



## **States Target Cell Phones for a Stealth, Burdensome Tax**

*Fiscal Fact No. 116*

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January 18, 2008

### *Cell Phones Are Multiplying, and So Are Cell Phone Taxes*

In the last decade, the number of U.S. cell phone subscribers has quadrupled, from 55 million in 1997 to over 250 million in 2007. That period has also seen a fall in landline telephones (the number of which dropped to 170 million), and 2007 marked the first year that Americans spent more on cell phones than on landlines.<sup>1</sup>

This trend toward cell phones has not gone unnoticed by state and local governments, which have targeted cell phones for higher taxes. These state and local levies averaged 9.04 percent in 2005, according to the Council on State Taxation, with 20 states charging a tax of 10 percent or more. Taking into account the infamous federal telephone excise tax (dating to the Spanish-American War and partly repealed in 2006), some cell phone subscribers pay more than 20 percent in cell phone taxes.<sup>2</sup> States favor the taxes because they can raise revenue in a relatively hidden way; Texas has even sued Sprint because it listed a state tax as a line-item in its bill.<sup>3</sup>

As a result, cell phones are taxed at a much higher level than other consumer items, even as much as or more than alcohol or cigarettes. Scholars from across the political spectrum have criticized telecom taxes as burdensome, regressive, and stifling consumer choice.<sup>4</sup> In response to this problem, Senators Jim DeMint, John McCain, John Sununu, and Gordon Smith introduced a bill in 2007 that would bar new cell phone taxes with rates higher than comparable products. The bill, the Cell Phone Tax Moratorium Act, had passed committee the previous year but died before reaching a floor vote.<sup>5</sup>

Because each state and many localities can impose cell phone taxes, and because they can be imposed as a percentage or as a flat rate, there are numerous taxes which vary widely. Researchers have found it difficult to create a database of cell phone taxes, and cell phone companies have encountered similar problems in calculating the taxes. This can be a serious

problem for cell phone businesses, because they collect the taxes from subscribers and can be held legally accountable for any mistakes—both over-collection and under-collection.

### **Cell Phones Can Only Be Taxed In the "Place of Primary Use"**

Even if applying the rate and collecting the tax owed were easy, determining which tax should apply to a particular cell phone user remains difficult. Which state should be able to tax a Florida resident who buys a cell phone there, moves to Idaho, but calls friends in Georgia more than anyone else?

Attempting to address this problem in an increasingly mobile world, Congress passed the Mobile Telecommunications Sourcing Act of 2002. That law stated that a cell phone subscriber is liable for cell phone taxes only in his or her "place of primary use."<sup>6</sup> The "place of primary use" is determined by the cell phone company based on the address provided by the subscriber, and cannot be overruled by a state taxing authority.<sup>7</sup>

Interestingly, some cell phone companies (including Verizon) link cell phone taxes with the area code of the phone number, rather than later changes to billing addresses (which Sprint, for instance, uses).<sup>8</sup> So when the Florida resident moves to Idaho (which has relatively low cell phone taxes), he may still pay Florida taxes if he keeps his Florida area code. In 2005, a Los Angeles-based reporter for *Forbes* magazine described his "success" in saving cell phone taxes by switching to an Idaho cell phone number.<sup>9</sup> Unless a consumer is vigilant, he or she could even end up paying taxes to more than one state.

### **Conclusion**

Making cell phone calls nationally may be getting easier, but paying cell phone taxes is not. State and local governments should not single out one product for stealth tax increases, as they are doing with cell phones. Such actions distort market decisions, violating the sound-tax-policy principle of neutrality. Cell phone users are often overtaxed relative to consumers of other goods, and at risk of double taxation. Finally, the wide number of taxing authorities and the wide variety in rates makes tracking problematic and burdensome.

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### **Notes**

1. "Cell phone spending surpasses land lines in U.S.," Associated Press, Dec. 18, 2007, <http://articles.moneycentral.msn.com/Investing/Extra/CellPhoneSpendingSurpassesLandLinesinUS.aspx>. See also "Spending on Cell Phone Services Rapidly Approaching That of Residential Phone Services," U.S. Department of Labor Bureau of Labor Statistics, at <http://www.bls.gov/cex/cellphones.htm>.

2. See Andrew Chamberlain, "Are Cell Phone Taxes Good Tax Policy?," Tax Foundation Tax Policy Blog, Jun. 16, 2005, <http://www.taxfoundation.org/blog/show/548.html>; Dennis Cauchon, "City, state cell phone taxes on the rise," *USA Today*, May 8, 2005, [http://www.usatoday.com/news/nation/2005-05-08-cellphone-taxes\\_x.htm](http://www.usatoday.com/news/nation/2005-05-08-cellphone-taxes_x.htm).

3. See Andrew Chamberlain, "What 'Economic Incidence' of Business Taxes Looks Like," Tax Foundation Tax Policy Blog, Jan. 18, 2007, <http://www.taxfoundation.org/blog/show/2158.html>; "Texas AG Sues Sprint Nextel Unit For Deceptive Billing," *Kansas City Business Journal*, Feb. 6, 2007, <http://www.bizjournals.com/kansascity/stories/2007/02/05/daily21.html>.

4. See Katherine Barrett and Richard Greene, Pew Center on the States, "Growth & Taxes: Why Outdated State Tax Systems Undercut Economic Vitality and What States Can Do About It," *Governing Magazine*, Jan. 18, 2007, <http://www.governing.com/articles/1taxmain.htm>; David Tuerck, Paul Bachman, Steven Titch, and John Rutledge, "Taxes and Fees on Communication Services," The Heartland Institute and Beacon Hill Institute at Suffolk University, April 2007, at <http://www.heartland.org/article.cfm?artId=21102>.

5. See Anne Broache, "Bill Seeks To Curb Cell Phone Taxes," *CNET News*, Jan. 5, 2007, [http://www.news.com/8301-10784\\_3-6147623-7.html](http://www.news.com/8301-10784_3-6147623-7.html).

6. See 4 U.S.C. § 122(a)(2).

7. *Id.* See also 4 U.S.C. § 124(8).

8. See, e.g., Scott Wooley, "How to Duck Cell Phone Taxes," *Forbes*, Jun. 7, 2005, [http://www.forbes.com/2005/06/06/cz\\_sw\\_0606cellphone.html](http://www.forbes.com/2005/06/06/cz_sw_0606cellphone.html).

9. *Id.*

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