

May 26, 2006

## Phone Tax Laid to Rest at Age 108

By [KEN BELSON](#)

Bowing to changes in technology and pressure from taxpayers and phone companies, the Treasury Department said yesterday that it would scrap the 108-year-old federal excise tax on long-distance phone calls. The move will bring consumers and businesses about \$15 billion in refunds on next year's tax returns.

The decision, which applies to cellphones and Internet phone services and some landlines, follows a series of court reversals for the government. Large businesses had successfully sued the [Internal Revenue Service](#) to recoup the taxes they paid. Phone companies also wanted the tax abolished to relieve them of having to collect it.

Originally a luxury tax to help pay for the Spanish-American War, the 3 percent surcharge was calculated based on the length of the call and the distance of the connection. But as unlimited long-distance calling plans became commonplace, and the tax was applied to a flat monthly fee, some taxpayers argued that the tax no longer applied to them because the duration and distance of a call were irrelevant.

Though the tax will still be imposed on local phone service, the government will reimburse three years' worth of taxes on long-distance calls, including any plans that combine local and long-distance calling. Consumers, who pay about 40 percent of the taxes collected, typically pay about \$18 a year in excise taxes if they have a long-distance service and a cellphone.

They will be able to file for a refund on their 2006 federal income tax returns.

"It's time to disconnect this tax and put it on the permanent do-not-call list," Treasury Secretary [John W. Snow](#) said. Yesterday's decision, he added, "marks the beginning of the end of an outdated, antiquated tax that has survived a century beyond its original purpose, and by now should have been ancient history."

The abolition of the tax, effective July 31, will cost the Treasury \$5 billion annually in lost revenues in the next few years.

With budget deficits soaring, the Treasury had been slow to scrap the tax. But several federal courts ruled in recent years that it was no longer applicable to customers with unlimited long-distance plans. The Internal Revenue Service has refunded hundreds of thousands of dollars in taxes to companies including [OfficeMax](#) and the American Bankers Insurance Group based on the court decisions.

While the courts said some businesses should get refunds, Congress had not repealed the tax, so the I.R.S. was compelled to continue collecting it. This created a peculiar dynamic in which taxpayers who won refunds still had to pay the tax in subsequent years and then reapply for another refund.

Companies in districts where courts had ruled against the tax could get refunds, while companies elsewhere still had to pay it.

Now, the hundreds of companies that applied for refunds before yesterday's decision will not have their claims processed, according to some tax lawyers. That means companies that could have won refunds through the courts might have to wait far longer for their refunds to arrive after they file their income tax returns.

"The Treasury wants to standardize the process, but it's grotesquely unfair to the people who got this started," said Hank Levine, a partner at Levine, Blaszak, Block & Boothby, a Washington law firm that has represented business plaintiffs in most of the successful cases to date. "The I.R.S. didn't want to give up the money, and now that they have been forced to, they are doing so grudgingly."

Congress was close to abolishing the tax in 2000, but it was attached to a larger tax bill that President [Bill Clinton](#) vetoed. Congressmen are again calling for its repeal.

Senators [Charles E. Grassley](#), Republican of Iowa, and [Max Baucus](#), Democrat of Montana, asked the Senate Finance Committee yesterday to look also at eliminating the tax on local phone service.

For now, the Treasury said that consumers and businesses would get refunds, including interest, on their 2006 income tax returns filed in 2007. The I.R.S. has not decided the size of the standard refund for individuals. But taxpayers who use a lot of phone services will be able to apply for a larger refund if they can document how much they paid in excise taxes.

The average household spends \$10 a month on long-distance calls and \$41 a month on wireless service, or \$612 a year, according to figures from the [Federal Communications Commission](#). Since those services are taxed at 3 percent, the typical household pays \$18.36 a year in federal excise taxes, or \$55 over three years.

Consumers, of course, can still expect plenty of taxes and fees on their phone bills. Phone companies are obligated to collect an array of state and local taxes as well as fees that pay for emergency response groups and public services provided by the Universal Service Fund and others.

Phone companies have opposed some of these taxes because of the expense of collecting them, and because it drives up the cost of their services, making them less attractive to consumers.

"[Wireless](#) consumers can now turn their attention and efforts to repealing discriminatory wireless taxes on the state and local level," said Steve Largent, the president of CTIA, a trade group that represents cellular companies.

Mr. Largent said 17 percent of the typical monthly cellular bill was made up of taxes and fees.

Carriers, however, are partly to blame for that burden because they charge their customers a range of discretionary fees to recoup their business costs. For instance, some customers are charged "property tax allotment" fees that are meant to pay for a company's real estate taxes. Other companies charge "carrier cost recovery fees" to pay for the administrative costs of collecting taxes.

These fees generate billions of dollars in revenue for the companies.

That is a far cry from 1898, when the tax was first levied and there were 681,000 phone subscribers in the United States, according to James Katz, a telecommunications historian at Rutgers University. Though relatively small in numbers, those subscribers paid a considerable amount in taxes to help finance the government's battle against Spain.

The annual basic charge for a home phone in the 1890's was about \$100, or more than \$2,200 in today's dollars. A three-minute call from New York to Chicago in 1902 cost \$5.45 — about \$120 today.

[Copyright 2006 The New York Times Company](#)

[Privacy Policy](#) | [Search](#) | [Corrections](#) | [XML](#) | [Help](#) | [Contact Us](#) | [Work for Us](#) | [Site Map](#)

---