

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of
Request for Review of a Decision of the
Universal Service Administrator by
Riverside County Office of Education
Riverside, California
Schools and Libraries Universal Service
Support Mechanism
File No. SLD-148309
CC Docket 02-6

ORDER

Adopted: July 21, 2016

Released: July 21, 2016

By the Chief, Telecommunications Access Policy Division, Wireline Competition Bureau:

I. INTRODUCTION

1. Consistent with precedent, we grant an appeal filed by the Riverside County Office of Education (Riverside) seeking review of a decision by the Universal Service Administrative Company (USAC) seeking partial recovery of E-rate support disbursed for funding year 1999. We find that USAC properly concluded that Riverside did not pay its full non-discounted share of the cost of E-rate eligible purchases because it paid only a portion of its non-discounted share using a trade-in credit for equipment that was worth substantially less at the time of the trade-in than it had been worth four months earlier when the valuation was conducted. Upon review of the record, we also find that Riverside has demonstrated the existence of special circumstances warranting a waiver of Commission rules.

1 Request for Review of a Decision of the Universal Service Administrator by Coordinated Construction, Inc.; Schools and Libraries Universal Service Support Mechanism, CC Docket No. 02-6, Order, 26 FCC Rcd 14308, 14309, para. 4 (WCB 2011) (Coordinated Construction Order) (granting a waiver of E-rate program rules where the "violation occurred during the second year of the E-rate program when applicants had less familiarity with program rules," "there is no evidence of waste, fraud or abuse," and "strict adherence with USAC's procedures and the Commission's rules . . . would be inconsistent with the public interest"); Request for Review of a Decision of the Universal Service Administrator by Idaho Falls School District 91; Schools and Libraries Universal Service Support Mechanism, CC Docket No. 02-6, Order, 25 FCC Rcd 5512, 5516, para. 9 (WCB 2010) (Idaho Falls School District Order) (finding that where an "error took place in the very early stages of the E-rate program, when applicants, service providers, and USAC were not yet familiar with the operation of the program," special circumstances may justify a waiver of E-rate program rules).

2 The E-rate program is more formally known as the schools and libraries universal service support program.

3 See Letter from Paul Besozzi, on behalf of Riverside County Office of Education, to Marlene Dortch, Secretary, Federal Communications Commission, CC Docket No. 02-6 (filed Apr. 16, 2009); Supplement to Request for Review of the Decision of the Universal Service Administrator by Riverside County Office of Education, CC Docket No. 02-6, File No. SLD-148309 (filed Aug. 27, 2009) (Riverside Request for Review). Section 54.719(c) of the Commission's rules provides that any person aggrieved by an action taken by a division of USAC may seek review from the Commission. 47 CFR § 54.719(c).

2. In the early years of the E-rate program it was unclear how applicants and service providers should perform fair market valuations for equipment trade-ins. Riverside acted in good faith when, at the start of only the second funding year of the E-rate program, it paid a portion of its non-discounted share by trading in equipment based on the value assessed in March 1999, rather than on an estimate of the equipment's value on July 1, 1999, when the vendor took possession of the equipment. Riverside had no notice that USAC would not allow it to pay its non-discounted share using the fair market value of the equipment to be traded in set at the time it entered into its contract nor did it have any way to know that the fair market value of the equipment would drop precipitously over the course of only a few months. We therefore grant Riverside's request for waiver, and remand the underlying application to USAC for further action consistent with this Order.

II. BACKGROUND

A. E-rate Program Rules and Requirements

3. The E-rate program, which was established in 1997, and first provided funding in 1998, allows eligible schools, libraries, and consortia that include eligible schools and libraries to apply for universal service support for telecommunications, telecommunications services, and internal connections.⁴ E-rate applicants may qualify for discounts, ranging from 20-90 percent of the purchase price of eligible services, determined by poverty indicators, geography, and the category of services being purchased.⁵ Applicants are required to pay the non-discounted portion of the cost of the E-rate goods and services to their service provider(s).⁶

4. In the *Universal Service First Report and Order*, the Commission found that requiring schools and libraries to pay a share of the costs of E-rate supported services encourages them to avoid unnecessary and wasteful expenditures because they will be unlikely to commit their own funds for purchases that they cannot use effectively.⁷ Schools and libraries have always been permitted to credit the trade-in value of their equipment toward the payment of their non-discounted share.⁸ Over the years, USAC and Commission guidance about how to treat equipment trade-ins has grown more robust, but at the start of the program, guidance was sparse and there was no published guidance regarding the valuation of trade-in equipment. In 2004, USAC began to advise stakeholders that the trade-in value of equipment credited toward the applicant's non-discount share must be the fair market value or acquisition cost of the equipment, whichever is lower.⁹ In 2011, the Commission clarified that equipment purchased

⁴ 47 CFR §§ 54.501-54.502.

⁵ 47 CFR § 54.505.

⁶ 47 CFR § 54.523 (“An eligible school, library, or consortium must pay the non-discount portion of services or products purchased with universal service discounts.”). Although this rule was not codified until 2004, it has been in place since the start of the E-rate program. See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 9035-36, para. 493 (1997) (subsequent history omitted) (*Universal Service First Report and Order*) (establishing the requirement that schools and libraries pay a share of the cost of E-rate supported services); see also *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Third Report and Order and Second Further Notice of Proposed Rulemaking, 18 FCC Rcd 26912, 26929, para. 41 (2003) (codifying the non-discount requirement).

⁷ *Universal Service First Report and Order*, 12 FCC Rcd at 9036, para. 493.

⁸ See, e.g., USAC, Schools and Libraries Program, *Frequently Asked Questions about Eligibility of Products and Services* (Dec. 14, 2001), <http://web.archive.org/web/20020117204706/http://www.sl.universalservice.org/reference/EPSFAQ.asp>.

⁹ See USAC, Schools and Libraries Program, *Frequently Asked Questions about Eligibility of Products and Services, Transfer or Trade-in of Components* (Feb. 13, 2004), <http://www.sl.universalservice.org/reference/EPSFAQ-f.asp> (explaining that applicants may use the fair market trade-in value of equipment not purchased with E-rate discounts toward payment of their non-discount share).

with E-rate discounts cannot be traded-in sooner than five years after the equipment is installed.¹⁰ In 1999, however, no specific guidance regarding the valuation of trade-in equipment toward an applicant's non-discount share of the cost of eligible services was available from the Commission or USAC.

B. Summary of Facts

5. Riverside is a service agency that provides support to Riverside County's 23 school districts.¹¹ Riverside established a consortium composed of its 23 member school districts, conducted a competitive bid process for internal connections, and selected Spectrum Communications Cabling, Inc. (Spectrum) as the service provider for funding year (FY) 1999, the second full year of the E-rate program.¹² Riverside and Spectrum agreed that Riverside would trade in certain equipment owned by its consortium members as credit toward the payment of its non-discounted share of the cost of services owed to Spectrum.¹³ The parties negotiated an agreement whereby Spectrum would accept trade-in equipment from the consortium that Spectrum valued as of March 1, 1999 at \$1,813,505.66.¹⁴ This amount covered the non-discounted portion of the total contract price that Riverside owed to Spectrum.¹⁵ Some consortium members later decided to retain their equipment and, instead, pay their portion of the contract price to Spectrum in cash, in an amount totaling \$155,996.21.¹⁶ Riverside paid the remaining portion of the purchase in the form of the equipment trade-in, consistent with the terms of the contract and the March valuation.¹⁷ That equipment was transferred to Spectrum on July 1, 1999.¹⁸ In April 2000, USAC approved E-rate support for Riverside's purchase of eligible internal connections from Spectrum on behalf of 23 school districts.¹⁹

6. In 2003, as part of a post-disbursement beneficiary audit, the auditors questioned the trade-in value that Riverside and Spectrum placed on the traded-in equipment in connection with Riverside's FY1999 E-rate application.²⁰ In response, Spectrum commissioned an independent appraisal, which found that in July, when the equipment was transferred to Spectrum, it was worth only \$1,316,159.²¹ That amount represented a \$340,945 decrease in value since the assessment Spectrum

¹⁰ See Schools and Libraries Universal Service Support Mechanism; A National Broadband Plan for Our Future, CC Docket No. 02-6, GN Docket No. 09-51, Sixth Report and Order, 25 FCC Rcd 18762, 18795, para. 74 (2010) (*Schools and Libraries Sixth Report and Order*); 47 CFR § 54.513(b); USAC, Schools and Libraries Program, *Disposal or Trade-In of Equipment*, <http://www.usac.org/sl/applicants/before-youre-done/equipment-disposal.aspx> (last visited June 13, 2016).

¹¹ Riverside Request for Review at 4.

¹² *Id.* at 5.

¹³ *Id.* at 6. The equipment at issue was not purchased with E-rate funds. *Id.*

¹⁴ *Id.*

¹⁵ Riverside Request for Review, Administrative Record (Riverside Administrative Record) at FCCAR00082-111 (Spectrum Request for Review (dated Aug. 30, 2004)).

¹⁶ Riverside Request for Review at 6, n.7; Spectrum Request for Review at 5.

¹⁷ Riverside Request for Review at 6; Spectrum Request for Review at 5.

¹⁸ See Riverside Administrative Record at FCCAR00077-79 (Letter from USAC, Schools and Libraries Division, to Pierre Pendergrass, Spectrum Communications Cabling Services, Inc. (dated July 1, 2004) (2004 USAC Appeal Decision)).

¹⁹ See Riverside Administrative Record at FCCAR00010-18 (Letter from USAC, Schools and Libraries Division, to ROP – Riverside County, Mr. Elliott Duchon (dated Apr. 18, 2000) (Riverside Funding Commitment Decision Letter)).

²⁰ Riverside Request for Review at 6-7.

²¹ *Id.* at 7; Riverside Administrative Record at FCCAR00019-37 (DMC Consulting Group Appraisal Report for Spectrum Communications dated March 2003 (Appraisal)).

conducted in March 1999. The audit therefore found that although Riverside had been credited as having paid \$1,813,505.66 to Spectrum for its non-discounted share (\$1,657,094 in trade-in value as of March 1999, plus \$155,996.21 in cash), Riverside should only have been credited as paying \$1,472,155.21 to Spectrum for its non-discounted share (\$1,316,159 in trade-in value as of July 1999, plus \$155,996.21 in cash).²²

7. In light of the audit findings, USAC concluded that the July 1999 appraisal value of Riverside's trade-in equipment was the appropriate value to use in determining whether Riverside had paid the non-discounted share of the services it purchased from Spectrum, because it was the value at the time Spectrum took possession of the equipment. Therefore, in October 2003, USAC sought to recover the erroneously disbursed E-rate support.²³ The amount USAC sought to recover represented the difference between the E-rate funding USAC previously committed based on the incorrect equipment valuation, and the E-rate funding USAC should have committed based on the correct trade-in equipment valuation.²⁴

C. Riverside's Request for Review

8. This appeal follows several rounds of procedural appeals, at the end of which USAC determined that Riverside was the party responsible for insufficient payment of its non-discount share and issued a decision on remand to Riverside.²⁵ Riverside now appeals this decision.²⁶ In the present appeal, Riverside challenges (1) USAC's approach to valuing equipment trade-ins for E-rate purposes, (2) USAC's authority to establish such an approach without an explicit Commission rule in place in FY1999, and (3) whether liability for any assessment error should be with Spectrum, rather than Riverside.²⁷ Alternatively, Riverside seeks a waiver of E-rate rules based on considerations of equity, fairness, and hardship.²⁸

III. DISCUSSION

9. The record demonstrates that during the relevant time period there was no clear guidance for applicants about how to value trade-in equipment.²⁹ The record further demonstrates that Riverside made a good faith attempt to move forward with its E-rate application by getting an early start on its service provider contract, months prior to the E-rate application deadline, and agreeing to trade in equipment to use towards its non-discounted share.³⁰ While Riverside does not dispute the determination

²² See Appraisal at Exhibit B (Portfolio Analysis – Detail).

²³ Riverside Request for Review at 7; Riverside Administrative Record at FCCAR00038-59 (Letter from USAC, Schools and Libraries Division, to Mr. Elliott Duchon, ROP – Riverside County (dated Oct. 3, 2003) (Recovery of Erroneously Disbursed Funds (Spectrum COMAD Letter)). USAC initially sought recovery of the erroneously disbursed funds from Spectrum, because E-rate rules at the time required recovery of funds due to rule violations from the service provider. Later, USAC determined that Riverside was the responsible party. See *infra* note 25.

²⁴ *Id.*

²⁵ Riverside Administrative Record at FCCAR00001-02 (Letter from USAC, Schools and Libraries Division, to Rina M. Gonzales, on behalf of Riverside County Office of Education (dated Feb. 17, 2009) (2009 USAC Decision on Remand)). This decision on remand was issued after the Bureau remanded the case to USAC to consider whether the repayment in erroneously disbursed funds should come from Spectrum or Riverside. In this decision, USAC concluded that Riverside was the party responsible for repaying the erroneously disbursed funds. *Id.*

²⁶ Riverside Request for Review.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.* at 3.

³⁰ *Id.* at 5-6, 21.

of the fair market value of the equipment at the time of the trade-in, when it filed its E-rate application Riverside believed it was correctly applying the equipment trade-in rules by valuing the equipment at the time it signed its contract with Spectrum, and it was unaware that the value of the equipment it was providing to Spectrum would rapidly decline over the course of only four months.³¹

10. We reject Riverside’s first two arguments. USAC did not adopt an incorrect or “new” valuation rule or policy when it concluded that Riverside’s trade-in equipment should have been assessed based on the value it would have at the time Spectrum took possession of the equipment, i.e., July 1, 1999. USAC merely applied the Commission’s requirement that an applicant pay its non-discounted share of E-rate services in a manner most consistent with protecting the E-rate fund from waste, fraud and abuse.³² The trade-in date is, after all, effectively the time at which the applicant is making payment for services. Routinely allowing applicants and vendors to use the fair market value of equipment at some other date would invite them to game the system and introduce the risk of waste, fraud and abuse into the E-rate program. Therefore, we affirm USAC’s finding that Riverside violated the Commission’s rules by valuing the trade-in equipment at the date of the assessment, ignoring any depreciation during the months before Spectrum actually took possession of the equipment, thereby failing to pay the full amount of its non-discounted share.³³ We also affirm USAC’s decision to hold Riverside responsible for this violation, as it was Riverside’s responsibility to ensure it was fully paying for the non-discounted share of the E-rate supported services, and it was aware that the equipment was valued by Spectrum as of March 1, 1999—four months before Riverside transferred the equipment to Spectrum.³⁴

11. Although we find that Riverside violated its obligation to pay the full amount of its non-discounted share, we also find that, based on the specific facts and circumstances presented here, Riverside has demonstrated the existence of special circumstances warranting a waiver of Commission rules.³⁵ As discussed above, at the time Riverside filed its E-rate application for FY1999 (more than 17

³¹ *Id.* at 21.

³² *Universal Service First Report and Order*, 12 FCC Rcd 8776 at 9036, para. 493 (“Requiring schools and libraries to pay a share of the cost should encourage them to avoid unnecessary and wasteful expenditures because they will be unlikely to commit their own funds for purchases that they cannot use effectively. A percentage discount also encourages schools and libraries to seek the best pre-discount price and to make informed, knowledgeable choices among their options, thereby building in effective fiscal constraints on the discount fund.”).

³³ See 47 CFR § 54.523; *Request for Review of A Decision of the Universal Service Administrator by Iosco Regional Educational Service Agency; School and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Order, 24 FCC Rcd 12735, 12739, para. 8 (WCB 2009); *Requests for Waiver and Review of Decisions of the Universal Service Administrator by Al-Ihsan Academy et al.; Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Order, 27 FCC Rcd 1927, 1927, para. 1 (WCB 2012) (*Al-Ihsan Academy Order*) (both denying requests for review where applicants failed to pay the full non-discounted portion of services received from their service provider).

³⁴ See *Federal-State Joint Board on Universal Service; Changes to the Board Of Directors for the National Exchange Carrier Association, Inc.; Schools and Libraries Universal Service Support Mechanism Schools and Libraries*; CC Docket Nos. 96-45, 97-21, and 02-6, Order on Reconsideration and Fourth Report and Order, 19 FCC Rcd 15252, 15256-27, paras. 13-15 (2004) (*Schools and Libraries Fourth Report and Order*) (determining that recovery of E-rate funds disbursed in violation of the statute or a rule should be directed to the party or parties responsible for the statutory or rule violation, including a school or library).

³⁵ See 47 CFR § 1.3 (the Commission may waive any provision of the rules on its own motion or on petition if good cause is shown); *Northeast Cellular Telephone Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990) (“Waiver is appropriate if special circumstances warrant a deviation from the general rule, and such deviation would better serve the public interest than strict adherence to the general rule.”); *Request for Review of the Decision of the Universal Service Administrator by Ysleta Independent School District et al.; Federal-State Joint Board on Universal Service, Changes to the Board of Directors of the National Exchange Carrier Association, Inc.*, CC Docket Nos. 96-45, 97-21, Order, 18 FCC Rcd 26407, 26437, para. 72 (2003) (finding that a waiver of the Commission’s rules was “in the public interest in light of the uncertain application of our rules to the novel situation presented”).

years ago), the E-rate program rules for valuing the fair market value of trade-in equipment were vague and unclear, resulting in Riverside's misunderstanding. We have previously found that where an "error took place in the very early stages of the E-rate program, when applicants, service providers, and USAC were not yet familiar with the operation of the program," special circumstances may justify a waiver of E-rate program rules.³⁶ The record here demonstrates that Riverside acted in good faith to comply with what it reasonably perceived to be the applicable program rules at the time. The record also shows that Riverside and Spectrum agreed to a valuation a mere four months before taking possession of the trade-in equipment. The short lapse in time between valuation and possession demonstrates that Riverside was not attempting to defraud the system, but was merely attempting to move quickly on its E-rate purchases. That the equipment suffered a precipitous decline in value despite Riverside's good faith efforts to transfer possession soon after valuation is a mitigating special circumstance in this case. Finally, there is no evidence of waste, fraud, abuse, or misuse of funds. Accordingly, we find there is good cause to waive Section 54.523 of our rules in this instance.

12. We emphasize the limited nature of this decision and stress that this Order does not alter the obligation of E-rate program participants to comply with the Commission's rule requiring applicants to pay the full amount of its non-discounted portion of E-rate services and/or equipment. We retain our commitment to detecting and deterring potential instances of waste, fraud, and abuse by ensuring that schools and libraries pay a share of the costs and be financially invested in E-rate services. Applicants who trade in equipment to use toward the payment of their non-discounted share must value that trade-in equipment based on the time the service provider takes possession of that equipment, and no earlier.³⁷

13. For all of the reasons discussed above, we grant Riverside's request for a waiver and remand the underlying application to USAC for further action consistent with this Order. In remanding Riverside's application to USAC, we make no finding as to the ultimate eligibility of the services or the application.

IV. ORDERING CLAUSES

14. Accordingly, IT IS ORDERED, pursuant to the authority contained in sections 1-4 and 254 of the Communications Act, as amended, 47 U.S.C. §§ 151-154 and 254, and sections 0.91, 0.291, 1.3, and 54.722(a) of the Commission's rules, 47 CFR §§ 0.91, 0.291, 1.3 and 54.722(a), that the request for review and/or waiver filed by Riverside County Office of Education IS GRANTED, and the underlying application IS REMANDED to USAC for further consideration in accordance with the terms of this Order.

³⁶ *Idaho Falls School District Order*, 25 FCC Rcd at 5516, para. 9; *see also Coordinated Construction Order*, 26 FCC Rcd at 14309, para. 4 (granting a waiver of E-rate program rules where the "violation occurred during the second year of the E-rate program when applicants had less familiarity with program rules," "there is no evidence of waste, fraud or abuse," and "strict adherence with USAC's procedures and the Commission's rules . . . would be inconsistent with the public interest").

³⁷ Riverside argues that the required timing for fair market valuation forces applicants to wait to value trade-in equipment almost three months after they are required to file the FCC Form 471, which would require parties to leave an essential element of their contract bargain (consideration) to some future date, and prevent applicants from timely filing their FCC Forms 471. *See Riverside Request for Review* at 14-15. We disagree. While E-rate applicants and service providers are required to agree on the total cost of services and/or equipment at the time they file their FCC Form 471, they are not required to agree on the form of payment. In determining how to pay for the negotiated price of services where trade-in equipment is involved, an applicant has two options. The applicant can either (i) determine the fair market value of the equipment and transfer the equipment to the service provider at the time the parties enter into the contract for E-rate supports services, or (ii) agree by contract that the applicant will trade-in equipment to be used, at least in part, towards the cost of its non-discount share, and value and transfer that equipment at some later date that is otherwise consistent with the applicant's obligation to pay its non-discount share.

15. IT IS FURTHER ORDERED, pursuant to the authority contained in sections 1-4 and 254 of the Communications Act, as amended, 47 U.S.C. §§ 151-154 and 254, and sections 0.91, 0.291, 1.3, and 54.722(a) of the Commission's rules, 47 CFR §§ 0.91, 0.291, 1.3, and 54.722(a), that section 54.523 of the Commission's rules, 47 CFR § 54.523, IS WAIVED for Riverside County Office of Education.

FEDERAL COMMUNICATIONS COMMISSION

Ryan B. Palmer
Chief
Telecommunications Access Policy Division
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