

Brief

House Bill 789/Senate Bill 332

Affordable Local Service and the Universal Service Fund

By Bill Peacock

BACKGROUND

Rates for Texas basic residential telephone service, including the federal subscriber line charge, range from about \$13.82 per month in rural areas to \$16.72 in urban areas. But long-run incremental costs for service range from \$11.84 per month in the most densely-populated areas to more than \$250 per month in rural areas. Approximately 95 percent of all basic residential lines are subsidized. Sources for the subsidies include added features, business service, long distance and the Universal Service Fund.

In 2001, the Texas Universal Service Fund distributed approximately \$613 million. The lion's share of the money – \$539 million – went to high cost and small rural carriers. This figure is almost equal to the large incumbents' estimated \$600 million total loss on local residential service, and generally represents a subsidy from urban and suburban customers of large incumbents, long-distance users, and wireless subscribers to customers of high cost and small rural carriers.

In addition to being an income transfer from one set of consumers to another, the USF causes price distortions and concomitant reductions in consumer welfare that occur because the current percentage assessment increases the cost of every additional wireless and long distance minute. In a January 2005 study for the Foundation, Robert Crandall and Jerry Ellig estimated that the USF reduces the welfare of consumers and providers by \$177 million annually.

POLICY RECOMMENDATIONS

Reducing USF subsidies would benefit most Texas consumers. Recognizing the Texas policy of supporting telephone service in high cost areas, the Foundation suggests that the Public Utility Commission study (or commission a study) and make recommendations on basic residential telephone rates and subsidies from the USF. Specific charges could include:

- ◆ Determining how to reduce USF assessments by more careful targeting of payments based on the number of households served who cannot afford phone service – currently 90 percent of USF payments instead go to high cost and small rural carriers without regard to need.
- ◆ Studying how to reduce USF assessments by determining an affordable level to which those basic rates that are not deregulated could rise.
- ◆ Assessing how the Lifeline program can be better utilized in place of the USF to meet the needs of Texans who need assistance paying their phone bills.
- ◆ Assessing the potential for funding the USF by some means other than a percentage assessment, which distorts telecommunications prices.