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Telecommunications Discounts for Schools and Libraries: The "E-Rate" Program and Controversies

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Telecommunications Discounts for Schools and Libraries: The "E-Rate" Program and Controversies

SUMMARY

Passage of the Telecommunications Act of 1996 (P.L. 104-104) codified the long standing policy commitment to ensure universal service in the provision of telecommunications services. The 1996 Act also expanded the concept to include, among other principles, that elementary schools and classrooms, and libraries should have access to telecommunications services for educational purposes at discounted rates. The Federal Communications Commission (FCC) was tasked with implementing the universal provisions of the Act and on May 7, 1997, adopted its order detailing its guidelines.

Included within that order was the establishment of the schools and libraries, or E-rate, program. Under this program telecommunications services, Internet access, and internal connections will be provided at discounts ranging from 20% to 90 % to eligible schools and libraries. The FCC established the Schools and Libraries Corporation (SLC), an independent, not-for-profit corporation to administer the program. As the result of a January 1, 1999 reorganization, however, the SLC became the Schools and Libraries Division of the Universal Service Administrative Company and ceased to exist as a separate corporate entity. The program receives no federal funds but is funded by mandatory contributions from interstate telecommunications service providers. Many of these providers have chosen to pass through universal service charges directly to consumers and earmark a universal service charge on subscribers' bills.

Although most support the concept, the FCC's implementation of the schools and libraries provisions of the 1996 Act has generated significant and diverse controversy. The decision by various telecommunications service providers to pass through and itemize universal service contributions on subscribers' bills has focused further attention on this issue. Concerns focus on : the administrative structure designed to implement the program; the scope and funding level of the program; and the potential for application fraud, waste and abuse.

Oversight of the program by the 105th Congress was intense, but no legislative measures were enacted. Legislation alternatives introduced in the 106th Congress ranged from those that sought to expand the program, eliminate the program, develop a new funding source, change its administrative structure or call for an in depth GAO study of the program; none of these measures were enacted. To date only one bill (H.R. 346) dealing with the use of unexpended program funds has been introduced in the 107th Congress.

In response to congressional concerns the FCC reduced the program's funding level and restructured the administrative aspects of the program. The May 27, 1999 decision by the FCC to increase the second year funding level for the program to its $2.25 billion cap prompted the 106th Congress to revisit the issues debated in the previous Congress. For the first two years of the program $3.7 billion has been committed. Despite Third year funding requests estimated at $4.72 billion, the FCC decided to maintain its $2.25 billion established ceiling, distributing $2.1 billion in funds. Funding requests for Year 4 are initially estimated at $5.2 billion.

MOST RECENT DEVELOPMENTS

FCC implementation of the schools and libraries, or E-rate program, has come under significant congressional scrutiny. A decision by major telecommunications service providers to place a line-item charge on subscribers' bills to cover universal service obligations, including those covered in this program, has given further impetus to this review.

In response to congressional concerns, expressed in the 105th Congress, the FCC modified the program's administrative structure and lowered the funding level for year one. However, based on application demand, the FCC, in a May 27, 1999 action, increased the second year funding level of the program to the program cap of $2.25 billion. Over the first two years of the program $3.7 billion has been disbursed. Funding requests for the third year of the program are estimated at $4.72 billion, however, the FCC has maintained its $2.25 billion ceiling for Year 3. As of December 1,2000, $2.1 billion has been committed for Year 3. The filing window for Year4 closed on January 18, 2001; an interim figure of $5.2 billion has been estimated for funding requests. Due to significant demand the FCC has issued a proposal, for comment, which would modify the funding priority for the internal connections portion of the program.

The FCC decision to significantly increase the second year funding level of the program generated some Congressional concern and a number of measures seeking to change the program were introduced in the 106th Congress. While one measure called for the elimination of the program another one sought to expand it. The other three measures focused on the establishment of an alternative funding source and/or administrative structure for the program. None of these measures were enacted in the 106th Congress. To date only one measure (H.R. 346) dealing with the use of unexpended program funds, has been introduced in the 107th Congress. However the Administration in its FY2002 budget proposal has called for the FCC to initiated a rulemaking to, among other things, modify the allocation of funding and expand the range of services covered under the program.

BACKGROUND AND ANALYSIS

Passage of the Telecommunications Act of 1996 (P.L.104-104) codified the long-standing commitment by U.S. policymakers to ensure universal service in the provision of telecommunications services. The universal service concept, as originally designed, called for the establishment of policies to ensure that local telephone service is available to all Americans by ensuring that rates for residential consumers as well as consumers in high cost areas were kept reasonable. Congress, through the 1996 Act, not only codified this concept, but also expanded the concept of universal service to include, among other principles, that elementary and secondary schools and classrooms, and libraries should have access to telecommunications services for educational purposes at discounted rates. (See Sections 254(b)(6) and 254(h)of the 1996 Telecommunications Act.)

Consistent with provisions contained in the 1996 Act the FCC, guided by the recommendations of a federal-state joint board, was assigned the responsibility for

implementing these universal service guidelines. On May 7,1997, the FCC adopted its order implementing the universal service provisions and principles set forth in the Act. Included within that order was the establishment of the schools and libraries, or E(education) - rate, program. Under this program telecommunications services, Internet access, and internal connections are to be provided at discounts ranging from 20% to 90 % to eligible schools and libraries. Therefore schools and libraries do not receive direct funding from the program but monies from the fund are used to reimburse the vendors who supply the services to the program's participants.

This issue brief does not attempt to explain the specifics of the E-rate program. It solely addresses the controversial issues surrounding the program's implementation and subsequent legislative measures introduced to address these issues. For additional information on the E-rate program focusing specifically on schools and educational issues, see CRS Report 98-604, *E-Rate for Schools: Background on Telecommunications Discounts Through the Universal Service Fund*, by James B. Stedman and Patricia Osorio-O'Dea. For background on technology in elementary and secondary education , see CRS Report 96-178, *Information Technology and Elementary Education: Current Status and Federal Support*, by James B. Stedman. An additional issue, concern that minors may gain access to "inappropriate" material through the Internet has also had an impact on the E-rate program. This issue and its subsequent legislative initiatives goes beyond the scope of this issue brief, but is addressed in CRS Report RS20036, *Internet-Protecting Children from Unsuitable Material and Sexual Predators: Overview and Pending Legislation,* by Marcia Smith.

Although most policymakers support the universal service concept, the FCC's implementation of the schools and libraries provisions of the 1996 Act has generated significant controversy. The decision by various telecommunications service providers to pass through and itemize universal service contributions on subscribers' bills has focused further attention on this issue. Oversight of the schools and libraries program by the 105th Congress became intense with congressional comments ranging from those who called for the abolishment of the program, to those who supported of the program but felt it needed major revisions, to those who continued to support the program as funded and designed. Concerns regarding the schools and libraries program focus on: the administrative structure designed to implement the program; the scope and funding level of the program; and the potential for fraud, waste, and abuse.

Administrative Structure

The FCC established the Schools and Libraries Corporation (SLC), an independent not-for- profit corporation, to administer the universal service program for schools and libraries. Since its inception, however, the SLC became the focus of a wide range of concerns which eventually led to the reorganization of the administrative structure of the E-rate program. (See Restructuring — from SLC to SLD, below.) Some questioned the need for the SLC and expressed concern that it only adds "new levels of bureaucracy" and siphons away money that could be used to fund universal service objectives. Concerns have also been expressed over the size of the SLC's first year operating budget ($18.8 million) as well as employee compensation levels. Of greater significance was the debate over whether the FCC had exceeded its authority when it directed the establishment of the corporation.

The General Accounting Office (GAO) in response to a November 1997 request from Senator Stevens, reviewed the FCC's action establishing the SLC. The GAO concluded, in its February 10, 1998 response, that the FCC had exceeded its authority when it directed the creation of the SLC, in violation of the Government Corporation Control Act (P.L. 97-258). FCC Chairman Kennard disagreed with the GAO's conclusion and stated that the FCC was within its authority, based on its general authority under Section 4(i) of the Communications Act, to establish this corporation. However, continued controversy over the legality of and the need for the SLC led to congressional action to modify the administrative structure of the E-rate program.

An amendment added to the Senate's 1998 supplemental appropriations bill (S. 1768), by Senator Stevens, addressed the administration of the schools and libraries and rural health care portion of the universal service fund. This amendment, which was approved by the Senate by voice vote on March 24, 1998, would have required the FCC to abolish the SLC and its rural health care counterpart, consolidate them into a single entity, and cap the compensation given to its officers and employees. The FCC was required to submit to Congress by May 8, 1998, a report detailing the revised structure for this entity, and additional information on the contributions to, and requests for funding from the schools and libraries program. These provisions were not included in the text of the final bill (H.R. 3579), which was signed into law on May 1, 1998 (P.L. 105-174). However, the conference committee's "joint explanatory statement" did make mention of these provisions and stated that "while the conference agreement does not include" the provisions relating to universal service contained in S. 1768 the conferees "expect that the FCC will comply with the reporting requirements in the Senate bill, respond to inquiries regarding the universal service contribution mechanisms, access charges, and cost data, and propose a new structure for the implementation of the universal service programs." The joint statement also concurs with the provisions relating to a compensation cap for employees administering the program. The FCC complied with the provisions contained in S. 1768 and submitted its report to Congress on May 8, 1998.

Restructuring — from SLC to SLD. In its May 8 Report to Congress (FCC 98-85), and a subsequent action of June 12, 1998 (CC Docket No. 96-45), the FCC: proposed the elimination of the SLC as a separate entity; lowered the compensation level of officers and employees of the SLC; and requested that Congress grant specific statutory authority for the newly proposed restructuring. The FCC requested that the administrative entities affected by this proposal submit a reorganization plan to implement these changes for FCC approval.

The restructuring plan was submitted to the FCC on July 1, 1998 and after receiving public comment was approved, with modifications, by the FCC on November 19, 1998. The approved plan, which went into effect on January 1, 1999, calls for the administration of all forms of federal universal service support to be consolidated in a single entity, the Universal Service Administrative Company (USAC). The USAC, the entity that among other duties currently administers the high cost and low income portions of the universal service program, was to become the permanent, sole administrator of all universal service programs, subject to FCC determination, after one year, that the USAC is administering support in an "efficient, effective, and competitively neutral manner." The SLC would become the Schools and Libraries Division (SLD), one of three divisions within the USAC. The USAC CEO would manage all three divisions. The USAC will continue to function as a subsidiary of the National Exchange Carrier Association (NECA), and the FCC will review, after one year, whether the

USAC should be divested from the NECA. This reorganization plan, became effective as of January 1, 1999 and the independent SLC ceased to exist. (A copy of the approved reorganization plan can be found on the FCC's web page at [http://www.fcc.gov/ccb/universal_service/usacjuly.pdf])

As a result of the reorganization a single entity, the USAC, is now responsible for administering all the telecommunications universal service programs for the FCC, including the schools and libraries or E-rate program. The USAC, a not-for-profit subsidiary of the National Exchange Carrier Association, is governed by a Board of Directors composed of a broad range of industry and non-industry interests. Committees of the USAC Board govern each division and each committee of the USAC Board oversees the budget of its respective Division and reports to the overall USAC Board. The USAC Board has the authority to review any action taken by a committee. The SLC no longer exists and has become one of three divisions of the USAC known as the Schools and Libraries Division (SLD). Although no longer a separate entity , the SLD essentially carries out the same functions as the former SLC.

While continuing to uphold its legal right to create a separate entity to administer the schools and libraries fund, a position contrary to a February 10, 1998 GAO opinion, the FCC has requested that the Congress provide specific statutory authority for the restructuring to eliminate any question concerning the USAC's legal status and authority.

The FCC also directed that effective July 1, 1998 the level of compensation be lowered for the officers and employees of the SLC. Compensation cannot exceed the rate of basic pay for level I of the Federal Executive schedule which is currently $151, 800 a year. (The May 8, 1998 Report to Congress, and the subsequent June 12, 1998 order are available at the FCC's web site at [http://www.fcc.gov].)

Scope and Funding

Although federally mandated, the E-rate program, as designed by Congress, is funded by telecommunications service providers. All interstate telecommunications providers, as defined by the FCC, are required to contribute to the program. Contributions are based on a percentage of both interstate and international revenues. This percentage or "contribution factor" is calculated by the FCC's Common Carrier Bureau on a quarterly basis and varies depending on the anticipated funding needs for the program. Many telecommunications service providers have chosen to pass through these costs directly to their subscribers ultimately making consumers of telecommunications services bare the costs of the program.

Congressional concerns regarding funding rest on both the scope of the services included in the program and the funding level established to meet the program's needs. The $2.25 billion per year funding ceiling established by the FCC to implement the schools and libraries discount and the range of services included in the program have generated significant concern.

While most support the basic concept of the program, many have questioned the need for a multi-billion dollar funding level and have expressed concern that the range of services included in the program goes beyond congressional intent. Critics feel that the program, as

implemented by the FCC, is too extensive and will result in the funding of "gold plated" systems. Coverage of sophisticated equipment such as routers, hubs, and network file servers, as well as the inclusion of internal connections (i.e., wiring to connect classrooms within a school), has been criticized. Opponents claim that the extensive scope of the program goes beyond the program's intent and has resulted in an unnecessarily high funding level. Those critical of the program as implemented support a more modest approach. Opinions have also been expressed that the FCC's time frame for accomplishing the program is too short and overly ambitious and should be lengthened, thereby reducing the amount of funding needed yearly.

On the other hand, many supporters of the E-rate program feel that the range of services covered and the funding level should remain or, if anything, be expanded. A decrease in funding levels or scope is viewed as a retreat to the commitment Congress made to schools and children. Furthermore, the $2.25 billion funding ceiling is not considered unreasonable, they state, given the revenue stream of the industry. The inclusion of internal wiring they note is consistent with the intent of Congress and critical to the program's success. They cite specific reference in the universal service provisions to access by "school classrooms" to advanced telecommunications services to bolster their claim. Some also support expansion of the program to include funding for time of use on the Internet. This they feel is particularly critical for economically disadvantaged schools since connection is of little value, they claim, if there is no funding for usage time. Proposals to expand the organizations covered by the program have also been discussed.

Concern has also been expressed that the FCC has given priority to the schools and libraries facet of the program at the expense of other, more primary aspects of the universal service mandate, such as the "high cost" fund. The primary cornerstone of universal service has been to ensure that telephone rates remain reasonable by assisting telephone providers in high cost, typically rural, areas. The emphasis on the schools and libraries some claim, has skewed the intent of Congress and diverted attention away from high cost concerns. The "high cost" program could suffer, they state, if contributors are forced to shift resources to the E-rate program. Some favor suspending the E-rate program and addressing all aspects of universal service simultaneously in an integrated proceeding.

FCC Funding Modifications. Concerns over the direction the FCC is taking in implementing and funding the universal service provisions of the 1996 Act in general, and the schools and libraries program in particular, prompted the FCC to reconsider its actions regarding universal service support for schools and libraries. The FCC released a public notice (CC Docket No. 96-45) on May 13, 1998, seeking comment on a proposal to phase-in funding for the schools and libraries portion of the Universal Service Fund. After examination of the comments, the FCC adopted an order on June 12, 1998, that modified funding aspects of the E- rate program. Among other actions the FCC adjusted downward the amounts that would be collected to fund the E-rate program through June 30, 1999.

More specifically the FCC, in its June 12, 1998 order (CC docket No. 96-45), made the following modifications to the funding level and disbursement rules of the E- rate program:

- revised the funding year from a calendar year (January 1 - December 31) to a fiscal year (July 1 - June 30) cycle. This is accomplished by extending the first year funding cycle by six months through June 30, 1999. This

modification, according to the FCC, will synchronize the program with the budgetary and planning cycles of most schools and libraries as well as align changes in universal service contribution levels with local exchange carrier annual access tariff filing schedules.

- froze the amount of funding at current rates. Program administrators were directed to collect and disperse no more than $325 million per quarter for the third and fourth quarters of 1998 and the first and second quarters of 1999. Although the cap for the program remains unchanged, at $2.25 billion, when added to the $625 million collected in the first half of 1998, the available funding for the first 18 months of the program will total no more than $1.925 billion.
- revised disbursement rules to insure that the most disadvantaged schools and libraries get priority for support. Based on a preliminary review of pending applications demand for discounts is estimated at $2.02 billion, an amount exceeding the ceiling of $1.925 billion for disbursements. Since funding will be less than demand, the FCC has adopted rules to prioritize distributions. When demand exceeds the level of funding all eligible schools and libraries will receive support for recurring services such as telecommunications services and Internet access, but only the most economically disadvantaged applicants will receive support for internal connections.
- changed the second year application cycle to begin no later than October 1, 1998, rather than July 1, 1998. Note, the application window for the second funding year (July 1, 1999 - June 30, 2000) was delayed. It opened on December 1, 1998 and closed on April 6, 1999.

The FCC's May 27, 1999 decision to fully fund the second year of program at the $2.25 billion cap generated significant controversy. In a 3-2 split decision the FCC Commissioners decided that, given the level of demand as determined by a review of pending applications, the second year of the program should be funded at its maximum level. This is in contrast to the annual funding level of $1.3 billion for the first year of the program. This significant increase reignited the debate which occurred in the 105th Congress regarding the need for, the administration of and the funding source and level of, the program. Despite the $4.72 billion estimated demand for the third year of the program, the FCC has maintained its $2.25 billion funding cap for Year 3.

Restructuring and Funding Alternatives. Changes in the administrative structure of the program, while welcomed by many, have not satisfied a number of critics. An alternative administrative structure was offered in legislative initiatives (H.R. 1746 and S. 1004) introduced in the 106th Congress by Representative Tauzin and Senator Burns. These bills, (which also contain provisions addressing funding) called for the elimination of the E-rate program and the transfer of authority for the program from the FCC. The E-rate program would be replaced by a Telecommunications Technology Trust Fund and would be designed as a state block grant program. The Department of Commerce's National Telecommunications and Information Administration (NTIA) would become its administrative entity. (See **Congressional Activity, Action in the 106th Congress**, for a detailed discussion of the specific provision contained in and the status of these measures.)

This approach, according to its supporters, would alleviate the present legal questions regarding FCC authority to establish entities and would give the program to an agency

familiar with the process of administrating grant programs. Supporters of the presently designed E-rate program have expressed concerns that this approach would remove the goals of the schools and libraries program from the universal service concept. Furthermore, they claim, it would have a severe disruptive impact on the existing program, would result in a more burdensome application process, and would make the program dependent on appropriated funds.

Debate over funding issues has also focused on what the appropriate funding mechanism for the E-rate program should be. One suggested source for funding for the E-rate program is the revenues collected from the 3% federal telephone excise tax. The federal telephone excise tax, which is currently assessed on consumers' local and long distance telephone service, generates approximately $5 billion in yearly revenues. The revenue, while collected from consumers by telephone companies, is forwarded to the U.S. Treasury and added to general revenues. Three measures, H.R. 727, S. 1004, and H.R. 1746 to use revenues generated from that tax to address the funding issue were introduced in the 106th Congress. (See **Congressional Activity, Action in the 106th Congress**, for a detailed discussion of the specific provisions contained in and the status of these measures.)

This approach, sponsors claim, would eliminate concerns over the legality of the present funding mechanism and would result in funding for the program without adding new upward pressures on consumers' telephone bills. Furthermore, sponsors state, expenditures for the program would be made explicit through a capped tax that is currently listed on telephone bills. While interest has been expressed in examining this proposal, a number of questions and concerns regarding the funding aspects of the measures remain. Included among these are: concern that it would, at a minimum, cause disruption of a presently functioning program; concern that the funding source for the program is not permanent; questions whether money generated by taxes can be used to support private or parochial schools; and the potential negative impact of use of general funds on other government outlays.

Need for the Program. Despite the changes made to funding levels and administrative structure a more fundamental question rests with the debate over whether the E-rate program, as implemented, is needed. Those who question the need for such a program claim that voluntary private sector initiatives such as "Net Days" as well as other federal programs alleviate the need for the E-rate program as designed. Some also question whether the alleged benefits that such access to technology has on education can be substantiated. However, supporters of the E-rate program cite its high level of demand (37,000 applications and an estimated funding request of $5.8 billion for Year 4) as proof that existing federal programs and private sector initiatives are not meeting the needs of schools and libraries. Citing statistics contained in a recently released Commerce Department study, *Falling Through the Net: Toward Digital Inclusion,* that show a decreasing but significant disparity in access to computers and online services by race and income, supporters also claim that this program is needed to help bridge the divide between information "haves and have nots" and ensure access to communities that may otherwise be left behind. Access to computers and on line services is vital, they claim, to ensure that the upcoming generation is prepared to fill the growing number of computer-related jobs. (For background on technology in education see CRS Report 96-178.)

Some question whether the E-rate program as designed duplicates or overlaps existing federal programs. In an attempt to address this concern then House Commerce Committee

Chairman Bliley (106th Congress) and House Education Committee Chairman Goodling (106th Congress) asked the General Accounting Office (GAO) to undertake an examination of federal programs, previously identified by the GAO at the request of Senator Stevens, that may in some way be duplicative. The report was directed to examine a number of areas including the potential for duplication and potential problems associated with fraud, waste, and abuse. The GAO report (*Telecommunications Technology: Federal Funding for Schools and Libraries*), which was released in August 1999, identified 35 federal programs that could be used as a source of support for telecommunications and information technology by libraries or elementary or secondary schools in fiscal year 1998; ten programs specifically targeted technology while the remaining 25 included technology as a possible use of funds. Based on the GAO's review it found that there are "similarities" among the programs, but the GAO "... did not identify instances where two programs were designed to provide identical services to identical recipients." Furthermore, the GAO did not "identify information that indicates that fraud, waste, and abuse are systemic or widespread problems" but did find instances of such problems with individual guarantees. The GAO noted that action was taken against these individual guarantees and to prevent reoccurrence of such problems. The GAO did not examine the implementation of each program or conduct its own audits but relied on interviews, agency program documents, and reports to reach its conclusions.

Eligible Services and Application Integrity

Directly related to the funding issue are concerns over the potential for possible fraud, waste, or abuse of the program. The ability to ensure that only eligible services are funded and that funding is dispersed at the proper level of discount has been questioned.

One concern has focused on possible confusion by applicants over the range of services considered eligible for the program and the fear expressed by some that pending applications contain requests for ineligible services. Confusion over what services and related expenses are covered by the program prompted the FCC to issue a public notice clarifying this issue. The FCC, in a June 11, 1998 order (CC Docket No. 96-45), stated that services eligible for discounts include "...All telecommunications services, Internet access, and internal connections provided by telecommunications carriers, as well as Internet access and internal connects provided by non-telecommunications carriers." The FCC also clarified what services *are not* eligible for discounts. Services not eligible for discounts include: purchases of personal computers, fax machines, modems, telephone handsets, as well as teacher training, and expenses related to the installation of wiring (such as removing asbestos, tearing down walls, repairing carpets, or repainting). The FCC reiterated that schools and libraries are required to select "the most cost effective bid" when examining competing bids and that "price should be the primary factor." However other relevant factors that can be considered include: "prior experience; personnel qualifications, including technical excellence; management capability, including schedule compliance; and environmental objectives."

Concern that only eligible services be funded also brought up issues relating to application integrity. Critics of the program, as well as some supporters, questioned whether the necessary mechanisms are in place to ensure that only eligible services receive funding and that such funding is given at the proper level of discount. Although the FCC's clarification order has helped to resolve confusion over eligibility criteria, critics said it had come too late for the 30,000 application that had already been filed. Concern was also

expressed that the FCC's decision to allow other "relevant factors" to be considered in the selection process, not solely cost, could result in inflated costs for the program as the lowest bidder may not necessarily be chosen. These other factors are ambiguous at best, critics claim, and could be used to manipulate the selection process.

Concerns about fraud and abuse are shared by both critics and supporters of the program. Some critics of the program claim that the program as devised is fraught with problems and at a minimum should be suspended until additional safeguards are in place. Supporters also want to ensure integrity of the program since the funding of ineligible services or unreasonable administrative costs will only decrease available funding to meet the program's goals. Many supporters, however, do not view this as a major problem and feel that the program as devised is basically sound. They point to the willingness of the SLD and the FCC to take further steps to ensure program integrity such as the establishment of a program integrity hotline (888-203-8100) to report potential instances of waste, fraud, or abuse of program rules as well as the creation of a Year 3 Task Force to evaluate and make recommendations to improve the program. (See: [http://www.ala.org/oitp/year3.html] for an executive summary of the task force's recommendations.)

In an attempt to ensure the integrity of the E-rate program and assess the ability to properly audit applications Senator McCain, requested that the GAO initiate a formal investigation and audit of the Schools and Libraries program. Results of the GAO assessment were released at a Senate Commerce Committee hearing held on July 16, 1998. Based on its review the GAO recommended that prior to making any funding commitments, the SLC should: conduct a statistically valid random sample of applications to assess the effectiveness of its procedures, and if needed take corrective action; finalize procedures, automated systems, and internal controls for the post-commitment phase of the program's funding cycle; obtain a report from its independent auditor verifying that the SLC has developed an appropriate set of internal controls to mitigate against waste, fraud, and abuse; and conduct a review of the technology plans of applications identified as "high risk" to determine whether applicants have the resources to effectively use the services requested and are in compliance with eligibility criteria.

The E-rate program administrator announced that it would comply with all of the GAO's recommendations prior to the commitment of any funds and incorporate other recommendations based on an FCC-required independent audit of its procedures conducted by an independent accounting firm. A follow-up report, conducted by the GAO at the request of Sen. McCain, assessing the program's progress in implementing the GAO's recommendations was released in March 1999 (*Schools and Libraries Program: Actions Taken to Improve Operational Procedures Prior to Committing Funds)*. According to the GAO assessment the SLD "...has taken actions to implement the key recommendations that we believe are needed to be completed prior to issuing any funding commitment letters to applicants." However, the GAO did express concern over the adequacy of the procedures used to ensure applicants' self certified discount levels are accurate. It also noted that "... the program still faces major challenges as it moves into new operational areas" and recommended that "... close oversight by the FCC will be especially important..." In addition the GAO noted that the FCC has yet to implement the earlier GAO recommendation "... to develop adequate goals, performance targets, and measures for the program." The president of the SLD stated that based on the experienced gained after the first year of the program and in response to the FCC Chairman's direction the SLD " ...will implement new, tighter

procedures for evaluating discounts." Furthermore, the FCC, according to the GAO report, acknowledged the importance of and intent to address the recommendation to establish adequate performance goals and measures for the program, but did not indicate a time frame for such action.

The GAO continued to express concerns regarding the administration of the program in its most recent report, *Schools and Libraries Program: Application and Invoice Review Procedures Need Strengthening,* issued in December 2000. According to the GAO their audit (which covered the first 2 years of the program) identified "millions of dollars of funds incorrectly committed to ineligible products and services" and despite the extension of deadlines for eligible applicants and vendors "a significant amount" of eligible committed funds have yet to be paid out. The GAO report cited a total of $1.3 billion (35 percent) of funds that while committed, were not dispersed as of the end of August 2000. The GAO also cited "weaknesses in the SLD's e-rate application review process [which] resulted in commitments of funds for ineligible products and services." According to the FCC/USAC only 10 percent of the commitments for GAO-identified ineligible services have been dispersed and that any that have been dispersed will be recovered. While the reasons why committed funds remain unused are likely to vary with each applicant the FCC/USAC "will undertake an analysis of the factors leading to funds being committed to applicants, but not ultimately disbursed." While acknowledging that the SLD has taken steps to alleviate some of these problems the GAO has made a number of suggestions for corrective procedures and recommended that they be enacted prior to the award and distribution of funds for Year 4 of the program. According to the GAO report the FCC and the USAC, after reviewing the draft of the report, have begun to implement, and in some cases have already completed action on, the recommendations.

Program Status

The first year funding cycle of the program(January 1998 through June 1999) has been completed. According to the SLD $1.66 billion of funds were committed to 25,785 applicants. (The $220 million difference between the amount committed and the authorized $1.925 billion includes reserves needed in case of successful appeals of rejections or pending reconsiderations as well as $45 million in administrative costs covering the first 20 months of the program.) Of total funds allocated 54% ($897 million) were committed for internal connection subsidies, 40% ($661.2 million)for telecommunications services, and 6% ($101.8 million) for Internet access. Funding received for the first year cycle is to be spent through September 30, 1999. Schools and mixed consortia (schools and libraries) received approximately 96% of the allocated funding with library and library consortium applicants receiving the remaining 4%. (For more detailed statistics on the breakdown of funding, including data by state, see the program's web site [http://www.sl.universalservice.org].)

The application period, or window, for the second year of the program covering July 1, 1999, through June 30, 2000, closed on April 6, 1999. Based on estimated demand the FCC, in a split decision, decided to fully fund Year 2 of the program at $2.25 billion. According to program administrators more than $1.93 billion in funding has been committed to 31,127 applicants and all qualifying requests filed during the application window were filled. Administrative expenses of $31 million were incurred. Additional funds have also been set aside to cover possible successful appeals of funding rejections.

The filing window for the third year of the program, covering July 1, 2000 through June 30, 2001, closed on January 19, 2000. According to the SLD more than 36,000 applicants, of which 60 percent are represented by the neediest schools and libraries, requested an estimated $4.72 billion in funding. Although the funding requests were more than double the existing yearly funding cap of $2.25 billion, the FCC maintained that cap for Year 3 of the program. As of December 1, 2000, $2.1 billion of funds have been committed to 26,276 applicants completing the processing of funding requests filed within the Year 3 filing window.

The Year 4 filing window, covering July 1, 2001 through June 30, 2002, closed on January 18, 2001. According to the SLD demand, based on 37,188 applications received during the open filing window, is estimated at $5.2 billion. However, the following factors are cited which may reduce the eligible funds needed from this most recent estimate: as yet undiscovered duplicate requests will be eliminated; and further examination will result in the removal of applications which are ineligible.

The FCC has initiated a proposed rulemaking to seek comments on a proposal to revise its method of distributing e-rate funds under certain circumstances. Under the proposal, when there is insufficient funding to fulfill all requests for internal connections, those entities who did not receive funding commitments for internal connections for the previous year would be given priority, in order of discount level, starting with Year 4. Funding for telecommunications services and Internet access would not be effected by this proposal. The FCC is also seeking comment on proposed administrative rules to provide additional time for recipients to implement contracts or agreements with service providers for non-recurring services. Comments are due May 23, 2001; replies May 30, 2001.(For more detailed information on this proposal see: *Federal Register*, Vol.66, No.89, May 8, 2001, pp. 23204-8.)

Congressional Activity -- 106th Congress

The decision by the FCC to significantly increase the funding level of Year 2 of the E-rate program prompted Congress to revisit the program. Legislation alternatives introduced in the 106th Congress that address the program included those that: sought to expand the program; sought its elimination; developed a new funding source; changed its administrative structure; or called for an in depth GAO study of the program. None of these measures were enacted.

S. 2229 and its companion measure H.R. 3897 sought to increase technology funding and contain among its provisions those to expand the E-rate program. Title III of these measures amends the 1934 Communications Act to extend e-rate eligibility beyond schools, libraries, and rural health care providers to include Head Start agencies and organizations that receive federal funds to provide job training services. Funding for the expansion of the program was not addressed and presumably would be covered under the existing e-rate program funding mechanism. No action was taken on these measures.

H.R. 692, introduced by Rep. Tancredo sought to terminate the E-rate program. This was largely accomplished by removing those universal service provisions contained in the 1996 Telecommunications Act (P.L. 104-104), and subsequently incorporated as Section 254 of the Communications Act of 1934, which provide for discounts for schools and libraries for

telecommunications services. The E-rate program is not needed according to the bill's supporters because of existing Department of Education funding. H.R. 692 was referred to the House Committee on Commerce where no further action was taken.

Three measures (H.R. 727, H.R. 1746, S. 1004) addressed funding aspects of the program. All three bills called for a new funding source for the program, the revenues collected from the 3% federal telephone excise tax. (For information on the unsuccessful attempt in the 106th Congress to repeal the telephone excise tax see CRS Report RS20119, *Telephone Excise Tax*, by Louis Talley.) The federal telephone excise tax, which is currently assessed on consumers' local and long distance telephone service, generates approximately $5 billion in yearly revenues. The revenue, while collected from consumers by telephone companies, is forwarded to the U.S. Treasury and added to general revenues. H.R. 727, a measure introduced on February 11,1999, by Representative Klink, called for all facets of federal universal service support, including the E-rate program, to be funded by the revenues collected from the federal telephone excise tax. A Telecommunications Trust Fund would be established from the collected revenue and funds would be made available for FY1999 and each of the 5 succeeding fiscal years. Funds were allowed to be made available on a school year versus a fiscal year basis. The present funding mechanism was to be terminated and any remaining funds collected under that mechanism distributed by the FCC. H.R. 727 was referred to both the Committee on Commerce and the Committee on Ways and Means. The measure was subsequently referred to the Subcommittee on Telecommunications. No further action was taken on these three measures

The two other measures (S. 1004 and H.R. 1746) introduced by Senator Burns and Representative Tauzin, respectively, also included provisions that called for federal telephone excise tax revenues to fund the E-rate program. However, both bills proposed to use only part of the revenues generated by the existing 3% tax as a funding source and use that revenue for funding the E-rate program. The two bills called for one third of the revenue collected to be designated for the funding of the E-rate program; the remaining two thirds of the tax would be repealed. The funding level was to be authorized for approximately a 5 year period (January 1, 1999 to October 1, 2004)with the first year funding level capped at $1.7 billion. Appropriations for the following 4 years were to be "such funds as necessary" limited to amounts collected by the tax. Effective fiscal year 2005, the 1% tax was to have been eliminated and up to $500 million a year appropriated from the Treasury to fund the program.

S. 1004 and H.R. 1746 also contained provisions that would have restructured the administration of the program. Oversight of the program would have been removed from the FCC and given to the Department of Commerce's National Telecommunications and Information Administration (NTIA). The E-rate program would have been replaced by a Telecommunications Technology Trust Fund administered by the NTIA. The program would have been a state block grant program, authorized for 5 years, that would have award grants based on state plans to assist in acquiring telecommunications and related services for elementary and secondary schools and libraries for educational purposes. The Commerce Department was to have been given authority to determine what services would be covered by the grants. S. 1004 was referred to the Senate Finance Committee. H.R. 1746 was referred to the Committee on Commerce, and House Ways and Means. Hearings were held on the measure by the House Telecommunications Subcommittee in September 1999 but no further action was taken on either measure.

107th Congress and Administration Activity

To date only one measure, H.R. 346, specific to the e-rate program has been introduced in the 107th Congress. The "Children's Access to Technology Act", introduced by Rep. Gene Green, addresses the use of unexpended program funds. This measure proposes to amend the 1934 Communications Act to require, with limitations, the disbursement of unexpended program funds. Under this bill if, at the conclusion of any program year, any unexpended funds, that is those funds which have been authorized for eligible services but have not been distributed, shall be made available to schools serving eligible school districts during the succeeding year. The total amount of funds made available shall not exceed $1 million for any program year and the amount made available for any individual school for any program year is capped at $25,000. Services that qualify for these funds are expanded beyond those currently eligible under the program to include "information services including devices necessary to access and use such services." Funding is to be distributed "by a system of random selection" to schools deemed eligible by the FCC. H.R. 346 was referred to the House Committee on Energy and Commerce and was subsequently referred to the Subcommittee on Telecommunications and the Internet.

The Bush Administration's initial proposal to combine the E-rate program with other technology based programs within the Department of Education has generated Congressional concern. Under the proposal, briefly outlined in President Bush's education reform proposal, *No Child Left Behind*, the E-rate program would be consolidated with other education technology grant programs. The E-rate program would become a block grant program removed from the FCC's jurisdiction, and placed under the jurisdiction of the Department of Education. Since then, however, the Administration seems to be reevaluating the proposal. According to comments made by Education Secretary Paige, at March 7, 2001 hearing, held by the House Education and the Workforce Committee, "Our current thinking is that the e-rate will not be consolidated into other technology programs."

However, contained in the Administration's FY2002 Budget, are provisions directing the FCC to complete a rulemaking by September 30, 2002, to revise the E-rate program. The FCC is directed to look into: allocating funds "using a need-based formula" (above present rules which give some priority based on students eligible for school based lunches); and redefining eligible services to include "additional services that promote effective use of telecommunications and information, such as teacher training and software." The FCC is also required to institute performance measures to assess how well funds were used by schools and libraries to increase student achievement. Supporters of the program including selected members of Congress, such as Senator Rockefeller, and the American Library Association have expressed concern about this proposal. The two main concerns are that: expanding the program to cover nontelecommunications activities such as software and teacher training could leave the program vulnerable to law suits and lead to the destruction of the program; and the proposal moves the program towards a formula grant approach.

Relevant Laws

P.L. 104-104 provides for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and

information technologies and services to all Americans by opening up all telecommunications markets to competition; the measure also contains provisions for other purposes.

P.L. 105-119. The 1998 appropriations legislation for the Departments of Commerce, Justice, and State. Contains provisions that require the FCC to undertake a review of the implementation of the provisions in the 1996 Telecommunications Act pertaining to universal service and to submit a report to Congress no later than April 10, 1998.

P.L. 105-174. Emergency supplemental appropriations for the fiscal year ending September 30, 1998. Contains within the conference committee's "joint explanatory statement" language that the conferees "expect that the FCC will comply with reporting requirements" contained in S. 1768, regarding universal service.

106th Congress Legislation

H.R. 692 (Tancredo)
A bill to terminate the E-rate program of the Federal Communications Commission that requires providers of telecommunications and information services to provide such services for schools and libraries at a discounted rate. Introduced Feb. 10, 1999; referred to Committee on Commerce.

H.R. 727 (Klink)
A bill to amend the Communications Act of 1934 to provide for explicit and stable funding for Federal support of universal telecommunications services through the creation of a Telecommunications Trust Fund. Introduced Feb. 11, 1999; referred to Committees on Commerce and on Ways and Means. Referred to Telecommunications Subcommittee Mar. 1, 1999.

H.R. 1746 (Tauzin)
A bill to amend the Communications Act of 1934 to reduce telephone rates, provide advanced telecommunications services to schools, libraries, and certain health care facilities, and for other purposes. Introduced May 11, 1999; referred to Committees on Commerce and on Ways and Means. Hearings held Sept. 30, 1999, by Telecommunications Subcommittee.

H.R. 2677 (Rivers)
A bill to amend the Communications Act of 1934 to require telephone carriers to completely and accurately itemize charges and taxes collected with telephone bills. Introduced Aug. 2, 1999; referred to Committee on Commerce.

H.R. 3897 (Reyes)
A bill to provide for digital empowerment, and for other purposes. Introduced Mar. 9, 2000; referred to Committees on Education and the Workforce, Commerce, Banking and Financial Services, and Ways and Means.

S. 1004 (Burns)
A bill to amend the Communications Act of 1934 to reduce telephone rates, provide advanced telecommunications services to schools, libraries, and certain health care facilities, and for other purposes. Introduced May 11, 1999; referred to Committee on Finance.

S. 1217 (Gregg)

An original bill making appropriations for the Departments of Commerce, Justice, and State, the Judiciary, and related agencies for the fiscal year ending Sept. 30, 2000, and for other purposes. This measure contains a provision requiring the GAO to do an extensive review of E- rate program. Introduced June 14, 1999. Reported to Senate from Committee on Appropriations June 14, 1999 (S.Rept. 106-76). Passed Senate, by voice vote, July 22, 1999.

S. 2229 (Mikulski)

A bill to provide for digital empowerment, and for other purposes. Introduced Mar. 9, 2000; referred to Finance Committee.

LEGISLATION

H.R. 346 (Green, Gene)

A bill to amend the Communications Act of 1934 to provide for the use of unexpended universal service funds in low-income schools, and for other purposes. Introduced Jan. 31, 2001; referred to House Committee on Energy and Commerce. Referred to the Subcommittee on Telecommunications and the Internet Feb. 14, 2001.

FOR ADDITIONAL READING

Benton Foundation. Communications Policy and Practice Program. *The E-Rate in America: A Tale of Four Cities.* February 2000. Washington D.C. Available at the Benton Foundation web site: [http://www.benton.org/e-rate/e-rate.4cities.pdf]

Education and Library Networks Coalition. *E-Rate: Keeping the Promise to Connect Kids and Communities to the Future.* July 2000. Available at the EdLiNC web site: [http://edlinc.org/pubs/eratereport2.html]

Federal Communications Commission education web site: [http://www.fcc.gov/learnnet]

Heritage Foundation. *Do Computers in the Classroom Boost Academic Achievement?* June 14, 2000. Washington D.C. Available at the Heritage Foundation web site: [http://www.heritage.org]

Schools and Libraries Division web site: [http://www.sl.universalservice.org]

United States Department of Commerce. National Telecommunications and Information Administration. *Falling Through the Net : Toward Digital Inclusion.* October 2000. Washington, DC. [http://www.ntia.doc.gov]

United States Department of Education. Office of the Under Secretary, Planning and Evaluation Service, Elementary and Secondary Education Division. *E-Rate and the*

Digital Divide: A Preliminary Analysis From the Integrated Studies of Educational Technology. September, 2000. Washington D.C. [http://www.ed.gov/offices/OUS/eval/elem.html#technology]