



of the fee as an administrative cost. The fees collected are deposited to the Commercial Mobile Radio Service Emergency Telecommunications Fund. Moneys in the fund are distributed to those state and local government facilities that are responsible for receiving 911 calls and dispatching public services to appropriate public safety agencies. These facilities are referred to as public safety answering points, or "PSAPs." While a few counties and cities operate a PSAP alone and some counties have joined together to form regional 911 boards, most PSAPs serve a county and one or more cities.

**2006 Amendments.** Wireless services are acquired on either a prepaid or postpaid basis. A postpaid customer receives a monthly bill, but a prepaid customer has a cell phone that is programmed with a set number of minutes for which the customer has already paid. The prepaid services are typically sold through third parties at a variety of retail outlets including stores, markets, gas stations, pharmacies, and vending machines. The customer's phone does not automatically renew those minutes and there is no monthly billing. The providers of prepaid services complained that this lack of a billing relationship created an administrative problem for them, and most providers of prepaid services took the position that the surcharge did not apply to their prepaid subscribers, and they ceased remitting the 911 surcharge to the CMRS Board. As a result, the CMRS Board sued two providers, Virgin Mobile and TracFone, in Jefferson Circuit Court. The TracFone litigation, however, was ultimately removed to U.S. District Court. In both cases, the trial courts ruled that the 1998 legislation required providers of wireless service to collect or remit the 911 surcharge of 70 cents per month with no distinction between prepaid and postpaid subscribers. In the Virgin Mobile case, the Kentucky Supreme Court held that Virgin Mobile and other pre-paid mobile phone providers were not required to collect the service charge owed customers prior to effective date of the 2006 amendments. The duty of cell phone providers to collect the service charge after the 2006 amendments was not contested. In the TracFone case, the U.S. Court of Appeals for the Sixth Circuit upheld the trial court's finding that TracFone improperly withheld payment of 911 service fees to the CMRS Board. As a result of this ruling, TracFone has paid more than \$4 million, of which \$2.9 million will be distributed to PSAPs across the state.<sup>1</sup>

**In 2006, the General Assembly amended KRS 65.7635 to provide alternatives to the 911 wireless surcharge for prepaid service providers:**

- (a) Deduct the value of the fee from the customer's account each month if there is a sufficient positive balance, also known as the decrement method.
- (b) Provide payment based on an average revenue per user formula: take the total revenue earned by prepaid subscribers and divide by \$50 and then multiply the quotient by 70 cents. This formula assumes an average subscriber bill to be \$50.
- (c) Permit the CMRS Board to promulgate an alternative by regulation.

The CMRS Board declined to promulgate a regulation to provide the third option. At least one company has refused to remit until the third option is available and is involved in one of the lawsuits previously mentioned. While AT&T uses the first option, most in the industry have chosen the second option, the average revenue per user option. The CMRS Board indicates they

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<sup>1</sup> February 26, 2014 and February 6, 2015 meetings with Joe Barrows, Executive Director, Kentucky Commercial Mobile Radio Service (CMRS) Board.

believe the formula in the second option, which is based on an assumption that the average monthly expenditure for prepaid subscribers is \$50, is flawed<sup>2</sup> since the average monthly cost for prepaid phones is actually about \$20.<sup>3</sup> The result, as noted by the CMRS Board, is that prepaid phones are generating less financial support for 911 than postpaid subscribers.

It should be noted that providers of prepaid wireless service pay the fee out of their own revenues, and while the cost may be built into a wholesale price, providers generally are not recovering the fee directly from its customers.<sup>4</sup>

**Program Review Study.** The Legislative Research Commission's Program Review and Investigations Committee adopted a report in December 2011 relating to funding for 911 services. One of the areas reviewed in the study was the 911 surcharge for wireless prepaid and postpaid subscribers and the formula discussed earlier:

Some prepaid providers remit far less than 70 cents for their prepaid subscribers under the average revenue per user option. Based on a widely cited industry figure, providers using this option remit an average of 38.5 cents per prepaid device.<sup>5</sup>

The reason for the average revenue per user formula/option was the assumption that some prepaid providers did not know how many devices are in the state. However, the Program Review and Investigations Committee study noted that method may no longer be needed since prepaid providers have been submitting customer counts to the CMRS Board.<sup>6</sup>

The Program Review and Investigations Committee report did not make specific recommendations on funding changes because of a lack of information available about the full cost of 911 services and the contribution of each revenue source toward that cost. The report includes a recommendation that the CMRS Board compile a complete statewide 911 financial statement showing all costs and revenues applied to 911 services.

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<sup>2</sup> February 26, 2014 meeting with Joe Barrows; February 17, 2015 telephone conversation with Joe Barrows.

<sup>3</sup> Federal Communications Commission, Annual Report and Analysis of Competitive Market Conditions with Respect to Mobile Wireless, Including Commercial Mobile Services, March 21, 2013, p. 283.

<sup>4</sup> Kentucky Program Review and Investigations Committee report, "911 Services and Funding: Accountability and Financial Information Should be Improved," adopted December 8, 2011, pp. 55, 130.

<sup>5</sup> Kentucky Program Review and Investigations Committee report, p. 34.

<sup>6</sup> Kentucky Program Review and Investigations Committee report, p. 56.

### Part III: Fiscal Explanation, Bill Provisions, and Estimated Cost

**The fiscal impact of HB 418 is expected to be positive. An estimated \$15 million in new revenue to support 911 operations is expected if the bill is passed with its current requirement to raise the service fee from .70 cents to \$1.00.<sup>7</sup> The current .70 cent fee generates approximately \$25 million per year.<sup>8</sup> Further, the repeal of cost recovery provisions in KRS 65.7631 could allow approximately \$4.25 million to be redirected to local governments and for the next generation 911 fund.<sup>9</sup>**

According to the CMRS Board, **of the three main sources of 911 revenue (landline fees, cell phone fees, and local government appropriations)**, revenue from cell phones accounts for less than 25 percent of total 911 revenues.<sup>10</sup> The prevalence of cell phones is problematic in two ways. First, many Kentuckians are abandoning landline phones in favor of cell phones. Secondly, the fastest growing segment of cell phone users are those who use prepaid phones. As previously stated, the 2006 Amendments have created a disparity between prepaid and postpaid phones as prepaid phone usage has produced less revenue than postpaid phones. According to KLC, local governments have lost approximately \$21 million in prepaid wireless revenue. All total, KLC estimates that local governments have lost \$42 million in revenue since the enactment of the 2006 amendments.

In an effort to alleviate this disparity between prepaid and traditional cell phone usage, HB 418 provides, in Section 8, that providers of prepaid services shall remit the equivalent of the statewide wireless fee in one of two ways. The first method, which involves new statutory language, requires the provider to multiply the service charge by the number of its active connections within the state. The provider is then required to remit the resulting amount to the CMRS board. The second option involves dividing the total revenue earned by prepaid subscribers and dividing by \$20. That quotient is then multiplied by the HB 418's new service charge, \$1.00. This second formula already exists in the statute, but HB 418 assumes an Average Revenue Per User (ARPU) of \$20, which reflects a national average.<sup>11</sup> The original assumption of \$50 failed to produce the revenue that had been expected if each prepaid phone had paid the current .70 cent monthly fee.<sup>12</sup>

**Relevant Provisions.** Among HB 418's other sections that directly relate to the impact on local government are the following:

Section 2 provides the definitions for key words and phrases used throughout the bill. Among the terms defined are "911 emergency service," "CMRS," "Local government," and "Voice over Internet Protocol (VoIP)."

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<sup>7</sup> February 26, 2014 meeting with Joe Barrows; February 17, 2015 telephone conversation with Joe Barrows.

<sup>8</sup> *Id.*

<sup>9</sup> Informational Bulletin prepared by Kentucky League of Cities, Kentucky Association of Counties, and Kentucky Emergency Number Association/Association of Public Communication Officers (KENA/APCO); February 26, 2014 meeting with Joe Barrows; February 13, 2015 email from KLC.

<sup>10</sup> March 3, 2014 email from Joe Barrows; February 17, 2015 telephone conversation with Joe Barrows.

<sup>11</sup> February 13, 2014 meeting with representative of KLC and KENA/APCO; February 17, 2015 telephone conversation with Joe Barrows.

<sup>12</sup> *Id.*; February 26, 2014 meeting with Joe Barrows.

Section 3 specifically requires any “telecommunications provider” (an undefined term) that provides VoIP services for a fee to collect the 911 charge and remit it to the local government. This section also limits the use of 911 service charge revenues to be used “solely for the establishment, operation, and maintenance of 911 emergency services,” subject to the requirements of 202 KAR 6:090.

Section 5, as alluded to previously, raises the CMRS service charge to \$1 from .70 cents, which has been the rate since 1998. However, this section also requires that this rate be indexed to the Consumer Price Index, unless otherwise directed by the General Assembly. Section 5(15) also adds “next generation 911 systems” as an additional platform that is required to be compatible with wireline E911 systems.

Section 6 amends KRS 65.7630 to require wireless providers to report to the CMRS Board on a quarterly basis the number of active CMRS connections in each zip code in the state for each month of the quarter.

Section 7 amends the CMRS distribution formula in KRS 65.7631 to encourage more consolidation of PSAPs and to implement next generation 911 capacity. First, Section 7 increases from 10% to 20% the amount of total monthly CMRS fund revenues under that KRS 65.731(2)(a) requires to be reserved for disbursement by the board. New language is also inserted that spells out how that money is to be apportioned. The apportionment formula is also changed in Subsection (3)(b) which requires 50% of those reserved funds to be distributed according to a method chosen by the board which is based on the wireless workload of PSAPs. The original percentage was 40%.

Further, in addition to establishing certain percentages for grants and the implementation of next generation technology, Section 7 increases the consolidation reimbursement to \$150,000 per PSAP and increases the county maximum to \$300,000. Section 7 also amends KRS 65.7631 by deleting the language for the cost recovery provision that required CMRS service providers (i.e., cell phone companies) to be reimbursed for the cost of complying with wireless 911 system requirements. This equipment is now in place, thus this fund is no longer needed. **It is estimated that the repeal of this cost recovery provision would allow approximately \$4.25 million per year to be redirected to local governments and to implement next generation 911 capacity.**<sup>13</sup>

**Data Source(s):** LRC Staff; Kentucky League of Cities; Kentucky Association of Counties; Commercial Mobile Radio Service Board; Program Review and Investigations Committee Study, adopted December 8, 2011; Federal Communications Commission Annual Report on Mobile Wireless Services, March 21, 2013

**Preparer:** Josh W. Nacey      **Reviewer:** MCY      **Date:** 2/18/15

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<sup>13</sup> *Id.*; Informational Bulletin prepared by KLC, KACo, and KENA/APCO; February 26, 2014 meeting with Joe Barrows.