Insight

The Debate on Universal Service Fund Reform: A Primer

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Executive Summary

- The Universal Service Fund (USF) is a decades-old program that aims to ensure that all Americans have access to essential telecommunication services; while initially focused on telephone services, it now covers "advanced services" such as broadband.
- The USF is funded through contributions from telecommunications companies, which must pay a percentage of its interstate and international revenues from its traditional telecommunications services, such as voice telephony.
- As the fund's scope has been broadened to cover new services, there has been a push to reform its contribution mechanism, especially as the subscription rate to landline voice services has been steadily declining; there is no consensus over what the appropriate funding mechanism should be, however.
- The introduction of new programs aimed at low-income populations such as the Emergency Broadband Benefit/Affordable Connectivity Program raises the question of whether the USF has become redundant.

Introduction

As the COVID-19 pandemic took the world by surprise in 2020, Americans saw their day-to-day routines significantly transformed with a significant number of workers and students shifting to remote working and learning options. While the advances in the broadband ecosystem help ease this transition, those with limited access or the ability to afford broadband bore the pain of adjustment. The pandemic has highlighted the gap between those with reliable, high-speed internet and those without, better known as the "digital divide."

Through several decades, the federal government has funded a variety of initiatives to ensure that all Americans have reliable access to the latest communication technologies. The Universal Service Fund (USF) and its associated programs are, according to the Federal Communications Commission (FCC), the "cornerstone" of the Communications Act of 1934, and by extension, other federal efforts to bridge the digital divide. While efforts to promote universal service initially supported the deployment and adoption of telephony, in recent years the fund's focus expanded from telephone service to "advanced services," including broadband. The continuous shift in priorities has sparked debates over the fund's structure, mainly its funding, which currently relies on charges to telecommunications service providers.

This primer outlines the current functioning of the USF, the programs that benefit from it, and the three major reform proposals that are being discussed.

What Is the Universal Service Fund?

The Communications Act of 1934 gave the newly created FCC the task to make "a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges" available to all Americans. As a part of the sweeping changes included in the 1996 Telecommunications Act, Congress explicitly codified the principles of universal service, leading to the creation of the USF and expanding the range of services it would cover to include advanced services such as broadband.

Currently, the USF supports four different programs:

- The Connect America Fund: This fund provides support for the deployment of broadband by qualifying telecom companies serving high-cost areas to provide access to a comparable service at rates reasonably comparable to those in urban areas.
- Lifeline program: The program assists low-income customers by providing a discount on their monthly telephone or broadband bills.
- E-Rate: Also known as Schools and Libraries Support, E-Rate provides access to telecommunication services, internet access, and internal connections to eligible schools and libraries.
- Rural Health Care Support: This program allows rural health care providers to pay rates for telecommunications services similar to those in urban areas by subsidizes Internet access and infrastructure with the intent of making telehealth services affordable.

The USF is funded through contributions from telecommunications companies, which must

pay a percentage of their interstate and international revenues from their telecommunications services such as voice telephony. This percentage, known as the contribution factor, is revised quarterly and may increase or decrease depending on the needs of the fund's programs. In some instances, these companies are permitted to explicitly transfer the costs to consumers, charging a fee for "Universal Service" in their monthly bills.

Major Proposals for Reform

While the USF's scope has been broadened to cover new services such as broadband, the funding structure still relies on telecommunication services such as voice telephony. As the subscription to landline telephony services has been steadily declining, many have called for reform of the way the USF is funded. While many parties broadly support reform, there is no consensus on an appropriate funding mechanism. Currently, there are three main reform proposals that have garnered support. First, the contribution base could be expanded to include a number of services that qualify for contribution to the fund, most notably broadband. Second, tech companies could be required to contribute to the fund, as they leverage broadband infrastructure and see higher profits from an increased user base. Finally, some propose ending the current contribution mechanism, and instead rely on direct appropriation from Congress.

Expanding the Number of Qualifying Services

One of the most prominent proposals for reform would aim to expand the number of services that contribute to the fund. In a recently published letter, a coalition of public interest organizations, think tanks, and local telecommunications businesses expressed concerns that the USF fee has "spiraled" from 7 percent to around 30 percent over the last two decades and is expected to exceed 40 percent in the near future.

The proposal would extend the contributing services in the Communications Act to include "broadband internet access services." Supporters claim that this expansion would lower the USF fee to around 4 percent, and justify this expansion on the grounds that broadband companies benefit from increases in adoption due to the programs that comprise the USF. Critics of this proposal worry that expanding the base would lead to increased prices that could affect adoption and retention rates of broadband services. Yet the coalition's letter cites a study by Berkeley Research Group that claims that this fee would not have material impact on adoption rates.

This proposal could also face significant legal hurdles in its implementation. The Communications Act's focus on interstate telecommunications carriers means that an

expansion of the qualified services would likely require Congress to reform the Act. Alternatively, as broadband services are classified as information services, proponents of this approach may seek to reclassify broadband as a Title II service, an issue that has sparked controversy in the past.

Require Tech Companies to Contribute to the Fund

Another proposal that has garnered significant support is to include tech companies – also called edge providers – among the contributors to the fund. This proposal has found a vocal leader in FCC Commissioner Brendan Carr. Proponents of such a reform claim that tech companies, especially those in the video-streaming industry, are benefitting from an increased user base, while also using a significant amount of bandwidth. In support of this proposal, Carr cites a study that claims online streaming services account for 75 percent of all traffic on rural broadband networks. The study also claims that between 77 and 94 percent of total network costs are related to adding capacity or supporting the delivery of these streaming services.

While the specific details over how to charge these companies remain scarce, Carr highlights that it would take 0.009 percent of the revenues of the main streaming companies in order to cover the USF's current costs. Among the goods and services that this proposal aims to include are streaming services, online advertising, app store services, device sales, content delivery networks, cloud services, and online gaming services.

This proposal would also face legal challenges similar to the ones mentioned in the previous section. Including edge providers as a qualified service will likely require congressional reform to the Communications Act. Nonetheless, this service category has less of a direct relation to those typically covered by the USF, particularly in comparison to broadband or telecommunications providers. This would likely make including them as qualified providers more difficult to justify. Service classification could also be a particularly complex topic in implementing this measure, as even if broadband was reclassified as a Title II service, the question of the authority of the FCC to regulate edge providers under Title II remains in doubt. Further, most vocal advocates for this proposal tend to oppose the reclassification of broadband as a Title II service at all, fearing that such a move would invite more intrusive regulation of the service.

Direct Appropriation from Congress

Rather than changing the contribution base and expanding services that must support universal service, some have proposed funding the USF through direct appropriation from Congress. This would allow the fund to remain financially sound while simultaneously

lowering costs for consumers; Congress could use a high-end estimate of the current $8 billion budget as a baseline, or ask the Universal Service Administrative Company to convey a funding proposal. With this change, the fund would not depend on fees on any services. This might be attractive because these fees tend to be transferred to consumers as higher prices and are regressive in nature, as users are charged the same fee regardless of their income level.

This proposal's biggest drawback is its reliance on political factors for budget approval. What it could potentially gain in financial stability in its execution could be lost in long-term planning capabilities if Congress' commitments waver. This could be potentially harmful for smaller carriers, which usually rely on long-term loans to finance their infrastructure deployment. Lenders might be more skeptical in approving loans where the potential revenue streams of a company are subject to change at any point in time.

The Potential Role of the USF Among New Broadband Programs

With the initial passage of the Emergency Broadband Benefit (EBB) and the inclusion of the Broadband Equity, Access, Deployment Program (BEAD) in the infrastructure bill, the FCC has various new programs directed toward closing the digital divide.

Unlike the USF, these programs have already secured funding. For deployment subsidization, Congress set aside $42.45 billion for BEAD which provides grants to states with the objective of funding broadband infrastructure in unserved areas. The infrastructure bill also created the Affordable Connectivity Program (ACP), a $14.2 billion program which extends and modifies the EBB. The ACP will allow eligible households to receive a $30 discount in their broadband service, and $75 for households in tribal lands. The plan also provides eligible households with a discount of up to $100 for the purchase of devices such as laptops, desktops, and tablets.

These programs are still early in their development and deployment, so the impact has yet to be quantified. Nonetheless, with the passage of these programs, it seems that policymakers are looking toward new mechanisms to fund low-income households and unserved areas. Considering the challenges with the USF mentioned above, policymakers could consider simply replacing the USF with the ACP or BEAD if they prove successful. The FFC has recently brought forward this possibility in a recent request for comments on the future of the USF.

Conclusion

The Universal Service Fund and its programs have aimed to help low-income Americans and those in high-cost areas access the telecommunications services that keep them connected

to the rest of the world. Currently, the program faces funding issues that have sparked a debate on an appropriate funding mechanism. While the need to reform seems apparent for most in the industry, there is no consensus on the best method of doing so. Additionally, the introduction of new programs such as the Emergency Broadband Benefit/Affordable Connectivity Program and the BEAD Program might raise the question of its utility. In a time when an internet connection is an essential tool for working and learning, assuring the viability of the programs that help bridge the digital divide should be a priority for policymakers.