TAX FOUNDATION
January 30, 2013
No. 355
Fiscal Fact

State and Local Governments Impose Hefty Taxes on Cell Phone Consumers

Nebraska Consumers Face Highest Tax Rates; Average Consumer Pays 17% in Wireless Taxes and Fees

By
Joseph Henchman & Scott Drenkard

The number of U.S. cell phone subscribers has grown significantly in recent years from 48.7 million in 1997 to 321.7 million in 2012. That period has also seen a fall in landline telephones, with 34 percent of households now only using wireless phones.[1] This trend toward cell phones has not gone unnoticed by state and local governments, many of which have targeted wireless services for higher taxes.

U.S. wireless consumers pay an average 17.18 percent in taxes and fees on their cell phone bill, including 11.36 percent in state and local charges, according to a newly released study that identifies and calculates wireless taxes and fees.[2] In Nebraska, the combined federal-state-local average rate is 24.49 percent, and in six other states (Washington, New York, Florida, Illinois, Rhode Island, and Missouri) it exceeds 20 percent. Twenty-six states have average state-local wireless taxes and fees in excess of 10 percent, and taking into account the infamous federal telephone excise tax (dating to the Spanish-American War and partly repealed in 2006), cell phone subscribers in seven states pay more than 20 percent in taxes. (See the table for a full list.)

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[1] CTIA, *U.S. Wireless Quick Facts*, http://www.ctia.org/consumer_info/index.cfm/AID/10323;
U.S. Department of Labor, Bureau of Labor Statistics, *Spending on Cell Phone Services Rapidly Approaching That of Residential Phone Services* (Dec. 13, 2007), http://www.bls.gov/cex/cellphones.htm.
[2] Scott Mackey, *Wireless Taxes and Fees Continue Growth Trend*, STATE TAX NOTES (Oct. 29, 2012), http://services.taxanalysts.com/taxbase/stnmag.nsf/(ME/66+STN+321-1?OpenDocument&Login (subscription required). Data is provided from FCC studies and the wireless industry, and a methodology developed by the Council on State Taxation is used to calculate averages.

Cell Taxes and Fees Are Often Hidden, Enabling Excessive Rates

States favor cell phone taxes because they can raise revenue in a relatively hidden way. Texas even sued Sprint because the company listed a state tax as a line-item on its bill rather than hiding it from customers. Utah uses what they call a wireless "fee" to fund its poison control centers, but the levy is really a tax because the government service benefits the general public regardless of cell phone ownership or usage.

Seven states (New York, Kentucky, Indiana, North Dakota, Pennsylvania, Rhode Island, and South Dakota) impose sales taxes on wireless customers as well as gross receipts taxes on wireless service providers. Both taxes are ultimately borne by customers. Universal Service Fund (USF) charges are modest in most states but particularly excessive in Alaska (5.98 percent), Nebraska (4.37 percent), and Kansas (3.86 percent).

Table: Taxes and Fees on Wireless Service, July 2012

State	State-Local Rate	Combined Federal-State-Local Rate	Rank
Alabama	7.49%	13.31%	39
Alaska	12.09%	17.91%	15
Arizona	12.98%	18.80%	11
Arkansas	11.54%	17.36%	17
California	10.95%	16.77%	21
Colorado	10.82%	16.64%	23
Connecticut	7.41%	13.23%	40
Delaware	6.28%	12.10%	46
Florida	16.59%	22.41%	4
Georgia	8.78%	14.60%	29
Hawaii	7.53%	13.35%	38
Idaho	2.28%	8.10%	48
Illinois	15.94%	21.76%	5
Indiana	10.86%	16.68%	22
Iowa	7.95%	13.77%	34
Kansas	13.11%	18.93%	10
Kentucky	10.54%	16.36%	24
Louisiana	7.21%	13.03%	43
Maine	7.27%	13.09%	41
Maryland	12.77%	18.59%	12
Massachusetts	7.85%	13.67%	35
Michigan	7.69%	13.51%	37
Minnesota	9.53%	15.35%	26
Mississippi	9.23%	15.05%	27
Missouri	14.29%	20.11%	7
Montana	6.09%	11.91%	47
Nebraska	18.67%	24.49%	1
Nevada	2.13%	7.95%	49
New Hampshire	8.21%	14.03%	31
New Jersey	8.91%	14.73%	28
New Mexico	11.08%	16.90%	19
New York	17.85%	23.67%	3
North Carolina	8.51%	14.33%	30
North Dakota	10.96%	16.78%	20
Ohio	8.04%	13.86%	33
Oklahoma	11.48%	17.30%	18
Oregon	1.85%	7.67%	50
Pennsylvania	14.13%	19.95%	8
Rhode Island	14.68%	20.50%	6
South Carolina	10.07%	15.89%	25
South Dakota	13.13%	18.95%	9
Tennessee	11.63%	17.45%	16
Texas	12.15%	17.97%	14
Utah	12.67%	18.49%	13
Vermont	8.10%	13.92%	32
Virginia	6.60%	12.42%	44
Washington	18.62%	24.44%	2
West Virginia	6.38%	12.20%	45
Wisconsin	7.24%	13.06%	42
Wyoming	7.79%	13.61%	36
District of Columbia	11.62%	17.44%	(17)
U.S. Simple Average	10.15%	15.97%	
U.S. Weighted Average	11.36%	17.18%	

Source: Scott Mackey, KSE Partners, LLP, based on Methodology from Council on State Taxation, 50-State Study and Report on Telecommunications Taxation, May 2005.

Notes: The federal rate on wireless service is 5.82 percent. D.C. rank given for information purposes only and does not affect other ranks.

The Patchwork of High Cell Phone Taxes Hurts Consumers

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.

Scholars have noted that these overlapping geographical and hierarchical taxing authorities are a strong example of a "tragedy of the anti-commons" where a lack of coordination hurts overall economic well-being. As many different government entities take aim at the cell phone service tax base in an uncoordinated fashion with little concern for how other taxing authorities treat the services, cell phones are taxed at a much higher level than other consumer items (even alcohol and cigarettes). Excessive taxes also lead consumers to underutilize cell phone services.[3]

Seven states have combined federal-state-local average cell phone tax rates exceeding 20 percent: Nebraska, 24.49 percent; Washington, 24.44 percent; New York, 23.67 percent; Florida, 22.41 percent; Illinois, 21.76 percent; Rhode Island, 20.50 percent; and Missouri, 20.11 percent. Notable among local jurisdictions, Baltimore, Maryland imposes a $4 per line per month tax on wireless users on top of federal and state charges. Nearby Montgomery County, Maryland imposes a $3.50 per line per month tax. This per line charge is especially burdensome on low-priced "family share" plans. Tallahassee charges a local communications services tax of 6.9 percent on top of an already hefty 9.17 percent state communication services tax.

Scholars from across the political spectrum have criticized telecom taxes as burdensome, regressive, and stifling consumer choice.[4] In response to this problem, legislation entitled the Wireless Tax Fairness Act that would restrict excessive state and local wireless taxes has been regularly introduced in Congress.

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[3] Matthew Mitchell and Thomas Stratmann, Mercatus Center at George Mason University, *Wireless Taxes and Feed: A Tragedy of the Anticommons*, Working Paper No. 12-06 (Jan. 2012). On anticommons generally, *see* Michael Heller, *The Tragedy of the Anticommons: Property in the Transition from Marx to Markets*, 111 HARVARD LAW REVIEW 621 (1998).

[4] *See, e.g.*, Centers for Disease Control, Steven J. Blumberg, *Wireless Substitution: Early Release Estimates from the National Health Interview Survey, July-December 2009* (May 12, 2010), http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless201005.pdf (finding low-income populations rely more heavily on wireless services); Pew Center on the States, Katherine Barrett & Richard Greene, *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, & John Rutledge, *Taxes and Fees on Communication Services*, The Heartland Institute and Beacon Hill Institute at Suffolk University (Apr. 2007), http://www.heartland.org/article.cfm?artId=21102.

Consumers Should Know that Cell Phones Are Taxed in the "Place of Primary Use"

Even if applying the rate and collecting the tax 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, which stated that a cell phone subscriber is liable for cell phone taxes only in his or her "place of primary use."[5] 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.[6]

Conclusion

Making cell phone calls and using wireless services for additional purposes 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 wireless services. Such actions distort market decisions and risk slowing investment that contributes to economic growth. Cell phone users are 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.

National Press Building
529 14th Street, N.W., Suite 420
Washington, DC 20045

202.464.6200
www.TaxFoundation.org

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[5] 4 U.S.C. § 122(a)(2).

[6] *Id. See also* 4 U.S.C. § 124(8).