Public Knowledge

Universal Service Fund (USF) and the Need for Reform

What is USF?

The Universal Service Fund (USF) consists of four FCC programs to help fund and implement the principle that all people in the United States should have access to affordable communications services as mandated by Congress in the Telecommunications Act of 1996 ('96 Act). The FCC has four USF programs to fulfill the universal service mission:

- High Cost Support (including the Connect America Fund, Rural Digital Opportunity Fund, and other programs to support service in rural areas)
- Lifeline for low-income consumers
- E-rate for schools and libraries
- Rural Health Care for rural health care providers

USF has been one of the nation's most important tools for connecting families, small businesses, and communities in need. It has been even more valuable during COVID-19 for families that must work and school from home.

USF is currently financed by residential and business customers who typically see a charge on their bill. USAC collects the fee (or "contribution") from telecommunications providers based on an assessment of their interstate and international end-user (customer) telecommunications service revenues. The amount of contributions that each provider pays on its telecommunications services is a percentage ("contribution factor") that is established in each quarter of every year by calculating the ratio of projected quarterly expenses for the USF programs to the total projected interstate and international telecommunications revenues collected.

Most contributions today come from wireline phone companies, mobile providers, cable operators, and others providing interconnected VoIP. There are several major categories of revenue that are not currently assessed for USF including information services, broadband internet access service ("BIAS"), or retail mobile data services that provide internet access.

How did we get here and why do we need USF reform?

The current funding mechanism for USF is under significant duress. The revenues subject to USF assessment have declined 63% in the last two decades, from almost $80 billion in 2001 to $29.6 billion in 2021—while we have seen explosive growth of broadband revenues. (In the last decade, revenues not subject to assessment, including broadband revenues, have increased from $173.2 billion to $361.2 billion.)

Meanwhile, the USF-assessed revenues decline has caused the contribution factor to increase dramatically from 6.9% in 2001 to a historic high of 33.4% in the second quarter of 2021. Assuming a continuation of historical trends of the decline of USF-assessed services, the contribution factor could approach 40% or more by 2025. This is unsustainable and puts the stability of the entire USF and its mission at risk.

To ensure the enduring value of the USF program and America's connectivity goals, we must have a smart and substantive conversation on the program's future. It is critical for the USF to be on a stable financial footing to ensure the viability and sustainability of the FCC's USF programs, which are key to ensuring affordable connectivity and service for schools, libraries, rural communities, and health care providers. While Congress has thankfully provided additional funding to meet consumers' broadband needs during COVID-19, that assistance is in addition to and does not replace the ongoing USF programs and the underlying statutory mission of universal service.

A common myth is that the contributions base has been declining due to a decrease in long distance and landline voice service revenues. In reality, however, the most dramatic decline in revenues has been for mobile services. Under the FCC's rules regarding providers' bundling of assessable and non-assessable services offered to customers (e.g., offering both telephone and broadband internet access service), contributors have discretion in determining what portion of the bundle is assessed. Mobile providers classify most of their monthly service revenues as broadband (i.e. data), which is not assessed. As a result, mobile carriers have shielded close to 80% of their mobile revenues from USF assessment. Other providers, such as cable operators and telcos, similarly attribute a small portion of the monthly bill to assessable voice service.

How should we solve this problem?

Reforming the current funding system for universal service is long overdue. The FCC first initiated a proceeding to consider changes to its framework for assessing USF contributions two decades ago in 2001, sought comment again in 2008 and in 2012, and referred it to the Federal-State Joint Board on Universal Service in 2014. The FCC has considered (1) expanding the current revenues-based system by assessing BIAS revenues; (2) assessing connections (both voice and broadband connections); or (3) assessing telephone numbers. But it has not taken action to date—even in the face of significant contribution factor increases.

INCOMPAS, NTCA-The Rural Broadband Association, SHLB, and Public Knowledge—organizations that don't always agree on other policy issues and even certain USF-related questions—have come together to find a smart solution. A recent report issued by USF expert and former FCC official Carol Mattey of Mattey Consulting sheds light on a path to USF sustainability that is within our reach—one that allows the FCC to move forward under its current statutory mandate to preserve and promote universal service, modernize the contribution mechanism, and save the critical USF program.

It is our belief that USF should evolve to encompass BIAS revenue as a foundational element of the program's survival. The Mattey Report estimates that the contribution factor would fall significantly and remain under 4% over the next four years under the recommended approach, which would stabilize USF and modernize it to reflect today's realities.

Here's why we support this reform proposal:

1. SMART: It is smart public policy. Broadband internet access service is the primary form of access to networks today and is the service that is driving value in today's communications marketplace. It should contribute to support today's modern communications network. In fact, all four USF programs now support broadband connectivity and broadband should contribute to support connectivity for every American. **It is common sense to use broadband revenues to fund programs that support broadband access.**

2. **STABLE: Broadband service revenues are expected to remain stable (with the potential for some modest growth), which would stabilize the current funding mechanism into the future.**

3. **FAST: Assessing BIAS can be implemented more quickly than the alternative proposals.** The FCC can use its existing authority to do so. In addition, companies have been contributing based on revenues for more than two decades, and it is a known system. In contrast, moving to a connections- or numbers-based assessment system likely would require a significantly longer implementation timeline, as there would be numerous definitional issues to resolve.

4. **TRANSPARENT: Retaining the current revenues-based financing system allows for an additional level of scrutiny for accuracy.** The vast majority of USF contributions comes from publicly traded companies whose revenues are already audited for financial reporting purposes. In contrast, there are no comparable safeguards to provide comfort that numbers or connections are accurately reported. **Assessing both BIAS and voice services also mitigates gamesmanship** and the incentives of providers to arbitrarily allocate revenues from bundled services to one service and not the other—which creates inequity where some continue to pay in and others do not, while everyone benefits from the increased connectivity made possible by USF.

5. **EQUITABLE: As more consumers have shifted their usage to broadband services, the end-user charge has fallen on those that have not made the switch, such as older Americans. Including BIAS revenues will ensure the costs of achieving our universal service goals are equitably shared.**

Reforming the current contribution methodology now to assess BIAS is a necessary and important first step in stabilizing the current system and ensuring USF can continue to meet its mission to make affordable broadband service universal.