E-Rate Central Summary
of the
E-Rate 2.0 Modernization Order (FCC 14-99)

The FCC released the first E-rate modernization Order (FCC 14-99) July 23, 2014. We are referring to this as the "first" Order because we are expecting companion releases later this year, including:

1. A draft and subsequent final Eligible Services List for FY 2015;
2. Changes to the Form 470 and Form 471 (and maybe other forms);
3. A follow-up order related to the Further Notice of Proposed Rulemaking included with this first Order;
4. One or more possible "clarification" orders addressing questions raised by the first Order; and
5. A second E-rate modernization order focusing on Category 1 issues.

The major provisions of the first Order, most importantly designed to reorient the E-rate program to focus on broadband services, are summarized below.

Performance Goals and Measures:

Most generally, the Order sets forth the following three goals:

1. Ensuring affordable access to high-speed broadband sufficient to support digital learning in schools and robust connectivity for all libraries.
2. Maximizing the cost-effectiveness of spending for E-rate supported purchases.
3. Making the E-rate application process and other E-rate processes fast, simple, and efficient.

More specifically, the Order establishes an Internet connectivity goal for schools, consistent with the President's ConnectEd initiative, of at least 100 Mbps per 1,000 students in the short-term, and 1 Gbps per 1,000 students in the longer-term. The WAN connectivity goal for schools focuses on the "scalable capacity" of 10 Gbps per 1,000 students. The equivalent Internet connectivity goal for libraries is 100 Mbps for those serving fewer than 50,000 people, and 1 Gbps for those serving larger populations.

The Wireline Competition Bureau is directed to revise information collection from applicants and vendors to reflect data on these measures.

The Order sets an application processing "target" to have "USAC to aim to issue funding commitments or denials for all 'workable' funding requests by September 1st of each funding year," while explicitly acknowledging that this may not be possible during the FY 2015 transitional year.

Support of Internal Connections:

In a change of nomenclature, the old Priority 1 and Priority 2 designations are being replaced with "Category 1" and "Category 2" to make a clearer distinction and to establish separate funding targets for connectivity to buildings ("C1") and connectivity to devices within buildings ("C2").

Beginning with FY 2015, Category 2 will cover only broadband distribution services and equipment including: routers, switches, wireless access points, internal cabling, racks, wireless controller systems, firewall services, uninterruptable power supply, and related software. Managed Wi-Fi, caching, and maintenance will also be eligible, at least for the first two years. Previously eligible P2 services such as servers, telephone switches, and VoIP components will no longer be covered.

The FCC is targeting at least $1 billion per year in C2 discounts over the next five years. To allocate these funds, the FCC plans a two-year test of a per-school or per-library budget limitation capping the amount of funding any one applicant can receive (and replacing the existing 2-in-5 restriction). The budgets would work as follows:

1. Individual schools can receive C2 discounts on up to a total pre-discount budget amount of $150 per student over a five year period.
2. Individual libraries have a similar five-year pre-discount budget of $2.30 per square foot.
3. The minimum pre-discount budget (or "floor") for a small school or library is $9,200.
4. The maximum C2 discount will be 85%, not 90%. All other discounts levels (for both C1 and C2) remain the same.

According to FCC estimates, this budget-limited plan would provide adequate funding to assure Wi-Fi system build-outs and management over the five-year span for all applicants (assuming the two-year test mechanism is extended). While this may be true as a whole, timely funding for individual applicants is less predictable. With no P2 funding in FY 2013 (and presumably none in FY 2014), the demand for C2 funding in FY 2015 (and maybe FY 2016) is likely to exceed the targeted $1 billion in funding in that year. In that case, C2 funding will be limited to the higher discount level applicants, as in the past. The added twist under this Order is that if only partial funding is available at a given discount rate, a further threshold will be established based on applicants' actual student eligibility percentages.

Eliminating, Phasing-Out, or Narrowly Defining Support for "Legacy" Services:

The re-focusing of E-rate on broadband connectivity both to and within schools and libraries will mean — and to a large extent be funded by — a concurrent phase-out of support for non-broadband or "legacy" services. In particular, as of FY 2015:

1. E-rate support will be completely eliminated for:
    a. Paging

   b. Email
   c. Web hosting
   d. Voice mail
   e. Directory assistance
   f. Text messaging
   g. Custom calling features
   h. Direct inward dialing ("DID")
   i. 900/976 call blocking
   j. Inside wire maintenance plans
2. Support for voice telephone services will be phased out. Voice services are defined to include:
   a. Local and long distance phone service (often referred to as "POTS")
   b. 800 service
   c. Satellite telephone
   d. Centrex
   e. Wireless telephone service (including cellular voice services)
   f. Voice over IP
   g. Circuits dedicated to providing voice services
3. Support for individual cellular data plans will continue to be eligible, but only under narrowly defined conditions in which an applicant can show that a cellular data solution provides a more cost-effective solution for intra-building Wi-Fi coverage than a "robust wireless network."

The phase-out of voice services will be accomplished by reducing an applicant's discount rate for those services by 20 percentage points per year. Thus an applicant with a 90% discount rate will receive a 70% discount on voice services in FY 2015, 50% in FY 2016, 30% in FY 2017, 10% in FY 2018, and nothing in FY 2019. A 40% applicant will receive a 20% discount on voice services in FY 2015, and nothing in FY 2016.

From an applicant's perspective, the implementation of these changes will require a thorough review of its carriers' bills to identify and breakout (i.e., cost allocate) various charges. A typical wireline telephone bill, for example, may include: (a) numerous small ineligible charges; (b) non-voice data circuits, which are fully eligible; and (c) voice telephone charges, which must be filed for in a separate FRN at a lower discount rate. Similarly, a cellular bill is likely to include: (a) ineligible text messaging charges; (b) voice service charges (again requiring a separate FRN at a lower discount rate); and (c) data services that will remain fully eligible only if the applicant can demonstrate the cost-effectiveness of the service as an internal Wi-Fi system.

Maximizing Cost-Effectiveness:

In line with the FCC's goal to drive down the costs of broadband equipment and services, the Order does the following:

1. Provides greater transparency on pricing by standardizing Item 21 product and service descriptions and, more importantly, making the pricing on this information public.
2. Encourages consortia and bulk purchasing by:
    a. Speeding the review of consortium applications — a process already noticeably in effect for FY 2014.
    b. Creating a limited number of "preferred master contracts" for Category 2 equipment. Presumably, such contracts would be similar to the arrangement that the FCC announced last month to leverage GSA pricing. The interesting twist, if such contracts are available, is that applicant's would have to include those contract prices in their bid evaluations.
3. Reminds service providers that their bids and pricing must conform to the Lowest Corresponding Price ("LCP") requirements, and directs the FCC's Enforcement Bureau to devote additional resources to investigate and enforce LCP.

Simplifying the E-Rate Process:

Although some of the new provisions discussed above appear to complicate the E-rate process, the Order also contains a number of other provisions designed, at least in principle, to simplify applications, discount rate calculations, invoicing and disbursement, and other aspects.

Changes to the application process, beginning with FY 2015, include the following:

1. Multi-year contracts (up to five years) will be reviewed in depth only in the first year. Subsequent year applications will be reviewed using streamlined and expedited procedures.
2. Technology plans will not be required for either Category 1 or Category 2 services.
3. Lower-dollar purchases of "commercially-available business-class Internet services" will be exempt from competitive bidding rules (i.e., no Form 470s, bid assessments, etc.) Internet services covered by this exemption must provide speeds of at least 100 Mbps downstream and 10 Mbps upstream, and have an annual pre-discount cost of no more than $3,600 per school.
4. Electronic filings by applicants, and applicant notifications by USAC, will be required by FY 2017.

Discount rates for districts will be based on the district-wide percentage eligibility of students rather than on a weighted average of individual school discount rates. For many districts, this will result in either an increase or decrease in their overall discount rate to the nearest "matrix" discount rate. For example, a district with a current discount rate of 56% will most likely have a 60% discount in FY 2015, while a district currently at 54% will most likely fall to 50%. The district discount rate will apply to all funding requests, even if a service is only being provided to a subset of the schools. Consortium discount rates will still be based on the average of their members' discounts.

Other changes affecting discount rates include:

1. The definition of "rural" and "urban" will now be based on U.S. Census data. For an individual school, the rural/urban classification can be determined by its mailing address using the Census Bureau's American FactFinder. The rural/urban classification for a district with schools in each category will be determined by the location of the majority of its schools.
2. The discount rates for schools participating in the Community Eligibility Provision ("CEP") program will be calculated using the same multiplier (currently 1.6x) of direct certification percentages used for free meal reimbursements.
3. Household income surveys may still be used to identify eligible students, but discount rate extrapolations based on those surveys will no longer be permitted. This is bound to lower the discount rates of schools that have historically relied on the survey method.

Beginning with FY 2016, BEAR reimbursement payments will be made directly to applicants, and will no longer have to be funneled through the service providers (nor will the applicants be required to have the service providers approve their BEAR forms). Direct applicant BEAR payments will be made by electronic transfer (requiring applicants to provide USAC with appropriate bank account information).

Beginning with FY 2014, invoicing deadlines may be extended once upon request for 120 days. Requests for further extensions, under "extraordinary circumstances," may be granted only by the FCC. The objective of this change is to permit USAC to "de-obligate" unused funds at an earlier date.

Other changes designed to simplify the E-rate process, for either the applicants or the program administrators, include:

1. Creating a consultation and outreach program for Tribal schools and libraries.
2. Requiring all appeals — exclusive of requests for FCC rule waivers — to be made first to USAC.
3. Establishing specific targets for application reviews, commitment decisions, and funding disbursements.
4. Modernizing USAC's information technology systems, including the creation of "an online portal with pre-populated information for returning applicants and service providers."
5. Publishing "all non-confidential E-rate data in open, standardized, electronic formats."
6. Adopting "plain language" review correspondence.
7. Extending the document retention requirements from five to ten years.
8. Clarifying the right of auditors, investigators, and other persons appointed by local, state, and federal authorities to access applicant and service provider sites for inspections.

Finally, recognizing "the complexities associated with modernizing the E-rate program" as it pertains to the rules modifying the rules and other programmatic changes adopted in the Order, the FCC has delegated authority to the Wireline Competition Bureau "to make any further rule revisions as necessary to ensure the changes to the program adopted in this Report and Order are reflected in our rules. This includes correcting any conflicts between new and/or revised rules and existing rules as well as addressing any omissions or oversights."

Further Notice of Proposed Rulemaking:

Accompanying the Order is a Further Notice of Proposed Rulemaking ("FNPRM") seeking comment on future funding needs and on several other issues not fully addressed in the Order. FNPRM comments are due September 15th; reply comments are due September 30th. A subsequent order, based on this FNPRM, may expand or modify provisions of the Order discussed above for FY 2015 or later funding years.

The FNPRM includes almost 130 questions or requests for comments focusing on the following topics:

1. Meeting future E-rate funding needs.
2. Ensuring the efficiency of multi-year contracts.
3. Standardizing the collection of NSLP data.
4. Encouraging consortium participation.
5. Ensuring sufficient support for libraries.
