%
70-79%		35% to 49%	\$0	\$0	0.0%
80-89%	50% to 74%	50% to 74%	\$177,954,000	\$27,234,000	21.8%

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9960 (Wireline Comp. Bur. 2008); *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Order, 24 FCC Rcd 10164 (Wireline Comp. Bur. 2009).

¹⁵⁶ See, e.g., USAC website, Schools and Libraries, Schools and Libraries News Brief (dated Dec. 4, 2009), available at <http://www.usac.org/sl/tools/news-briefs/preview.aspx?id=270> (last visited May 20, 2010) (setting funding year 2008 priority two funding requests at 87 percent); USAC website, Schools and Libraries, Schools and Libraries News Brief (dated March 12, 2010), available at <http://www.usac.org/sl/tools/news-briefs/preview.aspx?id=268> (last visited May 20, 2010) (setting funding year 2009 priority two funding approvals at 80 percent and above and denials at 54 percent).

¹⁵⁷ National Broadband Plan at 256 (NBP Recommendation 11.18) (citing to SECA NBP Public Notice #15 Comments at 29).

¹⁵⁸ While USAC has not completed funding commitments for FY 2009, it is likely that a similar situation will exist for FY 2009 as well.

90%	75% to 100%	75% to 100%	\$582,309,000	\$97,973,000	78.2%
		TOTAL	\$760,262,000	\$125,207,000	100.0%

65. The National Broadband Plan recommended that the Commission should provide E-rate support for internal connections to more schools and libraries.¹⁵⁹ The NBP noted that, while the vast majority of schools and libraries receive discounts to help pay for broadband services, they do not receive funds for the internal infrastructure necessary to utilize increased broadband capacity.¹⁶⁰ To ensure that schools and libraries have robust broadband connections and the capability to deliver that capacity to classrooms and computer rooms, the NBP recommended that the Commission develop ways that priority two funding can be made available to more E-rate applicants.¹⁶¹

66. The National Broadband Plan also recommended prospectively indexing the E-rate funding cap to the inflation rate.¹⁶² According to the NBP, the current program's purchasing power has fallen by about \$676 million in inflation-adjusted dollars since the program began.¹⁶³ The NBP noted that the E-rate program is "significantly oversubscribed, leaving most internal wiring requests unmet each year" and annual funding requests typically exceed the cap by nearly a two-to-one margin.¹⁶⁴

B. Discussion

67. Internal connections, such as routers or hubs, are essential to the effective use of broadband within schools and libraries because they enable students and library patrons to utilize higher bandwidth applications in multiple locations within a school or library. As schools and libraries are increasingly utilizing higher bandwidth services to meet educational and community needs, they need to upgrade and replace their existing internal connections as well in order to fully utilize the broadband services they are purchasing. Without upgraded Internet access and the internal connections necessary to bring the connection all the way to the classroom or library patron, many users simply will be unable to utilize the many applications available in today's marketplace, such as high-definition video streaming, that support online learning. Demand for priority one services has grown from \$800 million in 1998 to approximately \$2 billion in 2009. As noted above, only schools and libraries with the highest discount levels are receiving priority two subsidies, and the availability of priority two funding gets smaller as applicants apply for more funding for priority one services.¹⁶⁵ The net result is the E-rate program is funding high-capacity pipes to a single point of entry at the school (or library) but not providing any support for the equipment that enables the computer terminals or laptops across the school or library to access that high-capacity pipe. Further, without changes to the way in which we allocate funding for internal connections, it is quite possible that in funding year 2011, E-rate support for telecommunications services and Internet access could eliminate the availability of any funding for internal connections.¹⁶⁶

¹⁵⁹ National Broadband Plan at 237 (NBP Recommendation 11.16).

¹⁶⁰ *Id.*

¹⁶¹ *Id.*

¹⁶² National Broadband Plan at 256 (NBP Recommendation 11.18).

¹⁶³ *Id.* (calculated using publicly available Gross Domestic Product deflators from 1997 to 2009 yields total monetary deflation of \$676 million).

¹⁶⁴ *Id.*

¹⁶⁵ See *supra* paras. 63-65.

¹⁶⁶ See ALA NBP Public Notice #15 Comments at 19; SECA NBP Public Notice #15 Comments at 30; Wisconsin DPI NBP Public Notice #15 Comments at 6-7.

68. In this NPRM, we seek comment on how to ensure that schools and libraries receive funding for internal connections (priority two services). We have two important goals in mind: (1) providing funding for internal connections to more schools and libraries than in the past; and (2) ensuring a predictable amount of funding available to schools and libraries for internal connections each year.

1. Predictable Internal Connections Funding for More Schools and Libraries

69. One option would be to allocate funding for internal connections based on a per student cap per school district, to which the applicant's discount rate would be applied. Under this option, libraries would be eligible to receive the same amount of funding as the public school districts within which they are located.¹⁶⁷ To ensure that a predictable amount of funding is available for internal connections, we could set aside a defined amount of funding before funding is allocated to telecommunications and internet access, current priority one services. If we choose this option, we also could eliminate the 2-in-5 rule. Another option would be to eliminate support for basic maintenance for internal connections, or, in the alternative, to cap the amount available for basic maintenance. We seek comment on whether and, if so, how we could phase in any of these proposals on a trial basis to examine the distributional impacts of such rule changes. In what funding year should any of these options be implemented? Commenters should provide specific proposals on the timing and staging of specific reforms. We further describe these options below and seek comment.

70. We believe that these options for reforming how we fund internal connections could have several advantages over our current rules. First, the current discount matrix and rules of priority have the effect of providing funding to a limited number of school districts that have the very highest percentage of students eligible for free or reduced price school lunch, while providing nothing to other districts that are significantly impoverished. Second, many stakeholders have expressed a desire for a more predictable funding mechanism whereby schools and libraries would know on a yearly basis how much funding they will receive for internal connections. This predictability is essential so that schools and libraries can better plan for their future technological needs. If, for instance, a certain amount of total funding would be designated for internal connections, USAC would be able to issue funding commitment decision letters earlier for priority two projects, enabling schools and libraries to begin projects more quickly.

71. *Capped Amount.* To create a more predictable funding mechanism for priority two services, we seek comment on establishing a flat per student cap per school district for each funding year, with the applicant's discount rate applied after the cap is determined.¹⁶⁸ For example, if the cap were set at \$15 per student, a school district that has 100,000 students would have a cap of \$1.5 million in internal connections funding. If the district were eligible for an 75 percent discount (that is, a school with 50 percent to 74 percent of its students eligible for free or reduced price lunch), it would be eligible to receive up to \$1.125 million for internal connections each year.¹⁶⁹ If that same school district was eligible for a 30 percent discount (that is, a school with 20 percent to 34 percent of its students eligible for free or reduced price lunch), it could receive up to \$450,000. Under this option, libraries would receive the same discount as the public school districts in which they are located.¹⁷⁰ We seek comment on this option and

¹⁶⁷ We understand that tying library funding to local school districts' support levels, as the E-rate program has always done, may not be the best proxy for the determination of library support for priority two services. As such, we plan to propose additional changes for the allocation of funding specifically for libraries in a future NPRM.

¹⁶⁸ See Appendix A, 47 C.F.R. § 54.505(c).

¹⁶⁹ We also propose to calculate discounts based on school districts instead of individual schools, where those schools are part of a district, to better reflect the actual poverty level of the entire district. See *infra* para. 79.

¹⁷⁰ See *infra* para. 79.

any alternatives that would increase predictability of priority two funding while meeting the goal of ensuring internal connections funding to more schools and libraries.

72. We also seek comment on whether there should be a minimum amount for which a school, library, or school district is eligible, not tied to the number of students. For instance, should we establish a baseline amount of support that would be provided to an eligible facility, and then a variable amount of support depending on the number of students? If a minimum amount is established, what should it be? We note that smaller applicants might receive less funding because of their smaller number of students; however, some types of equipment are not necessarily usage-sensitive. Should there be additional funding provided to rural applicants, either by establishing a higher dollar amount for rural applicants or a higher discount level?

73. We recognize that schools and libraries at the highest discount levels could receive significantly less funding if we were to establish a capped amount than they receive under the current rules. However, in the near future, as demand for priority one services grows, it is likely that, absent changes to the current funding structure, there will be no funding available for internal connections for even the highest-discount applicants.¹⁷¹ In addition, those same schools and libraries may be able to realize savings on their purchase of priority one services if they have greater freedom to use lower-cost fiber, as proposed above, which could free up additional money in their budget to pay for internal connections. And in any event, we are concerned that the same few schools continue to receive all of the available funding, year after year, while many schools that have nearly as many students in poverty receive no funding for internal connections.

74. *Set Aside for Internal Connections.* We seek comment on revising section 54.507 of our rules to set aside a defined amount of funding from the \$2.25 billion fund for internal connections before priority one funding is allocated.¹⁷² We seek comment on an appropriate amount to set aside for internal connections. For instance, would \$500 million be an appropriate amount to set aside for internal connections? Depending on the amount set aside, it is possible that all of the requests for priority one would not be funded. If so, our rules of priority would operate to fund requests from the highest-discount schools first, and it is possible that recipients with the lowest discounts (namely, schools that serve very few students eligible for free or reduced price school lunch) would no longer receive any funding from the E-rate program. We seek comment on whether we should change our rules of priority to effectuate an alternative result.

75. *Threshold for Priority Two Funding.* We seek comment on the appropriate threshold for any revised methodology for internal connections funding. Today, the money effectively is channeled to school districts that have 75 percent or more students eligible for free or reduced-price school lunch. We seek comment on how to focus funding on improving internal connections to a broader group of needy schools, school districts, and libraries. For instance, should we adopt rule changes that would enable school districts where 35 percent or 50 percent of students are eligible for NSLP to obtain predictable funding for internal connections. We encourage parties to submit factual analyses of the distributional impact of alternative thresholds into the record.

¹⁷¹ See United States Government Accountability Office Report to Congressional Requestors, “Long-Term Strategic Vision Would Help Ensure Targeting of E-rate Funds to Highest-Priority Uses,” GAO 09-253 at 13 (March 2009) (“Although requests for Priority 1 services—that is, telecommunications and Internet access—have remained roughly level since 2002, commitments have increased, at least in part, because applicants received a greater proportion of the funds they requested. The increasing amounts committed for Priority 1 services has the effect of decreasing the amounts available for Priority 2 services, which are funded only after all eligible Priority 1 services requests are satisfied.”).

¹⁷² See *supra* para. 69; Appendix A, 47 C.F.R. § 54.507(g)(1)(i).

76. Revised Discount Matrix. Many commenters have suggested that the Commission should revise the priority two discount matrix to enable more school districts to obtain funding for internal connections.¹⁷³ SECA and other commenters argue that altering the discount rate is an effective way to increase the availability of priority two funds and more evenly distribute priority funds to a greater number of entities.¹⁷⁴ Additionally, we note that other governmental programs that award funding for similar purposes require recipients to pay 15 or 20 percent of the total cost.¹⁷⁵ An approach that strengthens incentives for applicants to find the most cost-effective services to meet their needs is an important tool to maximize the public benefits of a finite amount of governmental funding, and could further our efforts to curb waste, fraud, and abuse by applicants and service providers.¹⁷⁶ We seek comment on a revised discount matrix for internal connections and ask whether we should adjust the current level of additional discount provided to rural schools and libraries.¹⁷⁷ Commenters should set forth with specificity an alternative proposed discount matrix.

77. Eliminate the 2-in-5 Rule. We seek comment, in conjunction with the options detailed above, on eliminating section 54.506(c), the 2-in-5 rule, which limits an eligible entity's receipt of discounts on internal connections to twice every five funding years.¹⁷⁸ In the *Schools and Libraries Third Report and Order*, the Commission sought to make funds for internal connections available to more eligible schools and libraries on a regular basis by limiting the frequency with which applicants may receive priority two

¹⁷³ See e.g., KS NBP Public Notice #15 Comments at 13-14 (supporting a reduction of the highest priority one discount level from 90 percent to 80 percent); SECA NBP Public Notice #15 Comments at 22-25; SECA NBP Public Notice #15 Reply Comments at 7 (proposing to lower the maximum priority two discount from 90 percent to 75 percent so that priority two funding will be more evenly distributed to a greater number of underfunded entities); AK DOE NBP Public Notice #15 Comments at 82, 88-89 (proposing to lower the maximum priority two discount to 70 percent); AASA & AESA NBP Public Notice #15 Comments at 7-8 (asserting that the Commission should require a greater priority two "buy-in" for 90 percent schools so they might have a more vested ownership in the process and think more carefully about proposed projects). *But see* ASD NBP Public Notice #15 Comments at 21 (change in priority one discount level would have adverse consequences with existing contracts, technology planning, and budgetary projections); EdLiNC NBP Public Notice #15 Comments at 6 (arguing that requiring applicants to bear a greater share of the costs would damage school and library budgets); *see also* Iowa NBP Public Notice #15 Comments at 10; ENA NBP Public Notice #15 Comments at 9; NYS OCFS NBP Public Notice #15 Comments at 5.

¹⁷⁴ See SECA NBP Public Notice #15 Comments at 22-25; AK DOE NBP Public Notice #15 Comments at 82, 88-89.

¹⁷⁵ We note that the Commission's universal service Rural Health Care (RHC) Pilot Program provides funding only for up to 85 percent of an applicant's costs. See *Rural Health Care Support Mechanism*, WC Docket No. 02-60, Order, 21 FCC Rcd 11111, 11112, para. 3 (2006) (*2006 Pilot Program Order*). Similarly, awardees in the Broadband Technology Opportunities Program (BTOP), administered by the National Telecommunications and Information Administration, are required to provide matching funds of at least 20 percent toward the total eligible project cost. See 74 Fed. Reg. 33,104, 33,112 (July 9, 2009); 75 Fed. Reg. 3792, 3799 (Jan. 22, 2010). We also note that participants in the Distance Learning and Telemedicine Grant program under the Rural Utilities Service, an agency of the United States Department of Agriculture, must contribute at least 15 percent of the total amount of financial assistance requested. See 7 CFR 1703.125(g).

¹⁷⁶ *Id.*

¹⁷⁷ See 47 C.F.R. §§ 54.505(b), (d).

¹⁷⁸ *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26917-20, paras. 11-18; 47 C.F.R. § 54.506(c). The Commission exempted basic maintenance services from this restriction. *Id.* at 26917, para. 11. For example, under this rule, a school or library could receive support for internal connections in funding years 2005, 2008, and 2011. Alternately, a school that received support for priority two services in funding years 2005 and 2006 will not be eligible to receive support for priority two services until funding year 2010.

discounts.¹⁷⁹ Further, the Commission concluded that, by precluding a particular entity from receiving support for priority two discounts every year, the rule would strengthen incentives for applicants not to waste program resources by replacing or upgrading equipment on an annual basis but rather to fully use equipment purchased with universal service funds.¹⁸⁰

78. However, the 2-in-5 rule has not served its intended purposes. Today, funding for maintenance represents roughly 15 percent of all priority two funding, with the very largest school districts receiving most of that funding. The rule has not increased the availability of priority two funding to more eligible schools and libraries on a regular basis. In addition, because the availability of funding is dependent, in part, on the amount of funding sought by higher-discount eligible entities, the 2-in-5 rule actually has increased the unpredictability of priority two funding. Additionally, commenters argue that, instead of increasing the incentive for applicants to not waste program resources, the rule has encouraged schools to undertake large projects that might not be necessary and discriminates against schools that undertake smaller, more long-term projects.¹⁸¹ We seek comment on any potential implications the elimination of the 2-in-5 rule may have upon current recipients of funding for maintenance and how to address such implications.

79. *Application by School District.* We seek comment on requiring schools and libraries to submit applications for internal connections by school district, not by individual school. Schools that operate independently from a school district, however, such as private schools and some charter schools, should still apply for discounts individually. We propose, therefore, that any school that is part of an organized school district must apply as part of that district, with libraries receiving the same discount as the public school districts in which they are located.¹⁸² Requiring schools to apply by school district could help streamline the process and will simplify the discount calculation for schools.¹⁸³ Additionally, it would ensure that libraries receive funding for internal connections and at the same discount level as schools located within their school district.

80. *Eliminate funding for basic maintenance for internal connections.* We seek comment on options for modifying the funding of basic maintenance of internal connections.¹⁸⁴ Currently, the ESL lists basic maintenance as a supported priority two service.¹⁸⁵ In the *Universal Service First Report and Order*, the Commission determined that support for internal connections includes “basic maintenance services” that are “necessary to the operation of the internal connections network.”¹⁸⁶ Subsequently, in the *Schools and Libraries Third Report and Order*, the Commission provided further detail on which maintenance services are “necessary” under the terms of the *Universal Service First Report and Order*.¹⁸⁷ The Commission found that basic maintenance services are eligible for universal service support as an internal connections service if, but for the maintenance at issue, the internal connection would not

¹⁷⁹ *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26918, para. 14.

¹⁸⁰ *Id.* at 26919, para. 17.

¹⁸¹ See, e.g., Kuskowkim NBP Public Notice #15 Comments at 6.

¹⁸² *Id.* We note that some schools are operated by a state department of education. A state should file one application for all schools that fall directly under its authority.

¹⁸³ *Id.*

¹⁸⁴ See, e.g., West Virginia DOE NBP Public Notice #15 Comments at 15-17.

¹⁸⁵ See 2010 ESL at 5, 9, 20-21. We are not proposing to change the eligibility of maintenance and technical support for services provided as a component of an eligible telecommunications service under priority one.

¹⁸⁶ See *Universal Service First Report and Order*, 12 FCC Rcd at 9021-22, para. 460.

¹⁸⁷ See *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26921-22, para. 23.

function and serve its intended purpose with the degree of reliability ordinarily provided in the marketplace to entities receiving such services.¹⁸⁸ At that time, the Commission sought to identify maintenance as a separate category for priority two funding in part to provide greater transparency regarding the use of internal connections funding. It appears, however, some recipients of funding for maintenance may be using such funding to pay for ongoing information technology support functions, which siphons funding away from other critical uses.

81. One option would be to eliminate E-rate funding for basic maintenance of internal connections. We seek comment on whether funding of basic maintenance for internal connections should remain on the ESL. First, given that funding for the E-rate program is finite and there is a consistent level of unmet demand, we have concerns that our current rules inadvertently result in basic maintenance effectively taking precedence over funding the internal connections that are necessary to deliver higher bandwidth applications like high definition video streaming to schools and libraries. We believe it may be preferable to spread funding more broadly across needy schools and libraries for internal connections than to provide funding for maintenance of networks for a limited number of school districts. Second, it may be the case that funding for basic maintenance is used to pay for “warranties” on equipment or to support significant information technology departments. Given the limited funding available for internal connections, we question whether the E-rate should be supporting ongoing tech support to address potential problems when there is such unmet demand for actual equipment that will enable services *definitely* to be used. We recognize that maintenance in some form is important for services to be available, but are concerned that our current rules fail to impose appropriate limitations. Third, under our current allocation method, the same schools and school districts receive large amounts of funding year after year for basic maintenance, while others receive nothing.¹⁸⁹ In order to achieve our inclusion objectives, the limited funding available could be better utilized to pay for facilities for schools and libraries serving high poverty populations that have never received funding for internal connections. At least until priority two funding has been distributed more broadly, we ask whether the funding should be used to support initial installation of internal connections rather than pay for maintenance for entities that have already had their internal connections funded through the E-rate program. Finally, eliminating funding for basic maintenance could provide additional incentives for schools and libraries to evaluate carefully the reliability of different solutions from various providers and think seriously about maintenance costs when constructing their internal networks.

82. Another option would be to cap basic maintenance payments and reimburse requests that are based on actual repair and maintenance costs only. Specifically, consistent with the internal connections approach,¹⁹⁰ we seek comment on establishing a per student cap per school district for each funding year, with the applicant’s discount rate applied after the cap is determined. For example, if the per student cap were \$2, a school district with 100,000 students would have a total of up to \$200,000 in E-rate funding for basic maintenance for internal connections. If the district were eligible for a 75 percent discount, it could be eligible to receive up to \$150,000 for maintenance each year. Under this option, libraries would be eligible for up to the same discount as the public school district in which they are located. We believe that this approach would help to ensure that funding for basic maintenance for internal connections is

¹⁸⁸ See *id.* at 26921-22, para. 23. Specifically, the Commission determined that basic maintenance includes repair and upkeep of previously purchased eligible hardware and wire, and basic technical support including configuration changes. The Commission noted that basic maintenance services do not include services that maintain equipment that is not supported or that enhance the utility of equipment beyond the transport of information, or diagnostic services in excess of those necessary to maintain the equipment’s ability to transport information. *Id.*

¹⁸⁹ See USAC website, Schools and Libraries, Funding Request Data Retrieval Tool, available at <http://www.sl.universalservice.org/funding/opendatasearch/Search1.asp> (last visited May 20, 2010).

¹⁹⁰ See *supra* paras. 72-74.

allocated more equitably among the schools and libraries that most need funding support for maintenance. To address the potential waste that occurs by funding maintenance based on estimated costs, we also propose to limit funding for maintenance to actual expenses for repair and maintenance. In order to make this change, we propose to change E-rate program rules to allow applicants to seek E-rate funds for basic maintenance for internal connections in the funding year following the funding year in which they sought and received repairs on internal connections. We seek comment, therefore, on revising section 54.507(d) of the Commission's rules to allow applicants to request funding for basic maintenance that was received in the prior funding year.¹⁹¹

83. For either option (eliminating funding for basic maintenance of internal connections or capping such funding), we seek comment on whether such a change should be phased in over some number of funding years, and, if so, how. In either case, the requirement that applicants seek funding for only basic maintenance would remain unchanged. Specifically, we would continue to find ineligible any services that include maintenance of equipment that is not supported by E-rate or that enhances the utility of equipment beyond the transport of information, as well as diagnostic services in excess of those necessary to maintain the equipment's ability to transport information.¹⁹² Additionally, we seek comment on any other methods we could use to ensure support for basic maintenance is distributed equitably and in a way that is based on actual repair costs. For example, one alternative method could be that funding for basic maintenance could be distributed in the next funding year after the costs were incurred based on the actual amount for labor and parts or equipment.

2. Indexing the Annual Funding Cap to Inflation

84. We propose to amend section 54.507 of our rules to index the E-rate program funding cap to the rate of inflation, on a prospective basis, so that the program maintains its current purchasing power in 2010 dollars.¹⁹³ Many commenters responding to the *NBP Public Notice #15* support adjusting the annual E-rate funding cap to take into account inflation, suggesting that increasing the cap will allow schools and libraries to continue to benefit from upgraded connections that deliver faster and more efficient broadband service as demand for greater capacity increases.¹⁹⁴ In order to maintain predictability, however, we propose that during periods of deflation, the funding cap will remain at the level from the previous funding year.¹⁹⁵ We seek comment on these proposals.

85. We propose using the gross domestic product chain-type price index (GDP-CPI), which is released quarterly.¹⁹⁶ This is the same index used by the Commission to inflation-adjust revenue

¹⁹¹ See 47 C.F.R. § 54.507(d). This rule currently requires applicants receiving funds for non-recurring services to receive such services by the September after the funding year closes.

¹⁹² See *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26921-22, para. 23.

¹⁹³ See Appendix A, 47 C.F.R. §§ 54.507(a)(1), (a)(2).

¹⁹⁴ See, e.g., Dell NBP Public Notice #15 Comments at 4; Kuskowkwim NBP Public Notice #15 Comments at 7; SECA NBP Public Notice #15 Comments at 30; Schools, Health and Libraries Broadband Coalition NBP Public Notice #15 Comments at 4; Texas State Library NBP Public Notice #15 Comments at 2; U.S. Broadband Coalition NBP Public Notice #15 Comments at 36; Technology CEO Council NBP Public Notice #15 Comments at 1.

¹⁹⁵ See West Virginia Department of Education NBP Public Notice #15 Comments at 19.

¹⁹⁶ See, e.g., National Income and Product Accounts Table, Bureau of Economic Analysis, April 2010, Table 1.1.4., available at <http://www.bea.gov/National/nipaweb/TableView.asp?SelectedTable=4&Freq=Qtr&FirstYear=2007&LastYear=2009> (last visited May 20, 2010).

thresholds used for classifying carrier categories for various accounting and reporting purposes.¹⁹⁷ It also is used to calculate adjustments to the annual funding cap for the high cost loop support mechanism, which subsidizes service provided by rural telephone companies.¹⁹⁸ The Commission has noted that the Bureau of Economic Analysis of the Department of Commerce, which produces the index, considers the GDP-CPI a more accurate measure of price changes than other indices for the Commission's purposes.¹⁹⁹ The GDP-CPI is used by the Commission since it reflects price changes in all sectors of the economy.²⁰⁰ While inflation is currently very low, implementation of such a proposal could result in the E-rate cap growing from \$2.25 billion to approximately \$2.55 billion over the next five years if inflation were to occur similar to the historical rate for the last five years. We seek comment on this proposal and on whether there are better ways to index the E-rate funding cap to inflation.

V. CREATING A PROCESS FOR DISPOSAL OF OBSOLETE EQUIPMENT

A. Background

86. *E-rate Program Rules and Requirements.* Once an eligible school or library has purchased services at a discount under the E-rate program, section 254(h)(3) of the Act prohibits that school or library from reselling or otherwise transferring the purchased service, or any equipment components of such a service, in consideration for money or any other thing of value.²⁰¹ In the *Schools and Libraries Third Report and Order*, the Commission further prohibited schools and libraries from transferring the equipment components of eligible services to other schools within three years of their purchase, even without receiving money or other consideration in return for the equipment, with one exception.²⁰² If the school or library that orders the eligible services or equipment permanently or temporarily closes, then that school or library can transfer any services and equipment components of those services to another school or library, so long as the school or library notifies USAC of the transfer.²⁰³ The Act and the Commission's rules, however, do not specifically address what schools and libraries should do with equipment acquired with E-rate support once the equipment has become obsolete.

87. *E-Rate Central Petition for Clarification or Waiver.* E-Rate Central subsequently filed a petition for clarification or waiver of the Commission's rules concerning the disposal of equipment

¹⁹⁷ See, e.g., 47 C.F.R. § 32.9000 (defining mid-sized incumbent local exchange carrier with annual revenue indexed for inflation as measured by the Department of Commerce Gross Domestic Product Chain-type Price Index (GDP-CPI)).

¹⁹⁸ See 47 C.F.R. § 36.603(c). For the high cost loop support, the annual cap is adjusted by the "Rural Growth Factor," which is the sum of the annual percentage change in GDP-CPI and the annual percentage change in the number of rural incumbent telephone company phone lines, known as working loops. Because phone lines have been declining at a greater rate than inflation in recent years, the net result has been a downward adjustment in annual funding under that program.

¹⁹⁹ See *Implementation of the Telecommunications Act of 1996: Reform of Filing Requirements and Carrier Classifications*, CC Docket No. 96-193, Order and Notice of Proposed Rulemaking, 11 FCC Rcd 11716, 11721-22, para. 10 (1996) (*ARMIS NPRM*); *Implementation of the Telecommunications Act of 1996*, CC Docket No. 96-193, Report and Order, 12 FCC Rcd 8071, 8091, para. 41 (1997) (*ARMIS Order*).

²⁰⁰ *ARMIS NPRM*, 11 FCC Rcd at 11721-22, para. 10; *ARMIS Order*, 12 FCC Rcd at 8091, para. 41.

²⁰¹ 47 U.S.C. § 254(h)(3); see also 47 C.F.R. § 54.513(a) (2009).

²⁰² *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26923-24, paras. 26-28; 47 C.F.R. § 54.513(c).

²⁰³ *Schools and Libraries Third Report and Order*, 18 FCC Rcd at 26924, paras. 27-28; 47 C.F.R. § 54.513(c).

purchased under the E-rate program.²⁰⁴ Specifically, E-Rate Central sought guidance from the Commission on the proper method for disposing of equipment when its value or usefulness precludes the possibility of transferring the equipment to another eligible facility.²⁰⁵ E-Rate Central noted that the Commission's rules for the disposal of equipment funded under the E-rate program, which prohibit eligible services and equipment components from being sold or transferred in consideration of anything of value, may conflict with New York's state regulations mandating that obsolete equipment shall be sold through bid procedures, if possible, for the highest possible price.²⁰⁶ E-Rate Central argued that because much of the equipment purchased with E-rate funds becomes obsolete and expensive to retain after several years, schools and libraries should be allowed to dispose of obsolete equipment through a public auction or any other lawful means.²⁰⁷ Thus, E-Rate Central requested that the Commission clarify that the E-rate equipment transfer rules are meant to apply only to equipment being transferred from one location for use in another, not to the normal disposal of unusable surplus equipment.²⁰⁸

88. In the absence of specific rules governing the disposal of equipment, E-Rate Central proposed five principles to govern appropriate equipment disposal procedures.²⁰⁹ These five principles include: (1) the equipment subject to disposal has exceeded its useful life which, as a rebuttable presumption, is deemed to be five years; (2) the equipment subject to disposal is formally declared to be surplus by the school board, internal auditor, or other authorized body or individual; (3) the disposal process fully complies with state and local laws; (4) in the event any significant, non *de minimis* value is realized as a result of the disposal process, the applicant should return funds to USAC in proportion to the E-rate support received for the initial purchase (E-Rate Central suggested a definition of *de minimis* as any value that would result in the return of funds to USAC of \$1,000 or less); and (5) a record of the disposal must be maintained in compliance with the existing E-rate record retention rules.²¹⁰

²⁰⁴ See E-Rate Central Petition for the Clarification or Waiver of E-Rate Rules Concerning the Disposal of Equipment Purchased Under the Schools and Libraries Universal Support Mechanism, CC Docket No. 02-6 (filed Sept. 13, 2006) (E-Rate Central Petition).

²⁰⁵ See E-Rate Central Petition at 2.

²⁰⁶ See *id.* at Attachment A (citing to New York State Boards of Cooperative Educational Services' (BOCES) Regulation on Sale and Disposal of BOCES Property).

²⁰⁷ *Id.* at 1-2.

²⁰⁸ *Id.* at 2. The Bureau released a public notice seeking comment on E-Rate Central's petition. See *E-Rate Central Petition for Clarification or Waiver of the Commission's Rules Concerning the Disposal of Equipment Purchased Under the Schools and Libraries Universal Support Mechanism*, CC Docket No. 02-6, Public Notice, 21 FCC Rcd 13750 (Wireline Comp. Bur. 2006). In response to the public notice, the Bureau received comments from BellSouth Corporation (BellSouth) and the State E-rate Coordinators' Alliance (SECA), and one reply comment from AT&T, Inc. (AT&T). See Comments of BellSouth Corporation, CC Docket No. 02-6 (filed Dec. 18, 2006) (BellSouth E-rate Central Petition Comments); Comments of State E-rate Coordinators' Alliance, CC Docket No. 02-6 (filed Dec. 18, 2006) (SECA E-rate Central Petition Comments); Comments of AT&T, Inc., CC Docket No. 02-6 (filed Jan. 8, 2007) (AT&T E-rate Central Petition Reply Comments). In response to E-Rate Central's petition, the Commission also received an *ex parte* proposal filed by CXtec. Letter from Barbara S. Ashkin, VP & Chief Operating Officer, CXtec *et al.*, to the Federal Communications Commission, CC Docket No. 02-6 (filed May 21, 2007) (CXtec *Ex Parte*). CXtec is a Syracuse, New York, company that sells both new and pre-owned technology equipment. See *id.* at 1. CXtec proposes that the Commission apply the General Services Administration's (GSA) Exchange/Sale regulations to the E-rate program, which would allow a school or library seeking to replace aging equipment to sell or exchange that equipment and use the proceeds from that sale or exchange to purchase new equipment. See CXtec *Ex Parte* at 4; 41 C.F.R. § 102-39 (Replacement of Personal Property Pursuant to the Exchange/Sale Authority).

²⁰⁹ See E-Rate Central Petition at 2-3.

²¹⁰ *Id.*

B. Discussion

89. We propose to amend section 54.513 of our rules establishing how participants in the E-rate program may dispose of obsolete equipment purchased with E-rate discounts.²¹¹ We also propose revising an FCC form to report such equipment disposals to USAC. The changes we propose seek to balance the competing concerns of providing schools and libraries the flexibility to dispose of obsolete equipment and the need to guard against waste, fraud, and abuse within the E-rate program. We seek comment on our proposed changes provided below.

90. *Process for Disposal of Obsolete Equipment.* We seek comment on permitting the disposal of E-rate equipment for payment or other consideration, subject to four of E-Rate Central's proposed five principles.²¹² We propose to revise section 54.513 of our rules to provide for the disposal of equipment for payment or other consideration where such equipment has exhausted its useful life.²¹³ We clarify that, to the extent a school or library chooses to dispose of equipment purchased using E-rate funds and does not receive monetary payment or other consideration, it may do so without complying with these proposed rules. As BellSouth suggests, the Commission encourages schools and libraries to recycle the equipment when feasible.²¹⁴ We do not believe, however, that it is necessary to adopt a requirement that applicants return any non-*de minimis* value, as discussed below.²¹⁵ Specifically, we believe that the Act's prohibition on the sale, resale, or transfer of telecommunications services and network capacity was intended to prevent applicants from profiting from supported services during the time that the applicant is supposed to be using them.²¹⁶ We do not believe this prohibition extends to when the applicant is no longer utilizing equipment purchased with the assistance of E-rate funds because the equipment is past its useful life. Thus, we propose to allow schools and libraries to dispose of equipment for payment or other consideration under the following conditions: (1) the equipment has exhausted its useful life but no sooner than five years after the equipment is installed; (2) the equipment is formally declared to be surplus by the school board, information technology officer, or other authorized body or individual; (3) the school or library notifies USAC within 90 days of disposal and keeps a record of the disposal for a period of five years following the disposal; and (4) the disposal process fully complies with state and local laws, where applicable. We discuss these conditions separately below.

91. First, we propose that schools and libraries be permitted to sell or trade in equipment after the equipment has exhausted its useful life. We agree with commenters that there should be a rebuttable presumption of no less than five years from the installation date for the useful life of any equipment purchased using E-rate funds.²¹⁷ Commenters note that the absence of rules specifically addressing the disposal of equipment purchased under the E-rate program when it has reached the end of its useful life has led some schools and libraries to place obsolete, out-of-service equipment in school basements or

²¹¹ See Appendix A, 47 C.F.R. § 54.513 (d).

²¹² See E-Rate Central Petition at 2-3.

²¹³ See Appendix A, 47 C.F.R. § 54.513(d).

²¹⁴ See BellSouth E-Rate Central Petition Comments at 2.

²¹⁵ See *infra* para. 94.

²¹⁶ See *supra* para. 86.

²¹⁷ See E-Rate Central Petition at 2 (arguing that "much of the electronic equipment eligible for E-rate discounts has a limited technical and economic life of 3-5 years"); SECA E-Rate Central Petition Comments at 1 (supporting E-Rate Central's petition); see also AT&T E-Rate Central Petition Reply Comments at 1; BellSouth E-Rate Central Petition Comments at 1.

other on-campus storage locations.²¹⁸ Such indefinite storage imposes additional needless costs on schools and libraries. Additionally, our silence may have encouraged some schools or libraries to simply throw away unused equipment, even though that same equipment could be put to use by others.²¹⁹ We seek comment on permitting the disposal of E-rate equipment for payment or other consideration, subject to certain conditions. Specifically, we seek comment on whether five years is a reasonable minimum time period for retaining equipment components purchased using an E-rate discount. Further, this proposal would count five years from the date of installation. We seek comment on whether that is the appropriate date from which to count five years or whether some other date, such as purchase date, is more appropriate. We note that our proposal would not require schools and libraries to continue using the equipment for five years, but they could not resell or trade it in before five years had passed.

92. Second, we seek comment on the proposal suggested by commenters to require applicants to formally declare that the equipment is surplus.²²⁰ We propose to require that the school board or other authorized body make the formal declaration. We note that E-rate Central proposed that an internal auditor may make the formal declaration. While we do not believe that is typically the function of an internal auditor, we do not preclude schools or libraries from having such a person make the declaration at their discretion. We believe this formal process will prevent applicants from disposing of equipment prematurely. We also propose that the formal declaration be subject to the Commission's document retention rules, as detailed in section 54.516.²²¹

93. Third, we propose that schools and libraries notify USAC of the resale or trade of equipment funded via the E-rate program within 90 days of its disposal. We also propose that applicants be required to keep a record of the disposal for a period of five years following the disposal.²²² To implement this requirement, we propose to revise the FCC Form 500 (Adjustment to Funding Commitment and Modification to Receipt of Service Confirmation), as discussed below, to require applicants to submit certain information to USAC documenting the resale or trade of their equipment.²²³ We seek comment on these proposals.

94. In setting forth these proposed conditions, we seek comment on E-rate Central's proposal to require the return of any funds that are related to the resale or trade of E-rate equipment.²²⁴ We seek comment on whether E-rate Central's proposed *de minimus* threshold of \$1000 should be set at a higher level to reduce administrative burden.²²⁵ In many instances, the value of equipment after five years of purchase in all likelihood would be so small that it would not justify requiring schools to return a portion of the proceeds to USAC. As SECA notes, the administrative and financial burden on USAC and

²¹⁸ See E-Rate Central Petition at 2; SECA E-Rate Central Petition Comments at 1; AT&T E-Rate Central Petition Reply Comments; CXtec *Ex Parte*.

²¹⁹ To the extent that schools or libraries believe their equipment has no value, we encourage them to recycle the equipment when feasible.

²²⁰ See E-Rate Central Petition at 2; BellSouth E-Rate Central Petition Comments at 2; SECA E-Rate Central Petition Comments at 1.

²²¹ See 47 C.F.R. § 54.516.

²²² See E-Rate Central Petition at 2.

²²³ See *infra* paras. 95-96.

²²⁴ See E-Rate Central Petition at 3; AT&T E-Rate Central Petition Reply Comments at 2.

²²⁵ E-Rate Central Petition at 3 (proposing that "the applicant should return funds to USAC in proportion to the E-rate support received for the initial purchase"); see also AT&T E-Rate Central Petition Reply Comments at 2 ("AT&T would encourage efforts to return non-*de minimis* funds to USAC resulting from the sale by applicants of obsolete equipment that applicants purchased, in part, with E-Rate funds.").

applicants of documenting and processing any such refunds would far outweigh the value of the funds being returned since such refunds would be minimal.²²⁶ Further, requiring applicants to return any funds related to the disposal of E-rate equipment could deter them from disposing unneeded equipment. We seek comment on these proposals.

95. *Revised FCC Form 500*. Currently, to help the Commission track the use of equipment components purchased with E-rate discounts, schools and libraries are required to “maintain asset and inventory records of equipment purchased as components of supported internal connections services sufficient to verify the actual location of such equipment for a period of five years after purchase.”²²⁷ Similarly, if a school or library closes and transfers services or equipment components thereof to another school or library, the transferor “must notify [USAC] of the transfer, and both the transferor and recipient must maintain detailed records documenting the transfer and the reason for the transfer for a period of five years.”²²⁸ Consistent with the Commission’s recordkeeping and reporting requirements, we propose to revise the FCC Form 500 to require schools and libraries to report to USAC the disposal of equipment purchased with an E-rate discount for payment or other consideration. Specifically, the revised FCC Form 500 would require a school or library disposing of equipment to report the following information to USAC:

- (A) the applicant’s name, entity number, address, and telephone number;
- (B) the name, address, telephone number, and email address of the applicant’s authorized point of contact;
- (C) the date of the disposal of obsolete equipment;
- (D) the name of each piece of equipment disposed of, including the date of purchase and the funding request number(s) associated with the disposed equipment;
- (E) any payment, trade-in value, or other consideration received for such disposal of equipment;
- (F) the name of the entity that paid or otherwise gave the applicant valuable consideration for the equipment;
- (G) formal declaration by the school board or other authorized body or individual that the equipment subject to disposal is surplus; and
- (H) certification that the information provided on the form is true and accurate to the best of the applicant’s knowledge, evidenced by the signature of someone authorized to so certify by the applicant and the date.

96. Requiring schools and libraries to submit this information as part of the FCC Form 500 could facilitate our ongoing efforts to mitigate waste, fraud and abuse. Collecting this information would allow USAC and the Commission to better assess how long program participants are using equipment purchased with E-rate discounts prior to disposal of any obsolete equipment, and to track what E-rate program participants do with equipment they no longer use. Moreover, such revision would require limited information, all of which is easy to obtain whenever a school or library seeks to dispose of obsolete equipment. We seek comment on revising the FCC Form 500 and ways in which to further minimize any potential burdens on applicants while guarding against waste, fraud, and abuse in the E-rate

²²⁶ See SECA E-Rate Central Petition Comments at 2 (“[W]e strongly suspect that the administrative cost of processing any such refunds would far outweigh the value of the funds being returned.”).

²²⁷ 47 C.F.R. § 54.516(a).

²²⁸ 47 C.F.R. § 54.513(c).

program. We also seek comment on the information that we propose to obtain from applicants and whether less or more information would be appropriate.

VI. PROCEDURAL MATTERS

A. Initial Regulatory Flexibility Analysis

97. As required by the Regulatory Flexibility Act of 1980, as amended,²²⁹ the Commission has prepared an Initial Regulatory Flexibility Analysis (IRFA) for this NPRM, of the possible significant economic impact on a substantial number of small entities by the policies and rules proposed in this NPRM. The IRFA is in Appendix E. Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments on the Notice. The Commission will send a copy of the Notice, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration.²³⁰ In addition, the Notice and IRFA (or summaries thereof) will be published in the Federal Register.²³¹

B. Paperwork Reduction Act Analysis

98. This document contains proposed modified information collection requirements. The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public and the Office of Management and Budget (OMB) to comment on the information collection requirements contained in this document, as required by the Paperwork Reduction Act of 1995, Public Law 104-13. In addition, pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, *see* 44 U.S.C. 3506(c)(4), we seek specific comment on how we might further reduce the "information collection burden for small business concerns with fewer than 25 employees."

C. *Ex Parte* Presentations

99. These matters shall be treated as a "permit-but-disclose" proceeding in accordance with the Commission's *ex parte* rules.²³² Persons making oral *ex parte* presentations are reminded that memoranda summarizing the presentations must contain summaries of the substance of the presentations and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.²³³ Other requirements pertaining to oral and written presentations are set forth in section 1.1206(b) of the Commission's rules.²³⁴

D. Comment Filing Procedures

100. We invite comment on the issues and questions set forth in the NPRM and IRFA contained herein. Pursuant to sections 1.415 and 1.419 of the Commission's rules,²³⁵ interested parties may file comments on this NPRM within 30 days after publication in the Federal Register and may file reply comments within 45 days after publication in the Federal Register. **All filings related to this NPRM shall refer to CC Docket No. 02-6 and GN Docket No. 09-51.** Comments may be filed using:

²²⁹ See 5 U.S.C. § 603.

²³⁰ See 5 U.S.C. § 603(a).

²³¹ *Id.*

²³² 47 C.F.R. §§ 1.1200-1.1216.

²³³ 47 C.F.R. § 1.1206(b)(2).

²³⁴ 47 C.F.R. § 1.1206(b).

²³⁵ 47 C.F.R. §§ 1.415, 1.419.

(1) the Commission's Electronic Comment Filing System (ECFS), (2) the Federal Government's eRulemaking Portal, or (3) by filing paper copies. See *Electronic Filing of Documents in Rulemaking Proceedings*, 63 FR 24121 (1998).

- Electronic Filers: Comments may be filed electronically using the Internet by accessing the ECFS: <http://fjallfoss.fcc.gov/ecfs2/> or the Federal eRulemaking Portal: <http://www.regulations.gov>.
- Paper Filers: Parties who choose to file by paper must file an original and four copies of each filing. If more than one docket or rulemaking number appears in the caption of this proceeding, filers must submit two additional copies for each additional docket or rulemaking number.

Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail. All filings must be addressed to the Commission's Secretary, Office of the Secretary, Federal Communications Commission.

- All hand-delivered or messenger-delivered paper filings for the Commission's Secretary must be delivered to FCC Headquarters at 445 12th St., SW, Room TW-A325, Washington, DC 20554. The filing hours are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes must be disposed of before entering the building.
- Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743.
- U.S. Postal Service first-class, Express, and Priority mail must be addressed to 445 12th Street, SW, Washington DC 20554.

People with Disabilities: To request materials in accessible formats for people with disabilities (braille, large print, electronic files, audio format), send an e-mail to fcc504@fcc.gov or call the Consumer & Governmental Affairs Bureau at 202-418-0530 (voice), 202-418-0432 (tty).

101. Parties must also send a courtesy copy of their filing to Charles Tyler, Telecommunications Access Policy Division, Wireline Competition Bureau, Federal Communications Commission, 445 12th Street, S.W., Room 5-B540, Washington, D.C. 20554. Charles Tyler's e-mail address is Charles.Tyler@fcc.gov and his telephone number is (202) 418-7400.

102. Filings and comments are also available for public inspection and copying during regular business hours at the FCC Reference Information Center, Portals II, 445 12th Street, S.W., Room CY-A257, Washington, D.C., 20554. Copies may also be purchased from the Commission's duplicating contractor, BCPI, 445 12th Street, S.W., Room CY-B402, Washington, D.C. 20554. Customers may contact BCPI through its website: www.bcpiweb.com, by e-mail at fcc@bcpiweb.com, by telephone at (202) 488-5300 or (800) 378-3160, or by facsimile at (202) 488-5563.

103. Comments and reply comments must include a short and concise summary of the substantive arguments raised in the pleading. Comments and reply comments must also comply with section 1.49 and all other applicable sections of the Commission's rules.²³⁶ We direct all interested parties to include the name of the filing party and the date of the filing on each page of their comments

²³⁶ See 47 C.F.R. § 1.49.

and reply comments. All parties are encouraged to utilize a table of contents, regardless of the length of their submission. We also strongly encourage parties to track the organization set forth in the NPRM in order to facilitate our internal review process.

104. For further information, contact Regina Brown at (202) 418-0792 or James Bachtell at (202) 418-2694 in the Telecommunications Access Policy Division, Wireline Competition Bureau.

VII. ORDERING CLAUSES

105. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1 through 4, 201-205, 254, 303(r), and 403 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996, 47 U.S.C. §§ 151 through 154, 201 through 205, 254, 303(r), and 403, this Notice of Proposed Rulemaking IS ADOPTED.

106. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, SHALL SEND a copy of this Notice of Proposed Rulemaking, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION



Marlene H. Dortch
Secretary

APPENDIX A**Proposed Rules**

For the reasons discussed in the preamble, the Federal Communications Commission proposes to amend 47 C.F.R. Part 54 as follows:

PART 54 - UNIVERSAL SERVICE

1. The authority citation for Part 54 continues to read as follows:

Authority: 47 U.S.C. §§ 1, 4(i), 201, 205, 214, and 254 unless otherwise noted.

2. Amend § 54.5 to read as follows:

§ 54.5 Definitions.

Rural area. For purposes of the rural health care universal service support mechanism, a “rural area” is an area that is entirely outside of a Core Based Statistical Area; is within a Core Based Statistical Area that does not have any Urban Area with a population of 25,000 or greater; or is in a Core Based Statistical Area that contains an Urban Area with a population of 25,000 or greater, but is within a specific census tract that itself does not contain any part of a Place or Urban Area with a population of greater than 25,000. “Core Based Statistical Area” and “Urban Area” are as defined by the Census Bureau and “Place” is as identified by the Census Bureau.

3. Amend § 54.500 by adding new subsections (a), (e), (o), (p), and (q), eliminating subsection (m), and re-designating subsections (a), (b), and (c) as (b), (c), (d), re-designating subsections (d), (e), (f), (g), (h), (i), (j), (k), (l) as (e), (f), (g), (h), (i), (j), (k), (l), and (m), and re-designating subsections (k) and (l) as (r) and (s) to read as follows:

§ 54.500 Terms and definitions.

(a) **Applicant.** For purposes of this subpart, an “applicant” is an eligible school or library, or a consortium that includes an eligible school or library.

(b) * * *

(c) * * *

(d) * * *

(e) Internal connections. For purposes of this subpart, a service is eligible for support as a component of an institution's "internal connections" if such service is necessary to transport information within one or more instructional buildings of a single school campus or within one or more non-administrative buildings that comprise a single library branch.

(f) * * *

(g) * * *

(h) * * *

(j) * * *

(k) * * *

(l) * * *

(m) * * *

(o) Priority one services. For purposes of this subpart, "priority one services" are telecommunications services, Internet access, and information services as designated annually by the Commission in the Eligible Services List.

(p) Priority two services. For purposes of this subpart, "priority two services" are internal connections, as designated annually by the Commission in the Eligible Services List.

(q) Rural area. For purposes of this subpart, a "rural area" is within a territory whose locale code is classified as either rural-fringe, rural-distant, or rural-remote by the U.S. Department of Education's National Center for Education Statistics.

(r) * * *

(s) * * *

4. Amend § 54.501 by revising subsection (a) to read as follows:

§ 54.501 Eligibility for service provided by telecommunications carriers.

(a) Telecommunications carriers shall be eligible for universal service support under this subpart for providing supported services to eligible applicants.

* * * * *

5. Amend § 54.502, as proposed in FCC 09-105,²³⁷ to read as follows:

§ 54.502 Supported services.

(a) Telecommunications services - For purposes of this subpart, supported telecommunications services provided by telecommunications carriers include all commercially available telecommunications services in addition to all reasonable charges that are incurred by taking such services, such as state and federal taxes. Charges for termination liability, penalty surcharges, and other charges not included in the cost of taking such service shall not be covered by the universal service support mechanisms. Supported telecommunications services are designated annually in the Eligible Services List by the Commission in accordance with section 54.503 of the Commission's rules.

(b) Internet access and information services – For purposes of this subpart, supported Internet access and information services include basic conduit access to the Internet and the services defined in section 54.5 of the Commission's rules as Internet access. Supported Internet access and information services are designated annually by the Commission in the Eligible Services List in accordance with section 54.503 of the Commission's rules.

(c) Internal connections – For purposes of this subpart, supported internal connections are defined in §54.500(e) as eligible services. Discounts are not available for internal connections in non-instructional buildings of a school or school district, or in administrative buildings of a library, to the extent that a library system has separate administrative buildings, unless those internal connections are essential for the effective transport of information to an instructional building of a school or to a non-administrative building of a library. Internal connections do not include connections that extend beyond a single school

²³⁷ The proposed rule language in italics includes the rules as proposed in FCC 09-105.

campus or single library branch. There is a rebuttable presumption that a connection does not constitute an internal connection if it crosses a public right-of-way. Supported internal connections are defined and listed in the Eligible Services List as updated annually in accordance with section 54.503 of the Commission's rules.

(d) Non-telecommunications carriers shall be eligible for universal service support under this subpart for providing the supported services described in paragraph (b) and (c) of this section for eligible schools, libraries, and consortia including those entities. Such services provided by non-telecommunications carriers shall be subject to all the provisions of this subpart, except Sections 54.501(a), 54.502(a), and 54.515.

6. Amend § 54.504 by eliminating subsections (a) and (b) and revising and re-designating subsection (c) as subsection (a), and by re-designating subsections (d), (e), (f), (g), and (h) as subsections (b), (c), (d), (e), and (f) to read as follows:

§ 54.504 Requests for services.

(a) Filing of FCC Form 471. An applicant seeking to receive discounts for eligible services as designated by the Commission on the eligible services list under this subpart shall, upon signing a contract for eligible services, submit a completed FCC Form 471 to the Administrator. A commitment of support is contingent upon the filing of FCC Form 471.

(1) The FCC Form 471 shall be signed by the person authorized to order telecommunications services for the applicant and shall include that person's certification under oath that:

(i) * * *

(ii) * * *

(iii) * * *

(iv) All of the schools and libraries listed on the FCC Form 471 application are:

(A) covered by an individual or higher-level technology plan for using the services requested in the application that meets the requirements of § 54.508 of the Commission's rules;

(B) are not covered by a technology plan because the application requests only eligible priority one services as defined in § 54.500(1) and the applicant is subject to state or local technology planning requirements; or

(C) are not covered by a technology plan because the application requests only basic telecommunications services

(v) The applicant's technology plan(s) has/have been/will be approved by a state or other authorized body consistent with § 54.508 of this subpart.

(vi) * * *

(vii) The services the applicant purchases at discounts will be used solely for educational purposes and will not be sold, resold, or transferred in consideration for money or any other thing of value. Services that the applicant purchases at discounts are not deemed sold, resold, or transferred in consideration for money or any other thing of value if disposed pursuant to § 54.513.

(viii) * * *

(ix) * * *

(x) * * *

(xi) All bids submitted to an applicant seeking eligible services were carefully considered and the most cost-effective bid was selected in accordance with § 54.510 of this subpart, with price being the primary factor considered, and is the most cost-effective means of meeting educational needs and technology plan goals.

(2) * * *

(d) * * *

(e) Rate disputes. If they reasonably believe that the lowest corresponding price is unfairly high or low, applicants may have recourse to the Commission, regarding interstate rates, and to state commissions, regarding intrastate rates

(1) Applicants may request lower rates if the rate offered by the carrier does not represent the lowest corresponding price.

(2) Service providers may request higher rates if they can show that the lowest corresponding price is not compensatory, because the relevant applicant is not similarly situated to and subscribing to a similar set of services to the customer paying the lowest corresponding price.

* * * * *

7. Amend § 54.505 by revising subsection (b) to read as follows:

§ 54.505 Discounts.

(a) * * *

(b) Discount percentages. The discounts available to eligible schools and libraries shall range from 20 percent to 90 percent of the pre-discount price for eligible services as designated by the Commission. The discounts available to a particular applicant shall be determined by indicators of poverty and high cost.

(1) * * *

(2) * * *

(3) The Administrator shall classify schools and libraries as “urban” or “rural” based on location in an urban or rural area, according to the following designations.

(i) Schools and libraries whose locale code is city, suburb, town-fringe, or rural-fringe, as measured by the U.S. Department of Education’s National Center for Education Statistics, shall be designated as urban.

(ii) Schools and libraries whose locale code is town-distant, town-remote, rural-distant, or rural-remote, as measured by the U.S. Department of Education’s National Center for Education Statistics, shall be designated as rural.

(4) Applicants shall calculate discounts on supported services described in § 54.502 or other supported special services described in § 54.503 by first calculating a single discount percentage rate for the entire school district by dividing the total number of students eligible for the National School Lunch Program or **other alternative eligible mechanism** by the total number of students in the district. Applicants shall then compare that single figure against the discount matrix to determine the school district's discount for priority one and priority two services. All schools and libraries within that school district shall receive the same discount rate.

* * * * *

9. Amend § 54.507 by revising subsections parts (a), (a)(1), (a)(2), (c), (d), to read as follows:

§ 54.507 Cap.

(a) **Amount of the annual cap.** The annual funding cap on federal universal service support for schools and libraries shall be \$2.25 billion in funding year 2010. In funding year 2011 and subsequent funding years, the funding cap shall be automatically increased annually to take into account increases in the rate of inflation as calculated in subpart (a)(1). All funds collected that are unused shall be carried forward into subsequent funding years for use in the schools and libraries support mechanism in accordance with the public interest and notwithstanding the annual cap.

(1) **Increase Calculation.** To measure increases in the rate of inflation for annual automatic increase purposes, the Commission shall use the Gross Domestic Product Chain-type Price Index (GDP-CPI). To compute the annual increase, the average of the GDP-CPI for four quarters shall be calculated by adding the four GDP-CPI quarters and dividing the sum by 4. The increase shall be rounded to the nearest 0.1 percent by rounding 0.05 percent and above to the next higher 0.1 percent and otherwise rounding to the next lower 0.1 percent. This percentage increase shall be applied to the amount of the annual funding cap from the previous funding year. If the yearly average GDP-CPI decreases or stays the same, the annual funding cap shall remain the same as the previous year.

(2) Public Notice. When the calculation of the yearly average GDP-CPI is determined, the Commission shall publish a Public Notice in the Federal Register within 60 days announcing any increase of the annual funding cap based on the rate of inflation.

(b) * * *

(c) Requests. Funds shall be available to fund discounts for applicants on a first-come-first-served basis, with requests accepted beginning on the first of July prior to each funding year. The Administrator shall maintain on the Administrator's website a running tally of the funds already committed for the existing funding year. The Administrator shall implement an initial filing period that treats all applicants filing within that period as if their applications were simultaneously received. The initial filing period shall begin on the date that the Administrator begins to receive applications for support, and shall conclude on a date to be determined by the Administrator. The Administrator may implement such additional filing periods as it deems necessary.

(d) Annual filing requirement. Applicants shall file new funding requests for each funding year no sooner than the July 1 prior to the start of that funding year. Applicants must use recurring services for which discounts have been committed by the Administrator within the funding year for which the discounts were sought. The deadline for implementation of non-recurring services will be September 30 following the close of the funding year. An applicant may request and receive from the Administrator an extension of the implementation deadline for non-recurring services if it satisfies one of the following criteria:

(e) * * *

(f) * * *

(g) * * *

* * * * *

10. Amend § 54.508 by revising subsections (a), (b), (c), and deleting subsection (d) to read as follows: