

Is Obamaphone Good for the Poor? Maybe Not.

By Scott Wallsten and John Mayo

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The Obamaphone controversy—whether government should subsidize wireless phone service for the poor—has two great ironies. The first is that wireless subsidies, which are part of the Lifeline and Linkup programs, were actually begun under Republicans President Bush and FCC Chairman Kevin Martin. This irony has been well documented and thoroughly enjoyed by many liberals.

The second, which so far has flown under the radar, is that the dramatic expansion of the Lifeline program, from less than \$800 million in 2005 to \$2.2 billion in 2012, may not be a net benefit for the poor. It may seem counterintuitive that a program that provides subsidies could actually make people worse off, but welcome to the convoluted world of universal service.

The problem with the program isn't that it subsidizes phone service for the poor. In fact, academic and government research has shown time and again that the much larger subsidies to rural areas are largely ineffective while telecommunications subsidies targeted at the poor have increased (land-line) telephone adoption among low-income people.

No, the problem is that Lifeline subsidies are not funded by our relatively progressive income tax system, but by taxes all phone users, including the poor, pay to use their phones. In other words, the funding source of Obamaphone is highly regressive because the tax that funds it is the same regardless of the payer's income.

Thus, any poor person who does not receive subsidies either because he doesn't know about them or because he doesn't qualify is worse off when subsidies increase because the taxes on his phone service must also increase.

A second issue is whether subsidizing wireless phones increases wireless adoption by the poor. This turns out to be a very hard question to answer, and one that helps illuminate why economics is the dismal science. Low-income people have strong demand for wireless services. Data from the Centers for Disease Control show that more than half of all poor adults live in wireless-only households.

Normal people see high use of wireless by the poor and think it is a no-brainer to target subsidies for that service. Dismal scientists, on the other hand, wonder whether people with a strong demand for a service would buy it even without a subsidy. And if they would buy it anyway, then the subsidy itself has no effect on the targeted program's goal of enhancing telephone adoption.

That is not to say the subsidy has no benefits even if it does not boost wireless use. Because money is fungible, the phone subsidy may allow a household to allocate money elsewhere, and an extra ten dollars a month can make a big difference to many low-income people. Unfortunately, Lifeline isn't intended to be a generic welfare program. It is explicitly intended to make phone service more affordable. If it is making something else affordable, then it is not succeeding. And, as discussed above, due to the way the program is funded even the welfare benefits may not be net positive for low-income people.

To be sure, some of the big increase in spending was due to program mismanagement, such as not requiring providers to make sure that recipients were eligible or that each eligible household received only one subsidized phone. But the FCC is addressing those issues and noted that spending in 2012 was \$128 million less than it would have been otherwise due to better enforcement.

But whether the wireless Lifeline program increases wireless telephone adoption in a cost-effective manner is an empirical question and cannot be answered by ideology. Our history with targeted telecommunications subsidies tells us that it can be effective. Strong and growing demand for wireless

services by all segments of society tells us that it will have to target carefully in order to make a difference.

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