FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON

Mike O'Rielly
Commissioner

June 14, 2017

The Honorable Frank Pallone, Jr.
Ranking Member
House Committee on Energy and Commerce
2125 Rayburn House Office Building
Washington, D.C. 20515

Dear Ranking Member Pallone:

I am responding to your letter of May 17, 2017, regarding the Federal Communications Commission's Universal Service Fund (USF) High-Cost Program.

It is my understanding that Congress is considering adding provisions related to broadband deployment to larger infrastructure legislation being prepared for debate. If it were to do so, I firmly believe that Congress should give serious consideration to improving and strengthening the Commission's authority to remove barriers to broadband buildout nationwide, including our preemptive authority over state and local impediments and excessive fee extractions, and the need for similar provisions to apply to the tribal review process. Such barriers remain one of the most significant reasons broadband is not more readily available to American consumers.

Similarly, if Congress were to decide to provide further federal funds for broadband deployment, which should be weighed carefully, I would humbly suggest that it should consider allocating such funds via the Commission's High-Cost Program. While our High-Cost Program is not perfect, it is more efficient and better at targeting resources than existing programs in other federal agencies or any new programs that could be created. Additionally, the Commission has worked to increase market forces throughout the program, including installing multi-round reverse auctions to minimize subsidies to only that which is needed to accomplish program objectives. There is also greater demand for High-Cost Program subsidies than its current budget can afford, highlighting that funding could be rapidly distributed to promote deployment to additional unserved communities without much disruption.

At the same time, the High-Cost Program would benefit from certain improvements and the establishment of additional efficiencies. As you note, the Commission's findings with respect to fraud and illegal activity perpetrated by the former owner of Sandwich Isles Communications, Inc. indicates a need to further clarify which practices or costs may not be recovered through USF or included in the rate base for rate-of-return carriers. Here are my answers to your specific questions:

(1) To your knowledge, why has FCC not yet undertaken such a proceeding?

It is my understanding that the Commission is in the process of concluding a proceeding to further clarify that certain expenses are not permitted for USF reimbursement or inclusion in the rate base. I have worked collaboratively with Chairman Pai, Commissioner Clyburn and affected carriers on the matter and expect that the item, which was initiated as part of last year's reforms for rate-of-return carriers, should be before the Commission for a vote in the very near future.

(2) Are there additional actions that the FCC should take to address waste, fraud, and abuse in the High-Cost Program? What are those actions? How quickly can the FCC act to implement those reforms?

The Commission is pursuing, at the request of the affected industry, a number of smaller, technical changes to our rate-of-return regulations. These changes, which would improve the existing regulations, are expected to be considered in the coming months.

Additionally, one area that Commissioner Clyburn and I have worked on extensively is whether to means test the High-Cost Program. We have published a blog on the topic that includes questions to the public on how best to install means testing in the program while minimizing any reporting or compliance burdens on affected carriers. Given the difficult budgetary issues facing all of USF, this programmatic change seems appropriate to save scarce USF dollars. Overall, this effort may take a number of months to effectuate, but it is more important that it be done right rather than done quickly.

I hope the above information provides sufficient answers to your questions, but if not, please do not hesitate to contact me or my staff.

Sincerely,

Mike O'Rielly

Michael O'Rielly

Attachment: 5/31/17 Blog *"Would Means-Testing Bring More Efficiencies to the High-Cost Program?"*
cc w/ attachment: The Honorable Greg Walden

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Would Means-Testing Bring More Efficiencies to the High-Cost Program?

May 31, 2017 - 9:55 am

By Michael O'Rielly (/node/22746) | Commissioner
Mignon Clyburn (/node/22744) | Commissioner

The American people rightfully expect that all federal programs operate as efficiently as humanly possible and are targeted to help those truly in need. As FCC Commissioners, we have an obligation – as stewards of federal programs funded by monthly fees on American's communications bills – to improve the functionality and effectiveness of the programs we oversee, including the Federal universal service fund (USF). Failure to do so would waste consumers' hard-earned income, diverting it from the intended purposes and undermining public confidence in the programs.

While there is room for improvement in each of the USF programs, we firmly believe that it's time to fix a fundamental structural defect within our high-cost program. That is, we currently subsidize access to communications for people who don't need or deserve governmental assistance. In other words, we should end the practice of spending scarce USF high-cost support to illogically subsidize the cost of communications services for very rich people who happen to live in the more rural portions of our nation. For example, if someone is earning one million dollars per year, why should the American ratepayer be subsidizing their telephone and broadband service? And why are poor and middle-class Americans across the country asked to foot the phone and broadband bills of those in some of the wealthiest communities in America? This is not about stoking a debate over societal inequalities, as we have no animosity towards successful individuals; instead, it's about instilling some common sense in a government subsidy system where it is desperately needed. Because of our budgetary constraints, each dollar spent subsidizing service unnecessarily is a dollar that is not being used to help bring broadband to unserved Americans, particularly those who cannot afford the full cost of service.

The following language is meant to spark a conversation on how best to institute means-testing within USF's high-cost program. Given the importance of this issue, we seek public input on whether this proposal asks the right questions to enable the Commission to fully consider this issue, including the consequences of moving to a fully means-tested program and ways to minimize the administrative burdens for consumers, communications providers, and the Commission. In any event, we hope to bring this issue before the full Commission in the very near future so as to properly engage the entire American public.

* * *

Use of Means-Testing to Further Target High-Cost Universal Service Support

We seek comment on whether, and if so how, to implement means-testing within the high-cost universal service program.

Means-testing is the concept that government subsidies should be targeted to recipients who qualify for assistance based on their lower income and asset levels. It is commonly used in federal government programs to establish or scale eligibility for benefits, including in Medicare, Medicaid, the Supplemental Nutrition Assistance Program (SNAP), Supplemental Security Income (SSI), Low-Income Home Energy Assistance Program (LIHEAP), and Temporary Assistance for Needy Families (TANF).

In addition, the FCC's Lifeline program uses means-testing to direct assistance to low-income consumers that might not otherwise subscribe to phone or broadband service. Recipients qualify for discounted service based on participation in SNAP, Medicaid, SSI, Federal Public Housing Assistance, and the Veterans Pension benefit program, as well as all current Tribal qualifying programs.[1] Alternatively, consumers can qualify by demonstrating income of less than 135 percent of the federal poverty guidelines.[2]

While high-cost subsidies are not currently means-tested, the idea that they should be is not new. A 2002 report by GAO noted that there was support for making high-cost a means-tested program.[3] In 2006, former FCC Chief Economist Thomas Hazlett observed that while high-cost subsidies "may enable some operators to offer prices as low as those paid by urban and suburban residents for service that is much less costly to supply, the lower prices are offered to all residents, rich and poor alike."[4] And a 2013 paper by Thomas Hazlett and Scott Wallsten stated that "[t]he consensus among economists" is that the high-cost program is inefficient because "poor urban consumers pay significant telecommunications fees to subsidize affluent phone customers in Aspen, Colorado and Jackson Hole, Wyoming."[5]

Since that time, the Commission has taken a number of steps to root out inefficiencies in high-cost subsides. In particular, the Commission has begun using reverse auctions to produce more efficient funding levels, targeted support to unserved areas, established a policy of funding one provider per area, and limited funding to areas where there is no unsubsidized competitor. Indeed, because the high-cost program is subject to an overall budget, the Commission has tried to ensure that spending is as efficient and cost-effective as possible. Notwithstanding these reforms, high-cost funding has remained subject to criticism for having "perverse distributional effects, by subsidizing wealthy rural consumers, who are never subject to means-testing, but who can easily afford to pay the full cost of access."[6]

The Commission most recently sought comment on means-testing in the 2011 *USF/ICC Transformation Order and FNPRM*. In particular, it sought comment on limiting Remote Areas Fund support—which, at the time, was expected to take the form of consumer vouchers—to income-eligible consumers.[7]

We now invite comment on using means-testing more broadly within each of the high-cost programs. What are the advantages and disadvantages of using means-testing? Would it make the program more efficient as some commenters have suggested? Given our limited budget, would it enable the Commission and/or providers to retarget funding to areas or consumers in greater need of support? How can it be implemented without disruption to the current programs? Should it apply on a going- forward basis as rules for additional parts of the high-cost program, such as the Remote Areas Fund, are adopted? Could it eventually be implemented uniformly across all of the high-cost programs as they come up for renewal in the years to come, or would it need to be tailored to each program? How can it be structured to be effective and with sufficient accountability while imposing the fewest costs on providers and consumers? How should the Commission set income eligibility criteria? How should the Commission structure means-testing in a way that is administrable for the Commission, companies, and consumers? What data would the Commission need in order to effectively means-test the high-cost program?

We also seek comment on specific ways to implement means-testing. For example, should the Commission require that consumers identified as having adjusted gross income (AGI) levels above a set threshold to pay the full cost of providing service to their locations? If the Commission were to adopt this option, how should it set the income threshold? Would it be reasonable to select an AGI of $1 million or $500,000? How would consumers above the threshold be identified? Should consumers above the threshold be required to notify their provider? How can providers make consumers aware of such an obligation? Could they do so through an annual notice to their customers? How can the Commission ensure compliance with such requirements?

Another option is to utilize means-testing as a weighting factor in future reverse auctions or other distributions of universal service support. We seek comment on this approach. For example, should the Commission adopt a weighting mechanism that would give preference to bids or builds that target low-income areas? What are the appropriate income cutoffs? What is the appropriate area to which a bidding weight or credit would attach? How strong of a preference should the Commission adopt for the lowest-income areas? What should the interplay be between these preferences and other weighting factors the Commission has adopted in the past?

Alternatively, an idea that was incorporated into prior legislative efforts to reform universal service would have excluded support to service for "consumers in households in high-cost areas where the Commission determines, based on publicly available information, that a service area has a substantially high percentage of households with income at or above the 95th percentile of national household income levels or develops an equivalent measurement."[8] What information could the Commission use to make such a determination? How should the Commission define "substantially high percentage"? Instead of service area, should the geographic area be a census block and, if so, how would that change the definition of "substantially high percentage"?

We seek comment on these and other ideas, including how they could be implemented in each part of the high-cost program, and the costs and benefits of doing so.

[1] *Lifeline and Link Up Reform and Modernization et al.*, WC Docket No. 11-42 et al., Third Report and Order,

Further Report and Order, and Order on Reconsideration, 31 FCC Rcd 3962, 3964-65, para. 7 (2016) (*2016 Lifeline Modernization Order*).

[2] *Id.*

[3] U.S. Government Accountability Office, *Federal and State Universal Service Programs and Challenges to Funding*, GAO-02-187, at 23 and note 35 (June 2002) ("[S]ome experts disagreed with aspects of the current High Cost Program. They felt it should be a means-tested program—that we should not subsidize everyone who chooses to live in a rural area irregardless of their ability to afford the higher cost of telephone service in such areas."), http://www.gao.gov/assets/240/233640.pdf (http://www.gao.gov/assets/240/233640.pdf).

[4] Thomas W. Hazlett, *"Universal Service" Telephone Subsidies: What Does $7 Billion Buy?* at 24 (June 2006), https://www.scribd.com/document/22635423/Thomas-W-Hazlett-Universal-Serv... (https://www.scribd.com/document/22635423/Thomas-W-Hazlett-Universal-Service-Telephone-Subsidies-What-Does-7-Billion-Buy-06-2006).

[5] Thomas W. Hazlett & Scott J. Wallsten, *Unrepentent Policy Failure Universal Service Subsidies in Voice & Broadband* at 29 (June 2013), https://app.box.com/s/snp377aehtxicqy4q6ym (https://app.box.com/s/snp377aehtxicqy4q6ym).

[6] Free State Foundation, *Response to Questions in the Fifth White Paper "Universal Service Policy and the Role of the Federal Communications Commission"* at 6 (Sept. 19, 2014), http://www.freestatefoundation.org/images/Response_to_Questions_in_the_F... (http://www.freestatefoundation.org/images/Response_to_Questions_in_the_Fifth_White_Paper_091914.pdf.)

[7] *Connect America Fund et al.,* WC Docket No. 10-90 et al., Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 18093, 18098-99, paras. 1225, 1249-50 (2011) (*USF/ICC Transformation Order and FNPRM*); aff'd sub nom., In re: FCC 11-161, 753 F.3d 1015 (10th Cir. 2014).

[8] Universal Service Reform, Accountability, and Efficiency Act of 2008, H.R. 6356, 110th Cong. § 2(e)(2) (2008), https://www.congress.gov/bill/110th-congress/house-bill/6356/text (https://www.congress.gov/bill/110th-congress/house-bill/6356/text).

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