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Federal program buys cell phones for the poor.

By SCOTT CANON
The Kansas City Star

A cell phone in every pocket. And for growing numbers, it's free.

"It's a sign of the times," said Nicholas Eberstadt, a researcher at the conservative American Enterprise Institute and author of "The Poverty of 'The Poverty Rate.'" "

"When does a luxury become an absolute bare necessity?"

Roughly one in 10 American households qualifies for a direct phone subsidy. In a fast-growing number of states, including Missouri, that equates to a free cell phone.

It is both news and history — the extension of longstanding telephone subsidies for the poor, and cell carriers taking advantage of virtually guaranteed profits.

While cell companies see the federal Lifeline program as a way to scoop up hundreds of millions of dollars in business, the move has raised questions about the way Americans subsidize each other's phone service.

More than 2 million poor people have been given free handsets and prepaid cell service — albeit on the simplest of phones, often with barely an hour's talk time per month — as wireless carriers scramble for a toehold with a new class of customers.

Access to a cell phone appears to be drawing more low-income families to subsidized service, and to the marketplace of carriers TracFone and Sprint Nextel. Those firms stand to increase their profits even more by selling minutes to the poor beyond what the government provides.

It has also driven up spending on a longstanding subsidy. Between 2008 and 2009, spending on the phone program grew by nearly \$179 million. The portion of people using the federal government's Lifeline for cell rather than landline service rose to 30 percent from 4 percent.

Phone subsidies for low-income families are projected to rise \$200 million-plus more this year and total \$1.2 billion.

Advocates of the program, including the Federal Communications Commission and social service agencies, concede that the idea of free cell phones can drop jaws.

Yet in an age in which pay phones are an endangered species and finding work or managing child care and health care increasingly demands an electronic tether, they contend handing out cell phones might merely be pragmatic.

Evie Craig, who oversees services for the homeless at reStart Inc., said her shelter recently lost a pay phone. That, she said, effectively cut off people from practical access to a phone. Though clients of the agency can have the use of a voice mail, it is obvious to a prospective employer contacting an applicant about a job that the person is staying at a shelter, she said.

"And maybe that shouldn't matter, but it does," Craig said. "It's hard for people to get past the idea that somebody is getting a free phone, but it can still be a practical solution."

For generations, fees have been added to long-distance telephone bills under federal law to steer money to the Universal Service Fund. That money, in turn, has underwritten the least-profitable sectors of telecommunications, such as rural areas.

In 1984, the Democratic Congress and the Reagan administration agreed to establish the Lifeline program. It pays phone companies to discount the bills of poor families. That was augmented by the Telecommunications Act of 1996 that also directed money from the Universal Service Fund to provide more robust communications, and eventually Internet service, to schools, libraries, and rural hospitals and clinics.

For years, the mandated phone discounts to low-income households provided about \$10 a month per family in reduced landline bills.

Then came TracFone, the prepaid subsidiary of American Movil — the carrier owned by Mexican telecom mogul Carlos Slim. It proposed to the Federal Communications Commission that some of those subsidies be available for cellular service.

Give that \$10 a month to us, the company said, and we will give a free phone to any family that qualifies. Customers would gain the mobility of a cell phone. Instead of paying a reduced rate for a landline, the poor would pay nothing at all if they did not use their monthly allotment of 68 minutes.

The FCC gave its OK, and with gradual state-by-state approval, TracFone's SafeLink brand has moved across the country since 2008. It is now available to families in Missouri, 24 other states and Washington, D.C. TracFone plans to make the free phones available nationwide.

"We're able to create a profit off it. We created the business model off of the \$10 subsidy," said Jose Fuentes, director of government relations for TracFone.

Eligibility is the same as it has been for discounts to the poor that have been around for the last quarter-century. Although the income limits vary slightly by state, they are roughly the same as those for food stamps. The program is also open to the blind or those receiving disabled veteran benefits. (The income levels vary between states and allow for certain deductions, but the phones are generally available to a single person earning \$11,000 a year or a family of four bringing in \$22,000.)

Each eligible household is entitled to one free phone and service. TracFone's SafeLink accounts allow unused minutes to carry over indefinitely. If the minutes are used up, the phone is still good for 911 calls, and customers can purchase more time in advance at 10 cents a minute — compared with rates ranging from 15 to 33 cents on TracFone's other pay-as-you-go plans). Because it is a prepaid service phone, there is no way to go in debt by calling too much. The phone simply ceases to work.

The family cannot take both the cell service and a discount on its landline. After a year, the family must requalify for the service. If, say, mom has a job and the family earns too much to remain eligible for the service, it is free to keep the phone.

That leaves TracFone — which provides the service by buying access to AT&T and Verizon's cell networks — in a position to sell more prepaid minutes.

Overland Park-based Sprint has seen the prospects as well. The company launched its Assurance Wireless brand in December. (Sprint won't say how many customers have signed up for the service. TracFone's SafeLink website claims 2 million customers.) Assurance offers 200 minutes a month. Unlike Safelink, however, those minutes cannot be converted for text messaging or used on international calls.

Assurance is available in nine states, but not in Missouri or Kansas. It aims to operate in all 50. Once approved by state utility commissions across the country, the Sprint subsidiary would be eligible to give service to 35 million families and count on the government to cover their admittedly smallish bills.

"That is a good market and we think it has real promise," said Sprint Chief Executive Officer Dan Hesse.

Telecom analysts say that although profit margins won't approach what carriers can make off pricey, data-hungry smartphones, they still represent steady income.

"There will be very little marketing costs. Customer care issues probably aren't that big," said Rick Franklin, a market analyst at Edward Jones. "People will come to it for the free service and probably buy more. It's a way to get your foot in the door."

Even as the free cell offers have gained quick popularity, their cost remains dwarfed by the money passed out to smaller phone companies to subsidize service in rural areas. In 2009, for instance, the Universal Service Fund dished out about \$36.2 million nationally for free cell phones to the poor. The same year, it paid \$4.6 billion to keep down the cost of the rural telephone service for people of all income levels.

Yet it is the cell phones that have begun to renew debate about money doled out from the fund. At the libertarian Cato Institute, tax policy director Chris Edwards said the fund had developed an unhealthy life of its own.

"People get these fees on their bills and don't really understand where it's going," he said. "At the same time they're now subsidizing the cell phone industry. You could also subsidize everything that a low-income family does — their computers, cars, everything."

At the conservative Hoover Institution, welfare specialist Jeffrey M. Jones noted that more than 90 percent of Americans carry cell phones, including many poor people.

"Is this really a role the government needs to be playing?" he said. "Why not just let the market take care of this?"

The FCC, which approved adding cell phones to the subsidized program, sees wireless service as increasingly the norm in a country where nearly one in four households has dumped its landline. It sees the convenience and the avoidance of runaway phone bills — something that disappears with a prepaid service — as a way for poor families to control their budgets.

Those who work with the poor say a cell phone may be the difference between landing a job or not, hearing from a child's teacher, or being able to call for an ambulance.

"When somebody is trying to get a job and keep their life together," said John Hornbeck of Episcopal Community Services in Kansas City, "having some kind of telephone contact becomes absolutely essential."

SafeLink Wireless

The SafeLink brand is available to families living in Missouri; 1-800-977-3768; www.safelinkwireless.com.

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