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**Court Ruling on USF’s Unconstitutionality Should Spur Reform in Congress**

**by**

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A July 24 *en banc* decision by the U.S. Court of Appeals for the Fifth Circuit held the Universal Service Fund’s (USF) contribution mechanism – or “USF tax” – violated the U.S. Constitution’s Legislative Vesting Clause. The next day, the challengers to the USF regime made a filing in support of the Supreme Court’s review of the USF’s constitutionality. And on July 31, *Communications Daily* reported that members of a bipartisan bicameral congressional USF Working Group are considering how those developments impact their ongoing reform.

But Congress shouldn’t wait for the Supreme Court to act. Congress should act promptly to make the USF program fiscally sustainable and constitutionally sound for the broadband era. It should fund the USF via direct appropriations and intelligibly define broadband as a service eligible for support. If needed, Congress should consider requiring major online companies to make USF contributions under principles that limit subsidy amounts. Along with stronger curbs on waste and abuse, such reforms would preserve universal service, eliminate or at least reduce significantly the USF tax on consumers – which now stands at 34.4% – and enable future downsizing of the USF into a primarily voucher-like program supporting low-income consumers.

## **Need for Congress to Reform USF Intensifies Following Court Ruling**

Over the last several years – and in [several Perspectives from FSF Scholars papers](#) and [public comments](#) – Free State Foundation scholars have explained that reform of the USF subsidy system is urgently needed. The USF is outdated, no longer fiscally sustainable, and constitutionally dubious in its structure. The Fifth Circuit’s July 24 decision finding the USF’s contribution mechanism unconstitutional – including the USF tax line item on consumers’ monthly bills – heightens the urgency for reform.

In [Consumers’ Research v. FCC](#), the Fifth Circuit *en banc*, by a 9-7 vote, determined that Congress’s broad delegation of tax authority to the FCC under [Section 254](#) of the Communications Act, combined with the agency’s delegation of tax authority to the private Universal Service Administrative Company (USAC), amounted to a violation of Article I, Section I of the U.S. Constitution. That provision states: “All legislative Powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives.” A more detailed review of the Fifth Circuit’s decision and potential Supreme Court review of the constitutionality of the USF’s contribution mechanism is provided in my August 5 *Perspectives from FSF Scholars*, [“Fifth Circuit Rules USF Contribution Scheme Violates Legislative Vesting Clause.”](#)

## **Congressional Action Needed to Fix USF’s Fiscal Problems**

As the Fifth Circuit observed in *Consumers’ Research v. FCC*: “In 1995 the USF tax was \$1.37 billion.... [b]ut by the end of 2021, USAC ballooned the USF to over \$9 billion.” Also, interstate telephony revenues that form the program’s contribution base have declined significantly compared to years past. According to the Federal-State Joint Board’s [2023 Universal Service Monitoring Report](#), the USF contribution base declined to \$34.92 billion in 2022, down from \$64.19 billion in 2013. And the Fifth Circuit pointed out that “waste and fraud have also contributed to the USF’s astronomical growth.” The court cited several Inspector General (IG) and Government Accountability Office (GAO) reports and audits of the USF’s High-Cost, Lifeline, and E-Rate programs indicating gross levels of improper payments to telecommunications providers and subscribers, as well as a lack of effective controls.

Increases in annual subsidy distributions, decreases in telephony revenues, as well as wasteful spending have pushed up the USF tax rate substantially over two decades. This overburdens consumers of voice services. As the Fifth Circuit noted, the surcharge or USF tax rate on the interstate portion of consumers’ bills was just over 5% in 2000. For the third quarter of 2024, the rate is [34.4%](#). And [analysts](#) have predicted the rate soon will rise dramatically – up to perhaps 40%. Without a fix by Congress, future rises in surcharge rates most likely will crash the system.

## **Congressional Action Needed to Fix USF’s Constitutional Problems**

Added to the USF’s fragile financial outlook is the urgency of saving the program from the constitutionally defective aspects of the system’s structure identified by the Fifth Circuit in *Consumers’ Research v. FCC*. The court concluded that the broad delegation of taxing power to

the FCC under Section 254 of the Communications Act, in combination with the Commission's subdelegation of that power to the USAC, amounts to a violation.

Regarding public delegation by Congress to the FCC, the court determined Section 254 lacks any intelligible principle to guide and limit the agency's discretion in exercising the taxing power. Section 254(d)'s provision that USF funding should be "sufficient...to preserve and advance universal service" is devoid of meaning. This is because Section 254(d) is directly linked with Section 254(c)'s "amorphous" concept of "universal service" as "an evolving level of telecommunications services that the Commission shall establish periodically" and "consistent with the public interest, convenience, and necessity." As the court concluded, the combination of those provisions "amounts to a suggestion that FCC exact as much tax revenue for universal service projects as FCC thinks is good." In other words, the "FCC's universal service taxation is not formally limited by the amount it disburses on universal service projects."

Regarding private subdelegation by the FCC to the USAC, the court determined that it does not contain any limit on the size of the contribution amount for USF projects. Additionally, the court observed that "the contribution amount ultimately derives from the universal service demand projections of private, for-profit telecommunications carriers, all of whom have 'have financial incentives' to increase the size of universal service programs." It cited agency regulations requiring "nine of USAC's nineteen directors represent companies in the telecommunications industry who are compensated by the very same USF funds they raise" and "another seven represent the schools, libraries, health care providers, and low-income consumers who are direct recipients of USF funds." Moreover, the court found that even assuming, for the sake of argument, that the Constitution's Legislative Vesting Clause did not prohibit such a private delegation, nothing in Section 254 clearly authorized it.

### **Reform Options to Preserve and Modernize Universal Service**

The Fifth Circuit's decision in *Consumers' Research v. FCC*, and the potential Supreme Court review of the USF contribution mechanism's constitutionality, should accelerate efforts by Congress to modernize the USF system into a broadband-centric program that is financially stable, more efficient in its expenditures, and constitutionally sound in its structure.

Congress should expressly identify broadband services as supportable under the USF program. When Section 254 was enacted in 1996, Congress primarily had voice services in mind. There is now widespread agreement that universal service should support broadband access. Congress should replace the amorphous definition of universal service as an evolving level of services that are consistent with the public interest, and it should specify broadband Internet access services and voice services. Also, Congress ought to identify principles or specific criteria that would limit the amount or size of distributions to service providers or recipients. By making those important decisions explicit in the statute and not leaving them up to judicial inference or the discretion of the FCC, USAC, or the Federal-State Joint Board, Congress would alleviate public nondelegation concerns.

Additionally, Congress should reform the USF program by making direct appropriations to fund it. By making appropriations out of the Treasury periodically, Congress would decide subsidy

amounts and thereby alleviate constitutional concerns regarding the delegation of power identified by the Fifth Circuit. Unlike the workings of the existing contribution mechanism, Congressional appropriations constitute politically accountable decisions.

Moreover, appropriations are a preferable USF funding source to USF tax or surcharge line items. Surcharges are at odds with universal service goals because they increase prices for consumers and higher prices inhibit adoption of services like broadband, especially for low-income individuals. By funding universal service with congressional appropriations and removing surcharges, consumers would pay lower prices and be more likely to adopt services.

However, if Congress decides that direct appropriations need to be supplemented to cover ongoing operational expenses incurred by broadband providers, it should consider expanding the base of USF contributors. Congress could amend Section 254 to clearly include “Big Tech” web giants like Amazon, Apple, Facebook, Google, and Microsoft that provide advertising, web searching, social media, or e-commerce services and benefit immensely from universal access to broadband networks. Sufficiently intelligible principles or criteria could define what types of service providers should become USF contributors and how much they should contribute, using metrics such as annual gross revenues and providing for periodic adjustments. This approach would place some financial responsibility for maintaining universal service on companies that benefit the most from broadband connections. Also, this approach could allow surcharges to be significantly reduced and thereby provide relief to consumers.

The FCC could lay the groundwork for reform efforts by Congress. It likely has the authority to research contribution funding options and report findings to Congress. Absent Commission action on its own initiative, Congress could fast-track legislation such as the [FAIR Contributions Act](#) (S.586). If passed by Congress, the Act would require the FCC to examine and report on the feasibility of funding the USF with contributions from search engines, social media platforms, streaming services, app stores, cloud computing services, and e-commerce platforms.

Congress also ought to reform the USF with stronger measures to curb the waste, fraud, and abuse identified in numerous Inspector General and GAO reports identified by the Fifth Circuit in *Consumers’ Research v. FCC*. It should require the FCC to inquire into a broadband subsidy applicant’s legal, technical, and financial fitness before entrusting it with USF funds. By verifying such information, the Commission can help ensure a broadband provider’s ability to satisfy its obligations as a recipient of subsidies.

### **Unprecedented One-Time Broadband Subsidies Should Prompt Future USF Reforms**

In addition to immediate reforms to address fiscal and constitutional problems with the USF, Congress should plan a near-future reduction in the amount of annual USF subsidies once Broadband Equity, Access, and Deployment (BEAD) Program subsidies as well as other one-time subsidies have been dispersed and expended for network buildout. In the FCC’s 2022 [Report on the Future of the Universal Service Fund](#), the agency acknowledged that “[t]he Infrastructure Act and other legislation enacted in 2020 and 2021 provided unprecedented funding for broadband deployment, equity, affordability, and adoption.” It should be expected that the expenditure of over \$140 billion appropriated by Congress – in addition to the

approximately \$100 billion invested each year by private market wireline, wireless, and satellite broadband providers – should improve significantly broadband access shortly so that every location in America has access to a broadband connection. From that point, the High-Cost Fund ought to sunset or mostly wind down over 10 years to enable adjustment by providers to a more market-oriented environment. A sunset target date would create a realistic pathway to the goal of significantly reducing any remaining ongoing USF subsidy amounts.

Finally, Congress should plan for the future transition of the legacy USF programs into a voucher program for eligible low-income individuals to purchase broadband subscriptions. That transition ought to begin after the recent one-time subsidies appropriated by Congress have been distributed and expended on network infrastructure. The recently-expired American Connectivity Program (ACP) offers a model because it encourages consumer choice through broad provider participation and lack of minimum service requirements. The ACP model can be improved using vouchers instead of costly and paperwork-heavy reimbursement systems and should only support those truly in need. A USF program fit for the broadband era should make individual vouchers the exclusive, or at least primary, subsidy mechanism for ensuring that all Americans have access to broadband services.

## Conclusion

The Fifth Circuit’s decision in *Consumers’ Research v. FCC* identifies constitutional defects with the financially troubled USF program. The Fifth Circuit’s decision and potential Supreme Court review of the constitutionality of the USF should prompt Congress to expedite ongoing efforts to adopt legislation so that the program aligns with constitutional principles, is fiscally sustainable, and is modernized for broadband.

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## Further Readings

Seth L. Cooper, “[Fifth Circuit Rules USF Contribution Scheme Violates Legislative Vesting Clause](#),” *Perspectives from FSF Scholars*, Vol. 19, No. 26 (August 5, 2024).

Seth L. Cooper, “[FCC’s School Bus Wi-Fi Subsidy Lacks Statutory Support](#),” *Perspectives from FSF Scholars*, Vol. 19, No. 4 (February 1, 2024).

Randolph J. May, “[The FCC’s USF Report: Unprecedented Broadband Funding Requires Fundamental Universal Service Reforms](#),” *Perspectives from FSF Scholars*, Vol. 17, No. 42 (August 26, 2022).

Seth L. Cooper, “[Congress Should Consider Expanding Universal Service Contributions: FCC Poses a Potential Answer to USF’s Financial Problems](#),” *Perspectives from FSF Scholars*, Vol. 17, No. 41, August 23, 2022).