

**Remarks of FCC Commissioner Michael O’Rielly
Before the Hudson Institute
June 25, 2019**

Thank you, Harold, for that warm introduction. It is a pleasure to be back at such a highly-respected venue, to discuss the Federal Communications Commission’s universal service policy, no less. While I am thrilled to be here, I will admit it is somewhat daunting to make this presentation in front of a Hudson expert with such a deep and firsthand knowledge of the textual meaning of the FCC’s universal service mandate. As one of the chief staff architects of the Telecommunications Act of 1996, and a Commissioner who served during the earliest years of its implementation, we could all learn a great deal from Dr. Furchtgott-Roth.

The policy of universal service—that all Americans ought to have access to basic telecommunications services—has been inherent to federal communications law since its earliest days, and a principle that I fully support. Under the 1996 Telecom Act, what was previously an implicit cross-subsidy system became an explicit federal program. Today, the Universal Service Fund, or USF, is funded through fees imposed on consumers’ landline and wireless phone bills and currently features four sub-programs dedicated to bringing connectivity to different segments of America: high cost areas; low-income consumers; schools and libraries; and rural health care providers.

While bringing service to these four types of constituents is part of our statutory mandate, I emphatically believe that one of our primary obligations as Commissioners is to protect ratepayers’ hard-earned contributions to the best of our ability. Thus, in my role as Commissioner, I have repeatedly led efforts to eliminate waste, fraud, and abuse in the USF, and ensure that subsidies only flow to those who absolutely need them. In working to implement better incentives and efficiency, I have also encouraged the Commission to establish an upper limit on USF spending. As the Commission has repeatedly increased spending in the individual sub-programs over the years, the burden levied on consumers has continually risen, and the contribution factor for the current quarter is at an all-time high of 24.4 percent. At my urging, the FCC is currently in the middle of a proceeding to establish a topline budget on the USF. While certain special interest groups have fiercely attacked any measure to impose fiscal discipline—after all, as author and pithy linguist Mason Cooley once said, “a budget takes the fun out of money”—this action is both necessary and overdue.

Before I delve into the need for a cap, a bit of history: those who have followed the factor over the years know that it did not reach its current level overnight. Rather, it has grown progressively, from 10.2 percent in the third quarter of 2005, 13.6 percent for Q3 in 2010, 17.1 percent for the same period in 2015, and now above 24 percent. There are multiple reasons for this phenomenon: a shrinking base from which contributions are assessed; the conversion of implicit subsidies to explicit programs; and new spending for various purposes. While many have focused on the erosion of the contributions base, that issue is largely a distraction: broadening the base wouldn’t truly address how much consumers pay but only the means for collecting payments. After all, almost all reform solutions seek to impose fees on services not included today.

Similarly, policies that reduced implicit subsidies, such as interstate access charges, and in turn increased explicit subsidies, were largely a wash: the higher corresponding contributions factor was more than likely offset by lower rates elsewhere. In contrast, one aspect of the factor’s growth that *has* significantly impacted consumers is new USF spending: added funding authorized by the Commission—no matter how meritorious—requires additional money from consumers. And, needless to say, these increases have been dramatic: disbursements have grown from approximately \$6.5 billion in 2005 to an estimated \$10.2 billion for 2019.

The Need for a USF Budget

So why pursue an overall USF budget and what benefit would it bring?

First and foremost, a budget is necessary to protect the investments of ratepayers who pay for our programs. While there's never any shortage of special interest groups lobbying for additional spending, ratepayers are much less likely to spend time and resources defending their own interests. Quite reasonably and appropriately, they're focused instead on their everyday, busy lives. Those consumers deserve an agency that represents their interests as well—especially given the regressive nature of USF fees and their disproportionate burden on lower- and middle-income Americans. Since the fee is generally spread among consumers on an equal and agnostic basis, low-income households pay a far greater share of their income to the USF than their high-income counterparts. In fact, the lowest-income 10% of households pay *12 times more* than the highest-income 10% as a percentage of their income.

While a budget is by no means a comprehensive fix for the problem of an ever-increasing contributions factor, it would provide ratepayers with more stability in terms of the overall amount they'll be on the hook for every month. Moreover, determining this maximum level is also a necessary precondition to any effort to reform the FCC's method for assessing USF contributions.

Second, a topline budget would force the FCC to consider the whole USF when increasing program spending. While the Commission has repeatedly increased spending in each of the sub-programs over the years, it has done so without the constraints of a topline budget. In turn, it has made these decisions without considering the effect of spending decisions for the whole USF enterprise and how to fairly and efficiently allocate scarce funds among the four programs. That is not a responsible way to run an \$11 billion-plus fund, and not the way the vast majority of federal government programs—or American businesses and families, for that matter—operate.

I have frequently been asked whether there is a true need to have a topline budget if each of the individual programs is capped. While I strongly support capping each of the individual programs and would certainly welcome the establishment of a self-enforcing budget on Lifeline—the only program that currently lacks one—an overall budget serves a different purpose. It would require the Commission to examine the USF at a macro level and encourage debate about priorities for the fund as a whole before additional spending is authorized.

Third, an FCC running up against a cap would have greater incentive to eliminate inefficiencies that detract from achieving the program's mission and value. This is especially pertinent given the USF's storied history of waste, fraud, and abuse. While I have pushed reforms to reduce wasteful spending particularly in the High Cost program, and the Chairman has made strides to improve accountability, evidence of inefficiencies, fraud, and duplicative spending across certain parts of the USF is alarming, and much work remains. A budget would help to promote better management and oversight.

Fourth and finally, a budget would help protect universal service. One misconception spread by special interest groups in response to the NPRM was that a USF budget would undermine broadband access and create the "Hunger Games" scenario pitting various interested constituencies against each other. Nothing could be further from the truth. The proposed budget of \$11.42 billion is more than \$3 billion above current program disbursements and would be indexed to keep pace with inflation. That leaves room for reasoned and justified disbursement increases in the future. In other words, rather than provoking a fight to the death, this NPRM provides plenty for all. And, according to projections cited in the item, this substantial cushion will remain for many years to come. Moreover, and I think this is a very important point, the Commission would in no way be precluded from voting to raise the budget, should it someday see a need to do so. However, such a decision would require a thoughtful notice and comment

process and would be much more transparent and accountable than the status quo. I do not believe that any future Commission would hesitate to raise the budget cap should the record reveal a pressing need for such an action.

The Pernicious Consequences of USF-Funded Overbuilding

Returning to the topic of USF waste, one specific benefit of having an overall cap is that it would encourage the Commission to eliminate inefficient and duplicative spending among the programs to a much greater extent. As I have repeatedly pointed out in the past, every ratepayer dollar wasted on overbuilding broadband networks comes at the expense of consumers who still lack broadband access. While the country has seen great progress in deploying broadband, too many communities still lack even dial-up Internet and connecting those unserved Americans should be our chief priority.

This stands in sharp contrast to certain advocates who would rather direct scarce USF dollars to overbuilding—or, in their Orwellian-speak, promoting “greater competition” for consumers. Make no mistake: using federal subsidies to enable artificial competition does not help consumers or promote long-term competition. Rather, it undermines private incentives to invest in and upgrade broadband networks, distorts competitive outcomes, and makes it more expensive to connect Americans living in the most remote areas. In other words, government-subsidized overbuilding harms broadband access in rural America.

Take the case of several USF-supported broadband providers in Texas. Earlier this year, a group of rural rate-of-return carriers from that state informed me that their existing fiber networks were being overbuilt by E-Rate-funded Wide Area Networks, and that they had lost some of their school anchor customers as a result. Due to a loophole in the E-Rate rules, school district consortia had manipulated the competitive bidding process to ensure that funding went to build new wide area networks covering entire school regions, each covering well over ten thousand square miles, even though multiple fiber-based providers were already serving the individual schools within the regions. Given the large geographic scope of the projects and the short window to respond with a bid, small rate-of-return carriers didn’t stand a chance. This overbuilding scheme has created serious financial problems for those providers and undermined their ability to build out to more remote areas in their communities.

Beyond harming rural broadband deployment, intra-USF overbuilding also creates unacceptable burdens for USF ratepayers. That’s because any dollar that a rate-of-return provider loses to an overbuilder will inevitably be recouped from the High Cost program. While USAC insists that it only funds new fiber builds when doing so is the most “cost-effective” option, it does not inquire into whether a given fiber build duplicates another provider’s network—even if the duplication involves a network funded under USAC’s own High Cost program. That analysis is breathtakingly myopic: whether a given fiber build is cost-effective cannot be determined solely through the lens of E-Rate but must consider the overall costs to the whole USF. Due to our failure to pursue this analysis, it is extremely likely that certain E-Rate applicants raise the overall cost for USF without adding any corresponding benefit to consumers.

USAC’s troubling inability to identify and prevent this overbuilding problem largely stems from the previous Commission’s questionable decision to vastly expand support for E-Rate special construction projects, including by permitting funding of applicant-provisioned networks. As I cautioned at the time, this policy would likely lead to duplicative spending and we had not established nearly enough safeguards to protect against waste—an outcome that has clearly been borne out. Moreover, it may only be a matter of time before advocates return to their recent call that these new stand-alone E-Rate networks be allowed to provide service to non-E-Rate eligible recipients: first, the school’s surrounding neighborhood or perhaps just teachers’ houses, then eventually wherever the school district or its hand-

selected provider would like to serve, thus, in turn creating an existential threat to privately- and high cost-funded competing networks.

Perhaps if there had been an overall USF cap in 2014, the Commission would have been more inclined to evaluate the broader consequences of the special construction rules or at least mandate better coordination among the USF sub-programs. While establishing a cap now won't change the past, it would at least encourage the Commission to take a more holistic view of its policies and prevent us from making similar mistakes in the future.

Preventing Duplicative Spending by Other Federal Agencies

To stretch public funds as far as possible and minimize waste, it is equally crucial that federal agencies avoid duplicating each other's broadband subsidies. The FCC is arguably the best-positioned entity to award broadband subsidies in the most efficient manner, especially given its successful implementation of the Connect America Fund Phase II multi-round reverse-auction. However, to the extent that other agencies such as the Department of Agriculture (USDA) and the Department of Commerce are allocated new funding for broadband buildout, I have repeatedly urged Congress to spell out clear rules for agency coordination, to prevent cross-agency overbuilding and ensure that funding is directed only to those Americans without service.

Thus, while I am grateful that the USDA has coordinated with the FCC in implementing the Rural Utilities Service's ReConnect program, I remain concerned that some of the criteria developed will lead to undermining the Commission's CAF investments. For example, while the ReConnect program rightly eliminates areas won in the CAF II auction from eligibility, other areas receiving CAF support and subject to defined buildout and support obligations, such as areas served by rate-of-return carriers receiving model-based or CAF broadband loop support, are not explicitly ineligible under current program criteria.

Further, I remain concerned as to whether the application process will truly stretch dollars as far as possible and direct support to where it's needed most. Consider that under the current points-based evaluation criteria, which is problematic in and of itself, a disproportionate number of points will be awarded to applicants proposing to build networks capable of providing 100 Mbps *symmetrical* service to all premises. It strains credibility that this threshold would be necessary or cost-effective for most consumers, and I worry that encouraging gold-plated projects will come at the expense of Americans who will continue to remain without service.

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Throughout my career at the Commission, I have been committed to improving broadband access for unserved communities, stretching federal dollars as far as possible, and protecting the interests of those who pay into the system. While the FCC has made improvements to its broadband subsidies over the years, truly eliminating inefficiency and waste will take a lot more work, both inside and outside the agency. Establishing an overall USF budget is a crucial part of this effort and I am proud to serve as the lead advocate for the rulemaking. Thank you for your attention and I look forward to answering your questions.