

Special Review Memorandum

Re: USF Reforms: Reassessing Schools & Libraries.

Foreword

Two years ago, you'll probably recall, the top Republican leadership of the House Energy & Commerce Committee was seriously proposing an end to the Federal Communications Commission's (FCC) Universal Service Fund (USF).

Texas Congressman Joe Barton -- then full Committee Chairman -- made two basic points. First, competition and free enterprise currently provide lots of other services to small town and rural America, he argued -- all without benefit of an \$8 billion a year, FCC-regulated, revolving fund. We don't have special funds to support rural cable, or rural television. Why rural telephone?

Second, wireless has obviously revolutionized the economics of providing telephone service -- and, many of those central city, oppressed minority, and other putative USF beneficiaries these days have their own cellphones. We don't have to subsidize them, Barton said -- they're willing and able to identify and satisfy their own communications needs.

Not Part of the Current Agenda

Needless to say, the Democratic ascendancy in the House of Representatives moved Mr. Barton's USF proposals far down the agenda. Chairman John Dingell has lots of other things to worry about -- keeping Speaker Pelosi and Congressman Ed Markey from destroying the U.S. car industry, for instance.

The same's true in the U.S. Senate, where Senator John Sununu and others had been willing to contemplate the "null set solution" to USF "challenges -- Alaska Senator Ted Stevens (and, Hawaii's Senator Dan Inouye) notwithstanding.

These days, both House and Senate have been looking at some aspects of the USF and its increasingly precarious base of support. The USF, remember, is supported mostly by the equivalent of an 11% "tax" on long-distance voice telephone calls -- a part of the market that's been shrinking in recent years. Commendably, the House Telecommunications & Internet Subcommittee has also examined the "eligible telecommunications carrier" (ETC) situation. This is where a state regulatory agency certifies that a wireless company is providing "universal service." That company's then reimbursed for its costs based on the local wireline carrier's cost, not its own.

A rural wireless company described the ETC arrangements as "like finding a \$20 on the ground." Ten years ago, only a nominal amount was flowing to ETC and wireless carriers -- less than \$100 million of the ±\$4 billion earmarked for high-

cost telephone service. Currently, however, something approaching \$1 billion is slated to be paid to ETC wireless carriers. It's one of the more successful "slant-drilling" propositions in regulatory history.

What About Schools & Libraries?

What's interesting about the current Congressional and administrative USF review, however, is how little critical attention the USF's massive Schools & Libraries Program has attracted.

This program, allotted some \$2.25 billion, was created by the 1996 Telecommunications Act. The idea was to jump-start Internet-based education -- by extending connections to virtually every classroom in the country. Before the law was passed, slightly less than half the schools and classrooms in the country had been "wired." Volunteer efforts such as "Net Day" had accomplished that. A lot of schools and libraries also had been connected to the Internet by virtue of cable franchise provisions.

But Congress in 1996 thought more was needed. The FCC followed through with the Schools & Libraries Program (they also set up a fund to underwrite the cost of "tele-medicine" in some cases, but not much emphasis was placed on that effort, at least until recently).

"Seed Money," Capital Grants & Operating Subsidies

Now, your Review's Telephone Bureau once asked one of the School & Libraries program's prime architects why the fund was set so high, when there wasn't all that much left to accomplish. We were told that the FCC -- and, Congress -- wanted to complete the "school wiring" effort quickly, and then contemplated the funding levels would scale down.

That's consistent with longstanding Federal grantsmanship, of course. Historically, there's been a distinction drawn between initial capital grants -- helping a community muster the money needed to put an expensive capability in-place -- and providing operating subsidies. True, it's not always that easy to implement this policy differential. What happens when the initial bus fleet breaks down, for instance -- or, the public television station antenna falls down? Do the Feds resolutely refuse to supply more bus or antenna grants -- and, in so doing, risk "negative statistics"?

But very Democratic budget philosophers Nancy Teeters, Alice Rivlin, and Charles Schultze have nevertheless said that an effort must be made to enforce this distinction. It's one thing for the national government to help a community put a capability in-place, they say. But if the community's unwilling even to contribute the operating costs, doesn't that then become something of an exercise in Federal "imperialism," where a capability is imposed on the locality?

The Situation Today

Well, today virtually every classroom and public library in the country has Internet connections supported by the FCC's Schools and Libraries program. They have servers, interior plant, some PCs, some other pieces of equipment. It's all there, installed. So, wouldn't it make sense for the Federal Government to consider how the initial grant program needs to be reformulated?

If computers and the Internet are worthwhile additions to the education process -- and, a majority of educators seem to believe they are -- then shouldn't education budgets carry that cost? We're spending \$500 billion a year, or so, on K-through-12 education, you know. Do you seriously think the national school enterprise isn't able to pick-up the annual operating cost of existing computer installations?

Consider, too, the overall fairness of supporting these educational endeavors through people's telephone bills. For decades, economists and policymakers bemoaned the "cross-subsidies" reflected in traditional telephone prices. Competition was introduced as an effort to "straighten out pricing signals" and "wring those inefficiencies" out of the telephone network. The argument was made that since the phone network was increasingly integrated with the economy, these inefficiencies would otherwise "ripple throughout our economy." Now, however, aren't we re-inserting precisely the same kinds of "hidden cross-subsidies"?

Perhaps this is necessary. A major "user group" absorbing public education services these days is "out-of-status" immigrants. In many communities, most property owners -- the folks who are taxed to support the public schools -- don't themselves consume the service. Maybe through "taxing" telephone services, immigrants can help pay for some of the substantial costs they're otherwise imposing.

Not On the Table Right Now

The magnitude of the School & Libraries Program isn't on the public policy table, at least not right now, is it? But shouldn't Congress and the FCC go back and look at this program, and ask whether it doesn't warrant substantial changes.

The fundamental goal of the program, remember, has been achieved. We have Internet capability in the classrooms of the nation. The question thus becomes whether a capital grants program should be converted to an operating subsidy program -- and, if so, how should that be accomplished? By burying the operating costs in telephone bills -- or, by separately accounting for that as part of the overall education effort.

Conclusion

If the School & Libraries program were teased out of the overall USF effort, the levy on long-distance phone calls could be shaved by perhaps 40% -- which is a lot. Alternatively, there'd be a lot more money available for other "seed money"

capital grants -- in aid of tele-medicine, for example. Relatedly, the long-term survival of a program which many believe is necessary -- preserving telephone service in rural, small town, and central city areas -- would be better ensured, wouldn't it?

The School & Libraries program, in conclusion, may well have been an outstanding idea -- more than a decade ago. But the program's goals have been accomplished. This aspect of the USF needs, therefore, to be reassessed and changed, now.

* * *