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**CLIENTS & FRIENDS ALERT**[1]

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**(Updated)**

# "A Tax by Any Other Name": Fifth Circuit Strikes Down the FCC'S Universal Service Fund (USF) Assessments - But grants the Agency's Petition for Stay.

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## I. What Happened?

On July 24, 2024, departing from conflicting decisions in other circuits and from that of its own panel in 2023, on review of *Consumers' Research et al. v. Federal Communications Commission*, the full (en banc) Fifth Circuit Court of Appeals found that the FCC's assessment and collection of Universal Service Fund (USF) fees was an unconstitutional "tax".[2]

On August 23, 2024, the FCC filed an unopposed motion with the Fifth Circuit Court for a stay of its decision on condition that the U.S. Government file a petition for certiorari (review of the decision) with the U.S. Supreme Court by September 30, 2024.[3] The court promptly granted the motion on August 26, 2024, stating that the stay will expire on October 1, 2024 – but that it will

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[1] While accurate to the best of our knowledge, this alert is for tutorial purposes only, not a legal opinion and is not to be treated as legal advice. Please contact us if you have any questions regarding this disclaimer.

[2] Consumers' Research et al. v. Federal Communications Commission, No. 22-60008 (5th Cir. 2024, July 24,(2024) ("Consumers' Research"). **https://www.ca5.uscourts.gov/opinions/pub/22/22-60008-CV2.pdf**

[3] Consumers' Research v. FCC, No. 22-60008 (5th Cir. Aug. 23, 2024). The FCC specifically requested the Court stay its mandate (that had been scheduled for September 16, 2024) pending the filing of the FCC's certiorari petition. Petitioners (Consumers' Research) stated that they did not oppose the stay on condition (to which the FCC agreed) that the U.S. Solicitor General file this petition by October 1, 2024.

"continue until the Supreme Court's final disposition" if the petition for certiorari is filed by the agreed upon date.[4]

1. Background.

Briefly, USF fees are assessed on the interstate and international revenue derived from the provision of "telecommunications services" (both mobile and fixed common carrier services), "telecommunications" (private carrier services, *e.g.*, private lines and "lit fiber" connections, among others),[5] and interconnected VoIP services – but not on unregulated information services, such as Internet access services. A private entity (Universal Service Administrative Company or "USAC") invoices and collects these fees from telecommunications carriers and certain other entities following instructions published by the FCC.[6] It is standard practice throughout the industry to pass these fees through to end users. The FCC, in turn, uses these "contributions" to subsidize telephone services to a variety of funds covering low income, rural and high-cost areas, schools, libraries, and rural healthcare providers. Importantly, USAC calculates these fees with input from telecommunications carriers based on reported revenue projections.[7]

2. The Fifth Circuit Court of Appeals Decision.

The Fifth Circuit Court majority (with seven judges dissenting) had granted a petition for review by a consumer research group and others that, among other arguments, said the calculation and collection of such USF by a private entity assisted by private telecommunications carriers, was an unconstitutional sub-delegation of agency taxing authority. The court agreed, holding that this "misbegotten tax" violated Article I, Section 1 of the U.S. Constitution and remanded the FCC assessment that was before the Court (First Quarter, 2022) to the FCC.

*Consumers' Research* creates a split with conflicting decisions in both the 6th and 11th Circuits. Given its importance – USAC collected $8 - $9 Billion in USF contributions from telecommunications providers in 2023 – and the grant of the unopposed motion for stay pending the petition for certiorari, the decision is highly likely to be reviewed by the U.S. Supreme Court.

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[4] Consumers' Research v. FCC, No. 22-60008 (5th Cir. Aug. 26, 2024) (granting stay of the court's issuance of its mandate pending the filing of the FCC's petition for certiorari).

[5] The enabling statute, 47 USC 254, and related FCC Rules, 47 CFR Part 54, were enacted and adopted as part of the 1996 Telecommunications Act reform legislation. Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (codified as amended in scattered sections of 47 U.S.C.). A non-exclusive list of entities required to contribute to USF is currently listed at 47 CFR §54.706(a).

[6] USF fees are calculated quarterly and annually by filing FCC telecommunications worksheets (Forms 499-Q, 499A) and paid annually. See https://www.fcc.gov/licensing-databases/forms. Carriers typically pass through the fees to their subscribers subject to a cap, "contribution factor", calculated by the FCC on a quarterly basis.

[7] *Consumers' Research* at 6 ("…the contribution amount ultimately derives from the universal service demand projections of private, for-profit telecommunications carriers….").

The controversial decision also suggests the need for long overdue USF reform legislation, not an easy task in today's fractious political climate.

## II. USF Fee vs USF Tax: Why it Matters

As the USF contribution rules are sometimes unclear, especially when applied to new technologies, disputes are common, often between contributors and the FCC Enforcement Bureau and sometimes between USAC and the FCC.[8] USF contribution rules are especially unclear when applied to IP-Enabled and other hybrid, technologically convergent services (services using IP technology).[9]

Prior to *Consumers' Research*, federal courts had ruled that the USF program is not a tax under the Origination Clause,[10] and had strongly suggested that it is not a tax under the Taxing Clause.[11] *Consumers' Research*, in contrast, following a lengthy analysis, holds that it is. If so, the holding implies that under tax law principles, the ambiguities in the USF contribution requirements would be construed in favor of those paying the tax.[12] Consequently, if *Consumers' Research* survives, among other major disruptions to the USF program, the FCC and USAC could find their determinations that much harder to defend.

## III. Impact of *Chevron's* Demise

The FCC's USF travails do not end there.

Prior to *Loper Bright Enterprises v. Raimando,*[13] agencies had broad discretion to carry out actions and decisions, to which courts generally had to show deference.[14] So long as an agency could provide a reasonable explanation of an ambiguous statute that the agency was charged with enforcing, courts would generally uphold the agency decision.[15] *Loper Bright Enterprises* changed

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[8] See, *e.g.*, In re Universal Service Contribution Methodology, Order, WC Docket No. 06-122, FCC 16-179 (adopted Dec. 16, 2016) (FCC reversing USAC decision that Cisco Web-Ex online collaboration service must contribute to USF and finding instead that it is an integrated information service).

[9] See generally, **In the Matter of IP-Enabled Services**, Notice of Proposed Rulemaking, 19 FCC Rcd 4863 (200 See In re Universal Service Contribution Methodology, Further Notice of Proposed Rulemaking, WC Docket No. 06-122, FCC 12-46, 27 FCC Rcd 5357 (2012) (released Apr. 30, 2012) at Par. 38 *et. seq.*

[10] *Texas Office of Public Utility Counsel v. F.C.C.*, 183 F.3d 393 (5th Cir. 1999) (stating that the Origination Clause that all "bills for raising revenue" (*e.g.*, taxes) must originate in the U.S. House of Representatives, whereas the USF originated in the U.S. Senate).

[11] *Rural Telephone Comm'n v. F.C.C.*, 838 F.2d 1307 (D.C. Cir. 1988); *Texas Office of Public Utility Counsel v. F.C.C.* The Taxing Clause provides that taxes are monetary obligations imposed arbitrarily, without regard to benefits bestowed by the Government on a taxpayer, solely based on property or income. It further provides that taxes may only be imposed by Congress. *Id.*

[12] *Gould v. Gould*, 245 U.S. 151, 153 (1917).

[13] *Loper Bright Enters. v. Raimondo*, 603 U.S. ___, No. 22-451, (2024); https://www.scotusblog.com/casefiles/cases/loper-bright-enterprises-v-raimondo/

[14] *Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837, 842–5 (1984).

[15] *CBS Corp. v. F.C.C.*, 663 F.3d 122, 145-6 (3d Cir. 2011).

all that by striking down this so-called "Chevron deference". The FCC no longer has the benefit of that doubt.

It is unclear (perhaps debatable) whether *Loper Bright* will have any impact on the likely disposition of *Consumers' Research* before the U.S. Supreme Court, as the Fifth Circuit court did not rely on *Loper* in reaching its decision. Still, in the future, whether *Consumers' Research* is upheld or not, FCC (and USAC) determinations of USF assessments – especially those involving fuzzy contribution rules for new technologies – will likely continue to see challenges.

Perhaps *Varian Medical Systems Inv. V. Commissioner*[16]is an omen. In its first major decision applying *Loper Bright*, the Tax Court unanimously ruled in favor of a corporate taxpayer claiming both a deduction and a dividend for certain foreign tax-credit, a temporary anomaly resulting from from two different effective dates of the controlling tax sections. The sloppily drafted mismatch created a "gap period" during which affected taxpayers were entitled to a windfall (both a credit and a dividend) for amounts paid for foreign taxes.[17] Applying *Loper Bright*, the Tax Court refused to give deference to the IRS' regulation attempting to reconcile the dates in the flawed legislation.

Similarly, without *Chevron's* protection, agency assessments that rely on ambiguous provisions of the governing USF statute[18]are no longer presumptively correct. To the contrary, if appealed, USF collection and payment disputes will be heard by an independent judiciary no longer deferential to agency interpretations. Ironically, if *Consumers' Research survives*, under tax law principles, these disputes will be resolved in favor of the contributors, not the FCC: in other words, turning *Chevron* on its head.

## IV. What if and What's Next?

Much depends on the anticipated (now likely) U.S. Supreme Court review, some would speculate sometime during the Court's annual term beginning in October 2024, with a possible decision in June or July of 2025. If reversed, the prior decision of its earlier panel (one supported by the *Consumers' Research* dissent) and those of the 6th and 11th Circuit would leave the FCC's USF enforcement discretion unhampered by pro-consumer tax law principles. But the implications of *Loper Bright* (no deference) remain. So are the FCC's (by some accounts confusing) USF determinations involving new technologies.

In other words, the disposition of *Consumers' Research* will not obviate the need for USF reform legislation. If it survives, the possible unravelling of the FCC's USF policy that has been a decades' long staple of the telecommunications industry will demand a legislative fix. But even if it does not, so does the uncertainty to FCC authority created by *Loper Bright*. A Congressional rewrite of USF, especially a Democratic one if they win in November, could possibly expand the

[16] 163 T.C. No. 4 (2024).

[17] Richard Rubin, Congress Put the Wrong Date in the Tax Law, Companies Are Reaping Millions, WALL ST. J. Aug. 31, 2024, https://www.wsj.com/politics/policy/tax-law-date-congress-companies-da8c24c5

[18] *See, e.g.*, In Re: Safeguarding and Securing the Open Internet, Report and Order, FCC 24-52; 89 FR 45404 (2024), Par.350 (FCC forbearing from "applying portions [sic] of [47 USC] sections 254(d)(g) and (k)" to broadband internet service providers but "otherwise" applying statutory universal service requirements).

contribution base. Critics have long argued that the exemption from USF and other common carrier regulation for mass market Broadband Internet Access Services and so-called "edge" providers ("Big Tech"), both of whom benefit from universal service and the USF program and whose market caps far exceed most of the current fund contributors, makes no sense. As such, much of the ultimate outcome of the USF program, and how it is to be funded and administered, will depend greatly on what happens in November.

## V. Our Next Webinar.

And all that confluence of uncertainty brings us to our next webinar, sponsored by Thomson Reuters/West Legaled Center, soon to be recorded on October 28, 2024. As always, we are privileged to have a panel of experts who will navigate the complex web of *Consumers' Watch*, *Loper Bright*, and other recent SCOTUS rulings chipping away at the so-called "administrative state." Here is a list of our distinguished Faculty and we hope you enjoy the webinar.

1. Kurt E. DeSoto
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6. Walt Sapronov, Sapronov & Associates, P.C. wsapronv@wstelecomlaw.com Co-chair;

A recording of the webinar will soon be available from Thomson Reuters. Stay tuned for details by visiting our website at www.wselecomlaw.com/events/.