

The Cellphone Becomes a Taxpayer  
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Last year, the City Council in Baltimore faced a budget shortfall so bad that it considered laying off 186 city police officers, reducing some fire department operations and scaling back trash collection. Then it found an untapped honey pot: cellphones.

Starting in August, the city began collecting \$3.50 a month from each of Baltimore's 238,000 mobile phone subscribers. The extra income has helped to strengthen the city's finances and is expected to help the city fix up schools and trim the property tax.

"I can't remember the last time we've had such an easy budget year," said Sheila Dixon, the president of the City Council. "The bulk of our taxes come from property tax, but when you can't diversify and the federal and state taxes are drying up, you need other income."

Baltimore is not alone. The city of Springfield, Ore., for example, recently enacted a 5 percent tax on cellphones and land lines, which would help finance a new jail. Residents and utilities opposed to the tax, which is yet to take effect, have forced a referendum to be held on Tuesday.

Dozens of other cities and states have already passed cellphone taxes. Many other states and municipalities, including some in Louisiana and Missouri, are debating similar measures as they compile their budgets for the next fiscal year.

Officials are particularly eager to tax cellphones because the amounts individuals pay each month are small enough to go virtually unnoticed, but in aggregate can be substantial. Cellphone subscribers nationwide paid an estimated \$17.8 billion in federal, state and local taxes last year.

But mounting taxes have led wireless companies like Verizon Wireless and Sprint to form unlikely alliances with consumer advocates and tax reformers to fight new city fees. They argue that consumers are taxed twice in states and cities that also impose sales taxes, and that the extra burden is particularly hard on retirees and low-income subscribers and also reduces overall demand for mobile service.

The cellphone taxes, when added to existing federal excise and state sales taxes, as well as fees for 911 service, mean that \$8.75, or 16.7 percent, of the average monthly cellphone bill of \$52.50 now goes to government agencies -- about twice as much as on many other services, according to CTIA-the

Wireless Association, a wireless industry trade group. While cellphone subscribers in New York, Connecticut and New Jersey pay some of the highest tax rates in the country, the states do not levy a wireless-only sales tax.

The carriers say they do not oppose collecting taxes on behalf of governments, but they object to being subject to special taxes as tobacco and alcohol are.

"We have no problem with the revenue needs of the localities," said Steven Zipperstein, general counsel for Verizon Wireless. "But we have a big problem that a certain class of customers or services should be singled out for excessive taxation."

Cingular Wireless, Verizon Wireless, Sprint and T-Mobile filed a lawsuit in February in Maryland Tax Court against Baltimore and Montgomery County, which has its own wireless tax. They contend the cellphone fee is effectively a sales tax, which only the state has the right to impose.

They also say that cities have no authority to collect taxes on services consumed outside their borders, noting that many of the cellphone calls made in Baltimore go outside the city limits.

"Some portion of what they are taxing is outside their boundaries, so it's defective for that reason," said Kenneth H. Silverberg, a lawyer at Nixon Peabody, the firm representing the carriers.

Others have joined the move to repeal the fee. At least one Baltimore councilman wants to exempt senior citizens from the wireless tax. Progressive Maryland, a nonprofit group that promotes "pro-working-family legislation," said Maryland lawmakers should raise the corporate tax and scale back taxes on consumers.

"When you have a thriving corporate sector paying less and less tax, the taxes get foisted on working and middle-class families," said Tom Hucker, executive director of the group.

The National Black Caucus of State Legislators called on state and local governments last December to roll back taxes, including flat taxes, on wireless services because they "disproportionately burden low-income, low-volume cellular telephone subscribers."

But a Baltimore municipal spokeswoman said the city felt it was on firm ground. The telecommunication tax was "crafted and implemented with the expectation that it would stand up to a legal challenge," said the spokeswoman, Raquel Guillory.

The tussle over the right to levy taxes on wireless services comes as phone providers and federal regulators struggle with how technology is changing the meaning of a phone call. Some lawmakers argue that to encourage the spread of new technology, new services should not be taxed as heavily as traditional ones. Others, intent on cutting and streamlining local taxes, want to limit the power of states and cities to introduce their own special fees.

Yet city councils and state lawmakers with budget holes to plug argue that "a phone call is a phone call," regardless of how it is placed. With consumers increasingly using cellphones instead of land lines, local governments are eager to start taxing wireless services just as they have taxed traditional phone lines for years.

In Baltimore, the \$3.50 tax on cellphones extends to land lines as well. Businesses operating multiple phone extensions also pay 35 cents a line. Under the previous tax structure, the city charged a 12 percent tax only on land lines.

By moving to a flat fee for all phones, the city expects to raise \$26.1 million in the fiscal year ending June 30, double what it received under the old formula. Of that total, \$8.81 million, or 34 percent, will probably come from cellphone users, money the city did not receive before.

To be sure, the expanded phone tax is only one reason the city's finances have improved. Baltimore also nearly doubled its tax to record deeds and it expanded fees on utilities. The property market has also been booming in the area.

The income generated by Baltimore's broader phone tax has become a model for other cash-short cities. Council members in Portland, Ore., are debating whether to include cellphones for the first time in the city's utility license fee on phones. Cities in Missouri as well as the state legislature are considering similar measures.

Wireless companies point to Pennsylvania as a state with lofty taxes on cellular services. In 2003, lawmakers there extended the 5 percent gross receipts tax on land lines to include mobile phones. That tax goes on top of a 6 percent statewide sales tax.

Some cities in the state, like Philadelphia, have general sales taxes, too. Cellphone subscribers also pay into a fund for an emergency response system for wireless users. And then there is the federal excise tax of 3 percent. In all, taxes make up 19.05 percent of the average monthly wireless bill in

Pennsylvania, one of the highest levels in the country.

Some state and local lawmakers are already thinking beyond cellphones. One idea is to create a uniform use tax that covers all forms of telecommunications: land lines, mobile phones, Internet-based phones, high-speed data lines and programming provided by cable and satellite companies. By spreading the tax to services like satellite television, which are subject to very little city or county taxes, the fees on phone services could be lowered.

"We've had a tax system based on technology as a utility for almost 60 years," said Steven J. Rauschenberger, a state senator from Illinois and the president-elect of the National Conference of State Legislators. "But with the convergence of technology, we need to rethink the system."

Photos: The City Council chambers in Baltimore. Anticipating a budget shortfall, the council imposed a fee of \$3.50 a month on all cellphone users in August. Some utilities have challenged such taxes, saying cities do not have the authority to impose them. (Photo by Ken Cedeno for The New York Times)(pg. C1); Chatting in the harbor area of Baltimore. A tax on the city's 238,000 cellphone subscribers has provided substantial budget relief to the city. (Photo by Ken Cedeno for The New York Times)(pg. C10)

Chart: "Cellular Nation"

The number of cell phones may soon surpass the number of wired phones.

Graph tracks the number of cellular phones and local phone lines from 1985-2004.

(Sources by Federal Communications Commission; Cellular Telephone Industry Association)