



Commenters note that America's local communities are an integral part of the solution to our national broadband deficit. Indeed, we have been working on the frontlines of this effort for more than a decade, even as the Federal government chose to take a wait-and-see approach to broadband. In light of that Federal inaction, countless local communities became more engaged in developing the conditions to attract more private investment in broadband and in many cases where there was no other option, build out networks themselves because the private sector failed to adequately respond to their needs. Today, 44 communities operate successful fiber to the home networks and many more are considering this option. More advanced networks would be built if some states did not prohibit or limit local provisioning of broadband services.

In light of this decade of local effort to build or incent broadband deployment, and in light of all the compelling local interests in promoting access to advanced broadband, it is troubling to hear industry complaints that localities create the barriers to the deployment of broadband networks. These unsupported claims are based on the absurd premise that local communities are not interested in competition that will lead to advanced broadband services, lower prices, and greater adoption. The Commission is asked to believe that local governments are more interested in creating barriers to private investment than in ensuring the benefits of broadband to their constituents.

Perhaps such self-serving comments are meant to draw attention from the failure of the private sector to make adequate investment in broadband networks. Perhaps they are designed to elicit special treatment and limit competition. Commenters ask the Commission to regard localities as a key partner in solving the nation's broadband deficit, and to look with skepticism on the claims of various industries that seek to profit by limiting local authority – and by limiting competition from community-based networks.

Furthermore, given the inherent localism of both the broadband deficit and the potential broadband solution, Commenters ask the Commission to recognize local governments and local communities as key partners to industry, the states, and the Federal government in broadband development.

## **II. THE CENTRAL LOCAL ROLE IN BROADBAND SHOULD BE RECOGNIZED AND PROTECTED**

Communities must have the freedom to meet their unique communications needs.

Commenters ask the Commission to include in the National Broadband Plan a strong affirmation of the need for localities to have the choice, if they so wish, to own and operate public broadband networks, and a recommendation for preemption of existing state limitations and barriers to local government communications initiatives.

As the Commission recognized recently in its Report on a Rural Broadband Strategy,<sup>1</sup> solving our nation's broadband problem will require extensive collaboration among all parties: local communities, regions, state governments, the Federal government, tribal governments, the private sector, interest groups and others. Commenters note that the role of localities cannot be overstated:

- Local elected officials are intimately aware of the concerns and needs of constituents, including their frustrations with broadband availability, speeds, and costs.
- Local governments are central players in ensuring that "last mile" wireline connection to homes and businesses is achieved.
- Local officials are intimately familiar with the need for last mile wireless, because their first responders and other government users are frequently the largest aggregate users of wireless services in a community.
- Local elected officials are well positioned to evaluate the infrastructure and economic development tools needed to sustain viability, encourage growth, and ensure that the unique needs and specific interests of local communities are addressed.

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<sup>1</sup> See *Bringing Broadband to Rural America: Report on a Rural Broadband Strategy*, GN Docket No. 09-29, p. 25, released May 22, 2009.

For nearly a decade, local governments have been leaders in ensuring that the benefits of communications technology accrue to all of our residents. Local governments will, by necessity and by choice, continue to be part of the solution to our national broadband deficit. America's local communities are increasingly concerned that we are losing our competitive advantage to communities in Europe and Asia because of the lack, until recently, of Federal and state broadband policy initiatives and leadership. Our local – and national -- competitive status has been harmed relative to our competitor nation and cities with respect to education, healthcare, economic development, standard of living, and the level and quality of civic discourse. That is why many of our communities have risen to the challenge and become leaders in bringing advanced broadband networks to our residents, often in partnership with the private sector. Local governments have responded because of the inability or unwillingness of private companies to meet the demands of our residents and businesses for more competition, choice and service innovation.

Local communities regard broadband networks as critical infrastructure and a platform for the continuing development of innovative community services that will transform the way we work and play. Local governments are one of the biggest consumers of broadband services. They increasingly rely on reliable and fast broadband connections to provide more efficient government services, make government more transparent and enhance the democratic process by finding new ways to engage citizens with their elected officials and community organizations.

Local governments have a keen interest in promoting deployment of broadband networks because of the many positive externalities that can be realized in our communities through widespread broadband connectivity. Localities understand that broadband networks can and must be responsive to local community needs and interests. When decisions by private network owners fail to advance those social and economic imperatives, local governments often become involved as a matter of

necessity to better the quality of life and ensure that our communities are positioned for success in today's global economy. Among the benefits local governments consider are:

- **Improving Health Care:** Widespread broadband adoption in our communities will improve the delivery of medical care available to our residents and help maintain a healthier population. Doctors will be able to monitor heart rates, blood pressure and other vital indicators remotely over broadband connections. Unlike a network owner, cities consider the social value of enabling seniors to live in their homes longer because an interactive broadband network allows for video home monitoring by primary care givers and relatives. Broadband has great potential for improving the level of preventive care.
- **Improving our Schools:** Enhance distance learning opportunities and allow us to educate more of our citizens and reduce the cost of education. Studies indicate a strong correlation between the quality of images and the engagement with the material and quality of learning that takes place.
- **Inclusive Communities:** We can help to alleviate the isolation of some of our citizens. Broadband will allow people with physical disabilities to become more competitive in the job market and able to communicate over interactive video in real time with their friends and neighbors.
- **Improve Public Safety:** Our first responders must have reliable, interoperable broadband communications. When public safety communications systems fail, people can die. Local governments play a vital role in ensuring that communications systems operate as intended.
- **Reducing Carbon Emissions:** Many local communities believe that they have a special responsibility to exploit the potential of the Internet to reduce green house gas emissions. Broadband is seen as a major component in the mix of strategies for achieving progress in this area – more than 80 percent of which are originated in metropolitan areas. Broadband will make possible the enhanced telecommuting and collaboration options that will lead to reduced carbon emissions from automobiles, decrease traffic congestion and save wear and tear on our streets and bridges.
- **Spur Economic Development and Job Creation:** Local governments are front and center in the effort to create jobs. Multiple studies show that broadband does enhance economic growth.

The National Broadband Plan should recognize that communities must have the freedom to meet their unique communications needs and that localities must not be constrained to respond to the needs of local constituents.

### **III. WIRELESS FACILITIES SITING, RIGHTS-OF-WAY, FRANCHISING, AND BUILD OUT OBLIGATIONS**

A troubling pattern is evident in some comments in this proceeding: attempts by some industries to use the formation of a National Broadband Plan to (1) deflect blame for the failure to keep pace with our competitor nations in broadband deployment by charging that localities are creating barriers to deployment and (2) solicit special treatment and favors not afforded to other industries by requesting that local authority and policy be supplanted through Federal intervention and preemption.

#### *A. The FCC Should Resist Calls to Federalize the Management of Local Property*

Various industry commenters have encouraged the FCC to call for the federalization of local wireless facilities siting and right-of-way management through the adoption of defined national standards.<sup>2</sup> The FCC should not go down this path. The federal government is simply not equipped to deal with local property management and zoning issues. It is important for all concerned to remember that State and local governments must balance a range of competing interests in making siting and right-of-way management decisions: the public rights-of-way and other property subject to local control do not exist solely for the purpose of supporting telecommunications infrastructure. Even as it acted to protect the interests of the communications industry, Congress has recognized that state and local governments must retain the power to exercise their judgment in this area. By their nature, fixed federal rules cannot balance the many competing interests — including those extending far beyond the deployment of communications infrastructure — that intersect in a local community's streets and property. Instead of federalizing local property management, the FCC should draw from recent precedent and call for a renewed partnership between industry and local governments.

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<sup>2</sup> See, e.g., Verizon Comments at 63-66; CTIA Comments at 15-19; Level 3 Comments at 18-20.

## **1. The Local Wireless Facilities Siting Process Should Not Be Altered**

The FCC should reject calls from CTIA, Verizon, Clearwire, and others to interfere with the local wireless facilities siting process.<sup>3</sup> In the Telecommunications Act of 1996, Congress wisely elected to preserve local zoning authority, subject only to certain, express limitations contained in a single section of the Communication Act. 47 U.S.C. § 332(c)(7). Under that scheme, wireless deployment has flourished. Nevertheless, the wireless industry continues to misconstrue Congress's decision, and various commenters again call for the FCC to regulate the local wireless facilities siting process directly. This would be both unlawful and unwise. Federal policymakers should not interfere with a process that is successfully encouraging deployment while protecting local communities.

### *i. The Local Siting Process Serves Important Interests And Advances Deployment of Wireless Services.*

While local governments actively encourage the provision of advanced communications services to their citizens, local authorities also protect other important interests through the zoning process. Advancing the parochial interests of the wireless industry – for that is what the subordination of local authority to Commission oversight would do – would be no more acceptable than a process that entirely ignored the needs of carriers in favor of purely aesthetic goals. Federal preemption might be good for the wireless industry – but the good of the wireless industry is only one consideration. All too often, the wireless industry leaves the impression that every siting application is delayed and every local action is unreasonable. This is simply not true, and it is up to the Commission to recognize that without cooperation from local authorities the wireless industry could never have grown as much or as quickly as it has.

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<sup>3</sup> See, e.g., CTIA Comments at 15-19; Verizon Comments at 63-66; Clearwire Comments at 7-8; Comcast Comments at 50; American Consumer Institute Comments at 34.

Local authorities work with carriers and citizens to limit facility siting that could be unsightly or dangerous. Aesthetics and safety are both permissible and important considerations under the law. Through this process, local authorities necessarily consider diverse local circumstances on a fact-specific basis — an inquiry not amenable to a “one-size-fits-all” federal approach. This is precisely what Congress intended when it declined to federalize the local wireless facilities siting process in the Telecommunications Act of 1996. 47 U.S.C. § 332(c)(7). The result has been a resounding success. Local authorities have protected local interests, and wireless technology has expanded rapidly across the country.<sup>4</sup> Federal policymakers need not interfere with this success.

*ii. The CTIA Petition Misreads the Communications Act and Fails To Support Its Factual Assertions*

Based on a petition filed last year by CTIA,<sup>5</sup> a number of parties in this proceeding have asked the FCC to establish fixed timelines to govern local wireless facilities siting under 47 U.S.C. § 332(c)(7).<sup>6</sup> The FCC should decline to do so.

Like the CTIA petition, the suggestions of commenters in this docket are plagued by a number of problems. First, CTIA and other commenters appear to assume that Congress bestowed general rulemaking authority on the Commission with respect to local wireless facilities siting. Indeed, CTIA makes much of the fact that the FCC recently adopted timelines to

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<sup>4</sup> See, e.g., CTIA Comments at 2-7; Verizon Comments at 23. See also CTIA Petition for Declaratory Ruling, WT Docket No. 08-165, at 10 (July 11, 2008); *In re Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services*, WT Docket No. 08-27, DA 09-54 ¶ 2 (Jan. 16, 2009) (finding “[m]ore than 95 percent of the U.S. population lives in census blocks with at least three mobile telephone operators competing to offer service”).

<sup>5</sup> See *CTIA Petition for Declaratory Ruling*, WT Docket No. 08-165 (July 11, 2008).

<sup>6</sup> See CTIA Comments at 15-19; Verizon Comments at 65; Clearwire Comments at 8-9; Google Comments at 42; Comcast Comments at 50; American Consumer Institute Comments at 34.

govern the cable franchising process under Section 621(a)(1), 47 U.S.C. § 541(a)(1).<sup>7</sup> But Section 621(a)(1) and Section 332(c)(7) differ in key respects. When Congress added Section 621(a)(1) to the Communications Act, it was silent as to the FCC’s rulemaking powers with respect to that section. Because of this silence, the Sixth Circuit concluded that the FCC’s general rulemaking authority in *other* sections of the Act — specifically Section 201(b)— applied, and allowed the FCC to adopt substantive, binding rules interpreting “unreasonably refuse” in Section 621(a)(1). *Alliance for Community Media v. FCC*, 529 F.3d 763, 773-74 (6th Cir. 2008). In contrast, when Congress added Section 332(c)(7) to the Act, Congress directly addressed how the FCC’s general rulemaking powers in other sections of the Act would apply:

Except as provided in this paragraph, *nothing in this Act* shall limit or affect the authority of a State or local government or instrumentality thereof over decisions regarding the placement, construction, and modification of personal wireless service facilities.

47 U.S.C. § 332(c)(7)(A) (emphasis added). Accordingly, the legislative history specifically instructs that “[a]ny pending Commission rulemaking concerning the preemption of local zoning authority over the placement, construction or modification of [commercial mobile service] facilities shall be terminated.”<sup>8</sup> Lacking rulemaking authority, the FCC may not adopt binding rules with fixed timelines. CTIA also ignores that the language of Section 332(c)(7) only can be “construed” to preempt “expressly.”<sup>9</sup> Specifically, Congress instructed that amendments made by the 1996 Act “shall not be construed to modify, impair, or supersede Federal, State or local law *unless expressly so provided.*” Section 601(c) of the Telecommunications Act, 47 U.S.C. § 152 nt. (emphasis added). Of course, Section 332(c)(7) does not “expressly . . . provide[ ]” fixed

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<sup>7</sup> See CTIA Petition at 21-22, citing *In re Implementation of Section 621(a)(1) of the Cable Communications Policy Act of 1984 as amended by the Cable Television Consumer Protection and Competition Act of 1992*, 22 FCC Rcd. 5101 (2007).

<sup>8</sup> See H.R. Report No. 104-458, at 208. The FCC describes its role under Section 332(c)(7) as “primarily one of information and facilitation.” See <http://wireless.fcc.gov/siting/local-state-gov.html>.

<sup>9</sup> This limitation does not apply to the relevant language governing cable franchising in Section 621(a)(1), which was added earlier.

timelines to supersede local processes. Instead, it provides that a state or local government shall act “within a reasonable period of time . . . taking into account the nature and scope” of the particular request. The FCC may not “construe[ ]” the statute to provide otherwise.<sup>10</sup> Moreover, to read such timelines into the Act would directly contradict Congress’s intent: “It is not the intent of this provision to give preferential treatment to the personal wireless service industry in the processing of requests or to subject their requests to any but the generally applicable time frames for zoning decision.” H.R. Conf. Rep. No. 104-458 at 208.<sup>11</sup>

CTIA has also wholly failed to document the purported delays or to establish that local governments are at fault for them. CTIA has generally refused to name the local communities that are allegedly at fault, which makes verification virtually impossible. It also has not explained whether or how it has confirmed its information, and it has not indicated if it has examined whether applicants themselves impeded local process in such situations. And even if the specific instances cited by CTIA could be verified, CTIA has not shown that they are typical or representative in any way. The Commission must avoid the temptation to regulate by anecdote. Local governments have approved tens of thousands of requests for siting wireless

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<sup>10</sup> Verizon also calls for the FCC to preempt zoning ordinances under Section 253 of the Communications Act, 47 U.S.C. § 253. Verizon Comments at 66. However, this also ignores Congress’s instruction that Section 253, like other provisions of the Act, cannot be read to “limit or affect the authority of a State or local government” over wireless facilities siting. 47 U.S.C. § 332(c)(7)(A). Verizon’s proposed approach to Section 253 would directly “limit or affect” such “authority.”

<sup>11</sup> Clearwire contends that the FCC should also extend Section 332(c)(7) to “all mobile broadband access service providers” based on the requirement that a state or local government “shall not unreasonably discriminate among providers of functionally equivalent services.” 47 U.S.C. § 332(c)(7)(B)(i)(I). Clearwire Comments at 9. But Congress clearly defined the statute’s applicability. It applies to the regulation of “personal wireless service facilities.” 47 U.S.C. § 332(c)(7)(B)(i). “Personal wireless services” is defined as “commercial mobile services, unlicensed wireless services, and common carrier wireless exchange access services.” 47 U.S.C. § 332(c)(7)(C)(i). “Unlicensed wireless service” is “the offering of telecommunications services using duly authorized devices which do not require individual licenses, but does not mean the provision of direct-to-home satellite services (as defined in section 303(v)). To the extent Clearwire provides these services, the statute applies to its tower placements.

facilities in this country,<sup>12</sup> yet the wireless industry can only point to a relative handful of problems. The truth is that local governments do respond to the needs of the industry. Even if the FCC could adopt fixed timelines under Section 332(c)(7), the Commission should decline to do so based on such an inadequate record.

*iii. The FCC Should Not Urge Congress To Alter the Local Wireless Facilities Siting Process*

The FCC should also not invite Congress to revise Section 332(c)(7) to add fixed timelines or to otherwise limit local zoning authority.<sup>13</sup> The FCC has refused to fix a deadline for its own decisions under Section 332(c)(7)(B)(v) because it was “concerned that doing so will not afford the Commission sufficient flexibility to account for the particular circumstances of each case.”<sup>14</sup> The same flexibility is needed at the local level. While the local siting process ordinarily moves smoothly, in exceptional cases, for a variety of case-specific reasons (including delays by the applicant itself),<sup>15</sup> immediate action may not be possible. Congress should not remove this flexibility and “deem” applications “granted” that might jeopardize local interests.

Verizon also maintains that Congress should limit state and local authority to require zoning approval for co-location on towers “that were previously approved, that do not result in a ‘substantial increase’ in the tower, and that do not materially change the appearance of the tower.”<sup>16</sup> But this approach creates more questions than it answers, and, in so doing, underscores the importance of local zoning authority. Who would determine whether an addition to a tower would “materially change” the appearance of a tower? Who would decide whether the co-

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<sup>12</sup> CTIA recently informed the FCC that, as of December 2008, there were more than 242,000 cell sites in the United States. CTIA also stated that there were only 30,045 such sites in December 1996. Comments of CTIA, WT Docket 09-66, at 21-22 (June 15, 2009).

<sup>13</sup> Verizon Comments at 65; American Consumer Institute Comments at 34.

<sup>14</sup> *In re Procedures for Reviewing Requests for Relief from State and Local Regulations Pursuant to Section 332(c)(7)(b)(V) of Communications Act of 1934*, 15 FCC Rcd. 22821, 22827 at ¶ 14 (2000).

<sup>15</sup> For more information on the issue of delays caused by applicants, please see the Reply Comments of Montgomery County, Maryland, at p. 10.

<sup>16</sup> Verizon Comments at 64.

location, while safe and unobtrusive in one context, would not be dangerous and obtrusive in another? These are *precisely* the determinations that a local zoning board, not a wireless provider, is best-suited to make.<sup>17</sup> The FCC should not encourage Congress to pursue this approach.

## **2. The FCC Should Not Undermine Local Management of the Public Rights-of-Way**

The FCC also should also reject industry requests to undermine local management of the public rights-of-way. Such comments were few in this docket, consisting primarily of submissions from Verizon, Level 3, and EDUCAUSE, Internet2, and ACUTA. This is not surprising, because local management of the public rights-of-way is not an impediment to broadband deployment, and therefore need not be further addressed in this docket. In any case, the FCC recently confirmed that the courts are correctly applying Section 253 of the Communications Act, 47 U.S.C. § 253, which preempts local requirements that “prohibit” or have “the effect of prohibiting” the ability to provide telecommunications service.<sup>18</sup> Federal policymakers should reject requests to transform Section 253 into something much more speculative and disruptive to important local interests.

### *i. Local Right-of-Way Management Serves Important Interests*

Local governments manage the rights-of-way in order to protect the health and safety of the public, the facilities of the government itself, and the property and other interests of every class of right-of-way user. Those users include not just communications companies, but gas, water and electric utilities, as well as the commercial transportation industry, public transportation, and individual drivers. As with CTIA’s complaints about wireless facilities siting, the communications industry often takes a deeply parochial view of right-of-way

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<sup>17</sup> For more information on the need for individual review of co-location requests, please see the Reply Comments of Montgomery County, Maryland, at p. 16.

<sup>18</sup> See Brief for the United States as Amicus Curiae, S. Ct. Case Nos. 08-626, 08-759 (May 2009).

management issues, seemingly oblivious to the fact that the public rights-of-way – and other public property used by communications providers – does not exist solely to accommodate their needs. As important as communications services are to local governments and their residents, so is the proper management of the transportation infrastructure, not to mention the public purse. We trust that the Commission will rise above the parochialism of the industry, and recognize that local governments not only act reasonably in balancing their obligations, but also are aware of the need to accommodate the reasonable needs of communications providers, within the overall context of a larger and more complex endeavor.

Federal law already recognizes this important local role. In Section 253 of the Communications Act, 47 U.S.C. § 253, Congress specifically preserved local authority to “manage the public rights-of-way” and “to require fair and reasonable compensation from telecommunications providers.”<sup>19</sup> The FCC itself has described the role of state and local authorities in advancing the interests of their citizens through right-of-way management as “vital.”<sup>20</sup> We urge the Commission to continue to exercise its traditional restraint in this area.

*ii. The FCC Should Not Alter Its Approach to Preemption Under Section 253*

The FCC need not re-visit its recent recognition that courts are correctly applying Section 253, and should reject calls to alter the approach to preemption under this statute. In a brief filed at the request of the Supreme Court in May, the United States was joined by the FCC in confirming the proper approach to Section 253.<sup>21</sup> The United States found that the Eighth

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<sup>19</sup> 47 U.S.C. § 253(c).

<sup>20</sup> *Suggested Guidelines for Petitions for Ruling Under Section 253 of the Communications Act*, 13 FCC Rcd. 22970 (1998) (emphasis added).

<sup>21</sup> See Brief for the United States as Amicus Curiae, S. Ct. Case Nos. 08-626, 08-759 (May 2009).

Circuit<sup>22</sup> and the Ninth Circuit<sup>23</sup> had correctly rejected the view that the statute broadly preempts any requirement that “may” prohibit the ability to provide service:

[A] plaintiff seeking preemption under Section 253 cannot meet its burden simply by alleging that, under circumstances that might exist at some indeterminate future time, a legal requirement “may” affect its ability to provide a telecommunications service. Instead, a plaintiff must present evidence of the practical effects of the requirement at issue.

Brief of the United States as Amicus Curiae at 8 (U.S. S. Ct. Case Nos. 08-626, 08-759). The Supreme Court denied certiorari on June 29, 2009,<sup>24</sup> preserving the decisions of the Eighth and Ninth Circuits that the United States and the FCC had defended.

The FCC also should dismiss industry requests to transform Section 253 into something more speculative. Verizon urges that Congress restore the now-discredited “may prohibit” test.<sup>25</sup> But the Eighth Circuit, Ninth Circuit, and the United States all opposed this reading, and for good reason. Such a “preemption-by-speculation” approach would not only be unprecedented, but it would inevitably lead to a far-reaching interference with important local safeguards.<sup>26</sup> Quite literally, every legal requirement that obligates a provider to do anything—even, for example, obeying traffic signals or heeding antidiscrimination laws—“might” prohibit the ability to provide service, and would thus be subject to challenge. The result would be endless litigation and a significant loss of important local protections. As currently written, Section 253 takes a

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<sup>22</sup> *Level 3 Commc’ns v. City of St. Louis*, 477 F.3d 528 (8th Cir. 2007).

<sup>23</sup> *Sprint Tel. Co. v. County of San Diego*, 543 F.3d 571 (9th Cir. 2008) (*en banc*).

<sup>24</sup> Order of the Supreme Court, 2009 WL 1835180 (June 29, 2009).

<sup>25</sup> Comments of Verizon and Verizon Wireless at 66. As discussed, *supra* at n.10, Verizon erroneously contends that Section 253 applies to local wireless facilities siting.

<sup>26</sup> As the FCC is aware, courts are often called upon to interpret Section 253, but they are ill-equipped to speculate about what effect a local requirement “might” have on a provider. Such judicial speculation would be inconsistent with Article III of the United States Constitution.

much sounder approach: a provider must *demonstrate* that a local requirement literally “prohibits” or, as a practical matter, would have that effect.<sup>27</sup>

*iii. The Commission Should Reject Calls for Federal Intrusion in the Management of Local Rights-of-Way*

The FCC should also reject undeveloped ideas offered by some commenters for the federal government itself to more actively regulate local right-of-way management. EDUCAUSE, Internet2, and ACUTA urge the FCC to provide “national consistency regarding right-of-way management.”<sup>28</sup> Aside from being so open-ended as to be meaningless, and a call for intruding on state and local rights to manage their own property without even a hint of justification, such a proposal would be entirely unworkable. Local conditions – from state to state and locality to locality – vary significantly in a nation as large as the United States. The practices needed to properly manage the rights-of-way in earthquake-prone California are not the same as those necessary in the extreme cold of Alaska or the high water tables of Florida and the Gulf Coast states. Nor does the Commission have any expertise in this field.

Level 3 offers a specific proposal, calling for the FCC to compel a state or local government to issue permits for the construction of broadband networks *before* the state or local government has issued a franchise.<sup>29</sup> Level 3 cites no statutory authority to authorize such a rule, and we are not aware of any. Moreover, such a rule would put the cart before the horse, because it ignores both the purpose for requiring a franchise, and differences in local practices. The primary purpose of issuing a franchise is to grant the provider the right to occupy and use local

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<sup>27</sup> We note that Level 3—whose reading of Section 253(a) was rejected by the Eighth Circuit — *still* appears to be confusing the safe harbor language in Section 253(c), with the preemptive language in Section 253(a). Level 3 Comments at 19. The United States, joined by the FCC, agreed with the Eighth Circuit that only Section 253(a) has preemptive force. Brief for the United States as Amicus Curiae, S. Ct. Case Nos. 08-626, 08-759 at 19.

<sup>28</sup> Comments of EDUCAUSE, Internet2, and ACUTA at 10.

<sup>29</sup> Level 3 Comments at 20. The FCC lacks statutory authority to issue local permits, and it may not commandeer local officials to issue them, U.S. Const. Art. X.

property. Before a franchise can be granted, most communities require a demonstration that the prospective franchisee is legally, technically, and financially qualified: in other words, the local government first establishes that the applicant will be able to use and occupy local property without causing harm to facilities or the public.

Local permitting procedures, on the other hand, do not necessarily call for such a showing; they often presume competence, precisely because a franchise has been issued, or the provider has otherwise established its competence. It is also important to remember that local governments are required to behave in a nondiscriminatory fashion: if a city or county adopts a practice of allowing access to established or well-known providers, on the presumption that they know what they are doing, it may find it more difficult to control the activities of unproven companies.

It would be odd, indeed, for the federal government to compel a local government to authorize an entity to construct facilities in the public right-of-way before the locality has established that the entity could do so safely. The federal government is simply not well-suited to assume control over local property management decisions, particularly at such a level of detail.

Furthermore, a federal rule mandating access before the terms of access have been agreed to – including not only compensation, but all of the terms, such as insurance, indemnification, remedies, construction and safety standards, and all the rest -- would subvert the rights protected by Section 253 by giving the provider what it wants most at no cost: under such a scheme, what incentive would Level 3 have to complete franchise negotiations? Once the permits were granted and the facilities installed, Level 3 would have no reason to reach agreement, short of litigation. In fact, to the extent that Level 3 seems to be calling for the FCC to direct local

governments to grant access to the public right-of-way by issuing permits on demand, such a rule would constitute a *per se* taking, and therefore violate the takings clause of the Fifth Amendment.<sup>30</sup>

*iv. The Commission Should Consider Requiring Build Out Obligations*

In their comments, the American Consumer Institute warns that build out obligations on network operators are inefficient, and inject a level of financial risk into projects that could make further deployments of broadband untenable.<sup>31</sup> This concern focuses solely on the ability of a private broadband service provider to make the “business case” for investing in certain areas – the exact kind of behavior that has yet to deliver broadband to many communities. Not only does this statement overlook the concern being addressed by the imposition of build out requirements, it ignores the success with which build out requirements have worked in the cable franchising arena.

As Commenters pointed out previously, requiring build out obligations as part of the grant of a cable franchise has resulted in 92 percent of American households having access to cable.<sup>32</sup> These deployments were not made simply because cable operators could make the business case for serving most of the nation’s households, but were required so as to ensure that every citizen would have access to cable video service and, subsequently, cable modem service. Instead of bemoaning these obligations, the cable industry has instead touted its ubiquitous deployment,<sup>33</sup> albeit without mention of the actual impetus for many of its deployments.

Without local governments requiring cable operators to serve areas where the “business case” could not be readily made, one can imagine that America’s broadband standing would be

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<sup>30</sup> *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 438 (1982).

<sup>31</sup> Comments of ACI at p. 30.

<sup>32</sup> Comments of NATOA et. al. at p. 19.

<sup>33</sup> See Availability of Cable Services, NCTA, avail. at <http://www.ncta.com/StatsGroup/Availability.aspx>.

markedly worse. Build out obligations ensure that the public interest is being met by making sure that any citizen, regardless of location, economic status or social background, have access to the communications technologies that are essential to success in the 21<sup>st</sup> Century.<sup>34</sup> The Commission should ensure that any National Broadband Plan requires that broadband services be deployed in an efficient manner to all communities, so that every American can realize the benefits of broadband.

*B. The FCC Should Call for a Renewed Partnership between Local Governments and Industry*

Instead of federalizing wireless facilities siting or right-of-way management with *per se* rules that cannot adapt to diverse local circumstances, the FCC should call for a renewed partnership between local government and industry. There is precedent for this. In 1998, CTIA agreed to withdraw a petition for a declaratory ruling regarding local wireless facilities siting moratoria after local government and industry representatives reached an agreement regarding adoption of future moratoria. The agreement established recommended guidelines, and created a non-binding alternative dispute resolution procedure that either carriers or local governments could invoke.<sup>35</sup> Chairman Kennard praised the approach as a “fantastic example of the FCC, other branches of Government, and the telecommunications industry working cooperatively to ensure that the interests of all Americans are served, as this dynamic segment of the telecommunications industry expands competition in communities across this nation.”<sup>36</sup>

Commenters believe that creative ideas and new approaches could form the basis for a new partnership. For example, a number of commenters have called for the placement of fiber

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<sup>34</sup> For example, as part of building its FiOS fiber optic network in Washington, D.C., Verizon was required to deliver service first to areas where the “business case” is not as readily made, such as Anacostia, Fort Stanton, and Barry Farm in the city’s southeast quadrant. See “Fenty Administration and Verizon Announce Accelerated Deployment of Fiber-Optic FiOS Network Throughout the District,” District of Columbia Press Release, released October 30, 2008, avail. at <http://www.dc.gov/mayor/news/release.asp?id=1410&mon=200810>.

<sup>35</sup> See summary and links, available at: <http://wireless.fcc.gov/siting/local-state-gov.html>.

<sup>36</sup> [http://www.fcc.gov/Bureaus/Wireless/News\\_Releases/1998/nrwl8032.html](http://www.fcc.gov/Bureaus/Wireless/News_Releases/1998/nrwl8032.html).

and conduits during federally-funded highway construction projects.<sup>37</sup> In principle, this is an excellent idea. If sufficient capacity could be installed in the beginning, state and local governments would benefit from reduced costs arising from disruption to the rights-of-way, and private industry would benefit well into the future from lower construction costs and faster deployment times. The FCC could encourage local governments and industry to explore similar ideas on the local level with the goal of facilitating broadband deployment while limiting cuts to the streets. But such partnerships must be based on mutual respect and cooperation, and always guided by the public interest, not merely the communications industry's interests. Such proposals may run into objections from providers, who may be more concerned with reducing short-term costs than with long-term benefits, and who often are not sensitive to local planning needs. But with the support of the FCC -- were the federal agency to acknowledge both the multiplicity of local concerns, and the value to the public interest of a coordinated and foresighted effort -- such a partnership could prove truly innovative and beneficial. Continual attacks on local government interests, on the other hand, merely impede cooperation and progress.

### *C. The FCC Should Adopt Proposals to Reclassify Broadband Service*

While communities must retain the authority to meet local needs, Free Press and others recommended that the Commission reclassify broadband “as an information service with a telecommunications service transport component.”<sup>38</sup> Commenters here endorse this recommended reclassification of broadband service as a hybrid information/telecommunications service subject to Title II regulations. As pointed out in detail by Free Press, such a

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<sup>37</sup> Comments of New America Foundation, Public Knowledge, and Media Access Project at 9; Google Comments at 36; Comments of Computer and Communications Industry Association at 31. See, e.g., “Broadband Conduit Deployment Act of 2009,” H.R. 2428, 111th Cong. (2009).

<sup>38</sup> See Comments of Free Press at p. 260, Comments of Public Knowledge et. al. at pp. 23-25.

reclassification would afford the Commission additional tools for addressing areas of market failure in the provision of broadband, while maintaining the regulatory flexibility needed when dealing with a wide array of communities.

### **III. TELECOMMUNICATIONS TAXES**

In its initial comments, the American Consumer Institute claims that taxes on telecommunications services levied at the local level undermine the incentive for providers to invest or for consumers to subscribe.<sup>39</sup> AT&T recommends that Congress should make the Internet Tax Moratorium permanent, and goes on to recommend that state and local governments should not be allowed to levy taxes on telecommunications services at a rate higher than that assessed on other goods and services – all while calling for a reduction in the property tax assessment of telecommunications facilities.<sup>40</sup> Verizon likewise asks that the Commission ask Congress to impose a moratorium on new discriminatory telecommunications taxes without defining what discriminatory means.<sup>41</sup> All of these proposals are fundamentally misguided.

#### *A. Commenters' Recommendations Concerning Preemption of State and Local Communications Taxes Have No Place in a National Broadband Plan*

A few commenters claim that state and local taxes on communications services are, in their view, excessive and therefore urge that, as part of its National Broadband Plan, the Commission should recommend “the elimination of [these] excessive tax *burdens*.”<sup>42</sup> While the precise details of these commenters’ proposals are not clear, the gist seems to be that the Commission should endorse federal legislation that would preempt state and local governments

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<sup>39</sup> See Comments of American Consumer Institute at p. 34.

<sup>40</sup> See Comments of AT&T at pp. 95 -97.

<sup>41</sup> See Comments of Verizon and Verizon Wireless at pp. 127-28, 131.

<sup>42</sup> AT&T Comments at 95-97 (emphasis in original). *Accord* Verizon Comments at 129 & 130-31; ACI Comments at 2-3 & 34-40.

from taxing communications services at any rate that “exceed[s] the tax rate applied to other goods and services.”<sup>43</sup>

This self-serving plea for industry-specific federal preemptive insulation from state and local taxes rests on unsupported and inaccurate premises and represents an unsound policy that would create its own new set of economic recovery-threatening externalities. The efforts of those few commenters to transform this proceeding into one involving state and local tax structures and revenue sources, matters about which the Commission has no knowledge or expertise, are a distraction from the many other vital, broadband-specific matters at issue in this proceeding. Moreover, by threatening the tax revenue bases of already financially-strapped local and state governments, these so-called communications tax “reform” proposals are directly at odds with the Recovery Act’s other, equally important goal of stabilizing state and local government budgets.<sup>44</sup> The Commission should therefore reject commenters’ misguided invitation to inject state and local tax policy issues into this proceeding.

The fallacies of commenters’ arguments attacking state and local communications taxes are many, both legal and factual.<sup>45</sup> We refer the Commission to the attached exhibits for a more thorough analysis of those fallacies.<sup>46</sup> Here we highlight just a few of them.

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<sup>43</sup> AT&T Comments at 96. *See also* Verizon Comments at 131; ACI Comments at 36.

<sup>44</sup> American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (“Recovery Act”), at § 3(a)(5).

<sup>45</sup> One glaring flaw is that the communications industry already enjoys the tax-shielding benefits of the Internet Tax Freedom Act (codified at 47 U.S.C. § 151 note) (“ITFA”). We believe the ITFA represents bad policy. It has regressive effects, *see* note 54 *infra*, and by eroding the permissible state and local communications tax base, places upward pressure on state and local communications tax rates. In other words, the ITFA contributes to the very problem about which tax preemption supporters complain. But because the ITFA does largely shield broadband services from taxes, it confirms that commenters’ attacks on remaining state and local communications taxes here are totally out of place.

<sup>46</sup> *See* Appendix B (“Local Government Perspective on Telecommunications Taxes – A Response to Industry’s 2004 COST Study,” Summer 2006); Appendix C (Testimony of Joanne Hovis on behalf of the National Association of Telecommunications Officers and Advisors, the National Association of Counties, the Government Finance Officers Association, the U.S. Conference of Mayors and the National League of Cities, before the House Subcommittee on Commercial and Administrative Law, June 9, 2009); Appendix D (Testimony of Tillman L. Lay on behalf of the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties, the National

## *B. Commenters' Tax Preemption Proposals Are a Solution in Search of a Problem*

Commenters' attacks on state and local communications taxes, and their assertions that those taxes deter industry investment in broadband deployment and subscriber broadband demand, are belied by the industry's own data and arguments in their opening comments and by other sources as well. Supposedly "excessive" state and local taxes notwithstanding, industry comments in this proceeding repeatedly point to the tremendous growth in broadband investment, deployment and subscribership in the past several years, and how broadband investment and subscribership have continued to grow in the face of the recent economic downturn, while other sectors of the economy have declined.<sup>47</sup> A recent Pew survey revealed the same thing: Despite the recession, broadband subscribership increased by over 14% (from 55% to 63%) from a year ago, even though, in that same period, rates for broadband service also increased by 13% from a year ago.<sup>48</sup>

Such evidence of increasing broadband subscribership *and* prices in the face of an economic downturn simply cannot be squared with the claim that state and local communications

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Association of Telecommunications Officers and Advisors, and the Government Finance Officers Association, before the House Subcommittee on Commercial and Administrative Law, Sept. 18, 2008); & Appendix E (Oct. 24, 2008, letter to Subcommittee Chair Sanchez from Tillman L. Lay).

<sup>47</sup> *E.g.*, Verizon Comments at 11-23 & 72; AT&T Comments at iv-v, 9 & 78-82. *See also* Comments of Time Warner Cable, Inc. at 4 ("the development of the broadband marketplace has been a resounding and unequivocal success"); 5 (noting the "unprecedented rate" of broadband growth, and the "phenomenal and widely acknowledged proliferation of broadband networks") & 7-8 (citing Commission findings that broadband facilities have "dramatically increased" and have been deployed to a "tremendous degree"); Comments of United States Telecom Association at i-ii ("Broadband in the United States has developed with speed and scope unparalleled by any prior technology . . . [with] cumulative capital expenditures by broadband providers from 2000-2008 [of] over half a trillion dollars. . . . [A]n overwhelming majority of Americans today [over 90%] can choose among multiple broadband platform providers"); Comments of Cox Communications, attachment at 2 ("Broadband is a great American success story. . . . Since 1996, Cox has invested more than \$16 billion in its state-of-the-art broadband network. Cox High Speed Internet is available to virtually all of the 9.4 million homes its networks pass, in rural and urban communities alike"); Comments of National Cable and Telecommunications Association at 4 ("The Commission . . . should not lose sight of either the immense progress made by the private sector, or the policies that have enabled that progress"); & 10 – 13 (citing data on consistently increased access to high speed Internet through cable and telephone companies); Comments of W. Kenneth Ferree *et al.*, at 19-20 (citing data showing "enormous" growth in broadband investment and subscribership continuing into 2009) & 25 ("U.S. broadband deployment has proceeded at a remarkable rate").

<sup>48</sup> Todd Spangler, "Broadband Services Prove Resilient," *Multichannel News*, June 22, 2009, at p.3.

taxes are somehow retarding broadband investment, deployment or subscribership. To the contrary, it suggests that any preemptive reduction of state or local communications taxes would not provide any “demand-side” relief to subscribers, but would instead simply transfer revenue from already cash-starved state and local government budgets into the pockets of already large and profitable broadband service providers. Such a wealth transfer from financially-stressed state and local government budgets to already-cash-rich broadband providers would serve no interests other than those of providers’ executives and shareholders.

That state and local communications taxes have had no discernible effect on broadband or other communications-related services investment, deployment or subscribership is further confirmed by the fact that tax preemption commenters offer no evidence – and we are aware of none – remotely suggesting any sort of correlation, much less causation, between broadband or other communications service deployment and subscribership, on the one hand, and state and local communications tax levels, on the other. There is no evidence, for instance, suggesting that broadband deployment or subscribership is lower in those jurisdictions that impose broadband taxes grandfathered by the ITFA.<sup>49</sup> Nor is there is any evidence suggesting that states and localities with higher communications tax rates have lower communications or broadband-related investment or subscribership than those with lower tax rates.<sup>50</sup>

In fact, the opposite is demonstrated by both common sense and the anecdotal evidence that does exist. Communications-related taxes tend to be higher in major urban and suburban areas, and lower, or non-existent, in rural, low-density areas. Yet, as industry concedes, it is in

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<sup>49</sup> Indeed, AT&T inadvertently disproves its own hypothesis, touting Texas, one of the states with an ITFA-grandfathered tax, as “hav[ing] the second-highest number of high-speed lines in the nation” and reporting “tremendous growth of broadband provided over media other than ADSL and cable over the past two years.” AT&T Comments at 79.

<sup>50</sup> Likewise, there is no evidence showing nations with lower communications tax rates have greater broadband investment or subscribership than those nations with higher tax communications rates.

these latter, predominately low or no-tax areas, where broadband deployment and subscribership lag.<sup>51</sup>

*C. Commenters' Evidence of Supposedly Excessive State and Local Communications Taxes Is Artificially Inflated*

The few commenters that claim that the communications industry is supposedly subject to excessive state and local taxes cite, in echo chamber-like fashion, the same studies as support for that claim.<sup>52</sup> The problem, however, is that in order to conjure up those supposedly “excessive” tax rates, those studies include as “taxes” a host of charges – such as federal and state USF fees, E-911 fees, TRS fees, FCC and state PUC regulatory charges. These are not state or local “taxes” (general revenue-raising measures) in the normal sense at all but are federal and state user fees and federal taxes. Moreover, these are fees and taxes over which local (or often) state governments have no control. Tax preemption proponents are thus improperly, and disingenuously, blaming local governments, and threatening local government budgets, *not* for the communications taxes they have imposed, but for various user fees and charges imposed by federal and state governments. Why local governments should take the budgetary hit for user fees imposed by federal and state governments (including fees imposed by the FCC), tax preemption proponents do not, and cannot, explain.

*D. Any Preemption of State and Local Communications Taxes Would, by Industry's Own Admission, Cost State and Local Governments Billions of Dollars in Tax Revenue, Resulting in Massive Increases in Other State and Local Taxes and/or Drastic Reductions in Essential Services Provided by State and Local Governments, Directly Contrary to the Recovery Act's Purposes*

Even if tax preemption proponents were correct in their simplistic assertion that the communications industry is more heavily taxed than some other industries (and as we have

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<sup>51</sup> See, e.g., AT&T Comments at 82 & 85; Verizon Comments at 24-25.

<sup>52</sup> See AT&T Comments at 95-96 & nn. 272-74; Verizon Comments at 130 & n. 169; ACI Comments at 36-37 & nn. 64-65.

shown in Part III(C) above, their assertion is at best highly misleading), that assertion provides no justification for any federally-mandated lowering of state and local taxes imposed on the communications industry. Unlike the federal government, most state and local governments must balance their budgets. As a result, any federally mandated lowering of such taxes would necessarily mean that, to offset the resulting tax revenue shortfall, state and local governments would have to (a) reduce the essential public services they provide to their residents; (b) increase taxes imposed on other taxpayers; or (c) carry out a combination of service cuts and other tax increases. The problem should be apparent: State and local tax treatment of communications providers cannot meaningfully be assessed or reformed in a vacuum. If it is to be done at all, it must be done by looking at the much larger picture of a particular state or local government's entire budgetary needs and tax policies. Neither Congress nor the Commission has the ability to do that. Only state and local governments do.

Moreover, by industry's own estimates, the state and local government tax revenue shortfalls that would result from their proposed so-called "reform" of communications taxes would be enormous. Verizon, for instance, claims that the supposedly "excessive" state and local "taxes on communications services" amount to "tens of billions of dollars annually."<sup>53</sup> What Verizon and its allies studiously ignore is the obvious corollary of that claim: If, as they wish, these supposedly "excessive" taxes were preempted, the result would be a *tax revenue shortfall for state and local governments in the very same "tens of billions of dollars annually."* Furthermore, because state and local governments, unlike the federal government, must balance their budgets, they would have to make up for those billions of dollars in lost annual tax revenues either by substantially increasing the other taxes they impose, drastically reducing the essential services – police, fire, schools, health care, public works and infrastructure – that they provide to

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<sup>53</sup> Verizon Comments at 130.

their residents, or some combination of both. Taking any of these steps would create its own new demand-dampening, anti-stimulus effects. Moreover, state and local governments would have to accomplish that feat at a time when, as even tax preemption proponents concede, state and local governments are already under “enormous [fiscal] pressure” due to “budget deficits borne of spending plans accelerated during the boom years and [the current recession] driven decline in tax revenues.”<sup>54</sup>

Imposing such an enormous new budgetary shortfall on state and local governments would make no sense at any time, but especially not now during the recession. Imposing such new fiscal hardships on state and local governments, and forcing them to impose new, offsetting tax increases on *other* goods and services, would also be directly contrary to one of the express purposes of the Recovery Act itself:

To stabilize State and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.<sup>55</sup>

This Recovery Act goal is no less important, and worthy of no less weight, than the far narrower purposes of the National Broadband Plan at issue here. The Commission therefore should not, and cannot, endorse a recommendation that is itself at odds with the larger goals of the Recovery Act.

*E. Tax Preemption Proponents’ Claims about the Supposedly Outdated Justifications for, and Regressive Nature of, State and Local Communications Taxes Rest on a Fundamental Misunderstanding of Tax Policy*

Tax preemption proponents’ generalizations about state and local taxes imposed on communications providers are grossly misleading. They seem simplistically to assume that all state and local taxes imposed on communications service providers are the exclusive product of

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<sup>54</sup> ACI Comments at 35.

<sup>55</sup> Recovery Act at § 3(a)(5).

what they feel is an outdated assumption that such services used to be provided by a regulated monopoly.<sup>56</sup> That is a mistaken assumption. Tax classifications, including communications taxes, are made for a variety, and often a combination, of different reasons, many of which have nothing to do with whether services are provided by a monopoly or not.

### **1. Communications Service Providers and Utilities Receive Special State Law Privileges That Other “General” Businesses Do Not**

The vast majority of the taxes about which these commenters complain do not single out the communications industry at all. Many, in fact, are imposed on (or property tax valuation assessment methods applied to) all utility companies, including electric power, gas and water companies. The commenters presumably nevertheless believe that the communications industry should receive preferential treatment over utilities because it is no longer a monopoly. But aside from the fact that other utilities, such as electric power and gas, are likewise becoming increasingly competitive, those commenters ignore the fact that there are other obvious differences between telecommunications and utilities, on the one hand, and so-called “general” businesses, on the other, that might justify differential tax treatment.

For example, under the laws of many, if not most, states, telecommunications service providers, like classic utilities, typically receive special, unique benefits from state and/or local governments that other businesses do not. Telecommunications service providers and other utilities typically enjoy eminent domain power. And they also invariably receive the right to install millions of dollars worth of their own private profit-making assets on the public rights-of-way (“ROW”). In many states, telecommunications service providers, like other utilities, also receive special exemption from local land use laws. Each of these is, of course, an enormously valuable special privilege that other “general” businesses do not enjoy.

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<sup>56</sup> AT&T Comments at 96; Verizon Comments at 129; ACI Comments at 36.

Two conclusions should be apparent: First, if telecommunications providers were to continue to receive these enormously valuable benefits under state and local government law and yet, by federal fiat, be permitted to pay the same tax rate that so-called other “general” businesses pay, then telecommunications providers would enjoy huge preferential advantages, in terms of the economic benefits they receive from state and local governments in return for the taxes they pay, over all other such hypothetical “general” businesses.<sup>57</sup> Second, although telecommunications providers claim that, because they are no longer monopolies, they deserve the same tax treatment as the competitive corner drug store, none proposes to relinquish any of the special “monopoly” utility benefits of eminent domain, ROW access, and other special state law privileges they continue to enjoy.

## **2. Imposing High Taxes on Communications and Other Utility-Type Services Makes Local Transaction Tax-Based Systems Less, Not More, Regressive**

The special and preferential economic benefits given to telecommunications providers and other utilities by state and local law are far from the only rational reason for classifying them differently for tax purposes. Imposing higher transaction tax rates on telecommunications and other utility services may serve other important tax policies as well.

One relates to relative tax distribution effects. Contrary to the claims of communications tax preemption proponents,<sup>58</sup> forcing state and local governments to move toward a single business transaction tax rate would make their transaction-based tax systems *more*, not less, regressive. Because most local governments and many state governments are restricted by state law or state constitution to relying on more regressive transaction tax systems rather than more progressive income tax systems, their ability to create different tax classifications among

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<sup>57</sup> The proprietor of such a hypothetical “general” business would no doubt like the ability to be able to condemn the property of others, to be able to construct his plant on public property for free or at subsidized rates instead of market rates, or to be able to receive a special exemption from local land use laws.

<sup>58</sup> Verizon Comments at 130; ACI Comments at 36-37.

transaction taxes (in other words, having different transaction tax rates for different categories of goods and services) is typically the only means available for many local and state governments to soften the inherent regressivity of their transaction-based tax systems.

Taxing telecommunications and other utility services at a higher rate than general sales taxes is a classic example. Unlike the case with many other consumer goods and services, business enterprises consume proportionately more telecommunications and other utility services than do residential taxpayers, and proportionately less of most retail goods and services subject to general sales and use taxes than residential taxpayers. As a result, imposing a higher telecommunications and/or utility tax than a general sales tax tends to shift the overall local tax burden more to business taxpayers and away from residential taxpayers, thereby lessening somewhat the regressivity of a transaction-based tax system. On the other hand, requiring that telecommunications and other utility-type services be taxed at the same rate as all other consumer goods and services has the opposite effect: It would shift the overall local tax burden away from business taxpayers and toward residential taxpayers, making a transaction-based system more regressive.<sup>59</sup>

That income taxes might be more progressive than transaction-based telecommunications and utility taxes<sup>60</sup> is beside the point, because income taxes are not a legally available option for most local governments. Unless tax preemption proponents also are willing to advocate a federal law mandating that all states and localities must shift from transaction tax-based to income

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<sup>59</sup> For somewhat different reasons, the ITFA likely has regressive tax effects as well. Typically older and/or less well-to-do residents continue to rely more heavily on plain old telephone services to communicate and thus must continue to pay local telecommunications taxes, while businesses, as well as typically younger and/or more well-to-do residents, tend to rely on Internet access for most of their communications needs and are thus largely shielded by the ITFA from local telecommunications taxes.

<sup>60</sup> See Robert W. Hahn *et al.*, American Enterprise Institute for Public Policy Research, *Bandwidth for the People* at 3-4 & n. 3, available at <http://www.aei.org/article/21593> (cited in AT&T Comments at 96 n. 273). The Hahn article, ironically, also questions the continuing validity of the conclusions in Austan Goolsbee, Nat. Bureau of Economics Research, Working Paper No. 11994, *The Value of Broadband and the Deadweight Loss of Taxing New Technology* (2006), on which AT&T relies in its Comments (at 95 n. 269).

tax-based systems, their professed concerns about the supposed “regressivity” of utility-type transaction taxes is sheer hypocrisy.

### **3. Transaction Taxes on Telecommunications and Other Utility-Type Services Yield More Stable Tax Revenues than General Sales and Use Taxes**

Telecommunications and other utility-type taxes also typically generate more stable and recession-resistant tax revenue streams than general sales and use taxes on most other consumer goods. For any taxing authority, tax revenue stability and predictability are, of course, very desirable and important attributes for a tax to possess.

The reason for the relative stability and predictability of telecommunications/utilities taxes is that, as essential services, demand for telecommunications and other utility-type services tends to be more inelastic, and recession-resistant, than demand for other retail goods or services subject to general sales and use taxes. And this trait of telecommunications services is not altered by competition: Competition may increase the elasticity of demand for an individual telecommunications service provider’s services, but there is no evidence that it increases the elasticity for telecommunications services as a whole.

Moreover, the record in this proceeding confirms the stability, and recession-resistant nature, of communications sector revenue streams. As noted above in Part III(B) above, unlike almost all other sectors of the economy, broadband and communications service investment, subscribership *and* prices have continued to grow steadily during the recession.

These, of course, are far from the only potential justifications for state and local tax policies relating to telecommunications providers and their services and property. Nor do all states or localities subscribe to these justifications or adopt tax policies consistent with them. The point is a much more basic one: State and local tax policies are a product of several different, and sometimes conflicting, policy goals, and each local jurisdiction may balance those

goals differently, depending on the preferences of its voters.<sup>61</sup> Neither the Commission, nor Congress, is in a position to second-guess those local legislative judgments, unless those judgments can be shown to impede the growth and development of broadband or other communications services.

That is clearly not the case. As we have already shown in Part III(B) above, the broadband telecommunications industry sector has enjoyed increasing demand *and* prices in the face of the recession. This countercyclical growth has occurred even though, according to tax preemption proponents, the broadband/telecommunications industry has at the very same time faced allegedly heavier tax burdens than other industries. That leads to one of two conclusions, either of which is fatal to tax preemption proponents' complaints about state and local taxes: (1) these claims about the industry's supposedly heavy state and local tax burdens are inaccurate; or (2) industry's supposedly heavier state and local tax burdens have not inhibited its ability to continue to grow and expand far more rapidly than other industrial sectors that supposedly have lesser tax burdens. Regardless of which proposition is more accurate (it may well be a mixture of both), the outcome is the same: There is no justification for federal intrusion into state or local taxes in this area.

#### **IV. OPEN NETWORKS AND NETWORK MANAGEMENT<sup>62</sup>**

Numerous commenters addressed the question of open network principles and the need to manage network traffic. Clearwire states its support for a commitment to open networks.<sup>63</sup>

Level 3 suggests that, beyond allowing consumers to attach any device they wish to a broadband

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<sup>61</sup> See The White House, Office of the Press Secretary, Memorandum for the Heads of Executive Departments and Agencies, Subject: Preemption (May 20, 2009) ("in our Federal system, the citizens of the several States have distinctive circumstances and values, and . . . in many instances it is appropriate for them to apply to themselves rules and principles that reflect those circumstances and values").

<sup>62</sup> At this time, the U.S. Conference of Mayors has no official position on the issues of open networks and network neutrality. As such, this section does not reflect their views.

<sup>63</sup> See Clearwire Comments at p. 11.

network, the marketplace should be left to shape best practices in the area of network management.<sup>64</sup> AT&T urges continued reliance on the Commission's *Broadband Policy Statement* and its *post hoc* enforcement, and discourages imposition of a "dumb pipe" requirement for fear of its impact on streaming applications.<sup>65</sup> Verizon suggests that imposing an open network requirement would discourage further network upgrades since operators would no longer gain a competitive advantage in the intermodal marketplace, but supports continued reliance on the *Broadband Policy Statement*.<sup>66</sup> Other commenters, like Time Warner Cable,<sup>67</sup> Cisco Systems,<sup>68</sup> and the Fiber To The Home Council<sup>69</sup> also urge continued use of the *Broadband Policy Statement* without any additional regulation.

Several commenters claim that any requirements for network openness and neutrality would inhibit innovation in applications and services and lead to diminished investment in advanced broadband networks<sup>70</sup>. But open access networks and interconnection are important to arrive at active competition at the service layer which will lead to innovation in broadband services and greater wealth creation. While Commenters recognize that we may need to take an evolutionary path to open networks, we are convinced that at the end of the day open access networks will most benefit society.

We also differ with several other commenters regarding the need for network neutrality guarantees. We acknowledge that in some cases applications such as public safety communications and premium services like videoconferencing and gaming may require some level of prioritization due to their need for low latency and/or uniform bit rates. We also

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<sup>64</sup> See Level 3 Comments at pp. 9-15.

<sup>65</sup> See AT&T Comments at pp. 102, 111.

<sup>66</sup> See Verizon and Verizon Wireless Comments at p. 83.

<sup>67</sup> See Time Warner Cable Comments at p. 27.

<sup>68</sup> See Cisco Comments at p. 17.

<sup>69</sup> See Comments of the FTTH Council at p. 33.

<sup>70</sup> See Comments of Level 3 at pp. 11-12.

understand that in bandwidth-constrained networks such prioritization may result in less bandwidth allocation to other services and applications. However, we believe that rules must be enforced to provide equal treatment of network packets to the maximum extent possible taking legitimate network management practices into account.

The Commission must strive to clearly define the line between legitimate network management practices and unreasonable interference in network communications designed to obtain a competitive advantage for network owners and operators. The Commission must then make its *Broadband Policy Statement* enforceable and also add a fifth non discrimination rule requiring that all packets be treated equally to the maximum possible extent. As broadband services evolve and the Internet transitions to a two-way video platform, the potential for unreasonable and unnecessary interference from network owners will increase. If strong enforcement tools are not used, such interference will distort the evolutionary path of the Internet, stifle creativity and innovation and ultimately abridge the ability of the Internet to be a platform for the expression of diverse thought and opinion.

*A. The Commission Should Not Rely on Industry Promises that Market Competition Will Ensure Sufficient Openness*

Verizon indicates<sup>71</sup> that no open requirements are needed because competitive market forces and consumer preferences will lead to industry responses for more openness. The company claims that subscribers will simply exercise their choice and switch providers if they are unsatisfied with the level of openness that they experience on a given network. These comments are based on the erroneous assumption that we have arrived at a competitive market in broadband services. In reality, we know that most communities are served by a duopoly in landline broadband providers. Since neither wireless networks nor satellite can serve as

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<sup>71</sup> See Verizon Comments at p. 87.

substitutes for landline broadband networks, the only “choice” a customer has is to subscribe to another vertically-integrated and closed network or settle for lower Internet speeds.

*B. The Commission Can Not Rely Solely on Industry Assurances that the Commission’s Broadband Policy Principles will Curb Anti-Competitive Behavior. Enforceable Regulations are Required*

Several commenters claim that no further action is needed beyond the Commission’s *Broadband Policy Statement* to curb anticompetitive behavior on the part of network owners.<sup>72</sup>

While we agree that the Commission must guard against the possibility that network neutrality regulation results in unintended adverse consequences to a user’s Internet experience, recent history provides ample evidence that without strong, enforceable network neutrality protections existing providers will use their market power to act in ways that are contrary to the public interest. The examples below from the recent past serve to illustrate why strong, enforceable protections are essential.

- a. In October 2007,<sup>73</sup> reports began circulating that Comcast was degrading and blocking Bit Torrent and other peer to peer transmissions. Showing an alarming lack of respect for its customers, Comcast sent packets with RST flags to customer computers to deceive them into thinking that the computer of the user with whom they were communicating had terminated a session. It was equivalent of impersonating one party in a phone call and telling the other party that it is time to hang up. Comcast continued to deny blocking or degrading Bit Torrent traffic even after the Associated Press proved that this discrimination was taking place. Comcast has also challenged in court the Commission’s authority to impose any penalties for such blatant discrimination.
- b. In September 2007, the New York Times reported that Verizon denied a request by Naral Pro Choice America to use a text messaging program on the Verizon network on the grounds that it alone could decide if content on its network was unsavory or controversial and subject to censorship.<sup>74</sup> The article notes that the “laws that forbid common carriers from interfering with voice transmissions on ordinary phone lines do not apply to text messages.” While the Commission’s Broadband Policy principles can forestall such

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<sup>72</sup> See Comments of AT&T at p. 33.

<sup>73</sup> See “Evidence mounts that Comcast is targeting BitTorrent traffic”, Jacqui Cheng, ArsTechnica, published October 19, 2007, available at <http://arstechnica.com/old/content/2007/10/evidence-mounts-that-comcast-is-targeting-bittorrent-traffic.ars>.

<sup>74</sup> See “Verizon Blocks Messages of Abortion Rights Group”, Adam Liptak, New York Times, published September 27, 2007, available at <http://www.nytimes.com/2007/09/27/us/27verizon.html?ex=1348545600&en=800fc3af2fc8265d&ei=5088&partner=rssnyt&emc=rss>.

behavior in the short term, without enforcement capability, providers like Verizon are able to change their minds in the future.

- c. In August 2007, AT&T deliberately censored a webcast featuring the band Pearl Jam that contained lyrics critical of then-President George Bush. This type of censorship is permissible under current FCC standards – and has the potential to curtail the power of the Internet to be a medium for the diverse thought and opinion so essential to a democratic society.

### *C. The Commission Should not Accept as Fact Industry Arguments That Open Access Requirements will Stifle Investment in Advanced Networks*

Open access networks are relatively new here but are gaining traction in Europe and other parts of the world. None other than Sir Michael Rake, chairman of BT (British Telecom) is citing the benefits of the open access model. According to a report on the Washington Post website:<sup>75</sup>

Five years ago, Britain's largest telecommunications service provider was forced to do what at the time seemed like a losing proposition. Regulators required BT, formerly called British Telecom, to open its networks to competitors to lease, and for use by any device and software application. By doing so, BT and many analysts at the time predicted the company's demise, saying it would lose its monopoly power over the industry and its revenue streams from proprietary hardware contracts. The company would become a network of dumb pipes, some feared. Today, BT generates annual revenues of about 20 billion British pounds, the same as five years ago. What's different is that many more competitors have entered into the wireless, phone, and broadband Internet markets in the U.K.

The article goes on to quote Sir Rake:

It [moving to open access] was painful at the time but has been better for the country and consumers in the long run...There needs to be a level playing field and the simple thing to do to achieve that is to open access...It's the only way to create competition and thereby create investment and jobs.

Commenters therefore urge the Commission to explore whether greater network openness will result in equal treatment of bit transport for all providers of like services; and the degree to which it can promote the creation of next generation broadband networks capable of providing 100 Mbps and above to each user to eliminate the existing bandwidth constraints that give rise to

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<sup>75</sup> See " British Telecom Chairman Says Open Access Key to Broadband Growth", Cecilia Kang, Post I.T. on [washingtonpost.com](http://voices.washingtonpost.com/posttech/2009/05/british_telecom_chairman_rake.html), posted May 1, 2009, available at [http://voices.washingtonpost.com/posttech/2009/05/british\\_telecom\\_chairman\\_rake.html](http://voices.washingtonpost.com/posttech/2009/05/british_telecom_chairman_rake.html).

legitimate as well as specious reasons to discriminate against certain applications, services and content.

## **V. CONCLUSION**

The National Broadband Plan that will result from this process is a once-in-a-lifetime opportunity to meet the current and evolving communications needs of all Americans, be they urban or rural, wealthy or impoverished. Broadband possesses a singular ability to transform lives unlike any communications medium seen before, and this Plan must see to it that the transformative power of broadband is brought to every corner of our country. Local governments have and will continue to assist in meeting those needs, and hope that the Plan not only acknowledges this important role but provide our communities with the tools we need to ensure that every citizen has the essential benefits broadband has to offer.

Respectfully submitted,

Tonya Rideout  
Acting Executive Director

John D. Russell  
Government Relations Advisor

NATOA  
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Suite 401  
Alexandria, VA 22314

July 21, 2009

**APPENDIX A**

**LIST OF ADDITIONAL SUPPORTERS**

Access Humboldt (representing Humboldt County and the Cities of Eureka, Arcata, Fortuna, Rio, Dell, Ferndale and Blue Lake, CA), City of Albuquerque, NM, Houston Harris County Regional Coalition (representing the City of Houston, TX, Harris County, TX, Harris County Department of Education, Houston Community College, and the Texas Medical Center), Howard County, MD, City of Los Angeles, CA, City of Mentor, OH, Municipal Services Associates, Inc., PROTEC, TeleCommUnity.

**APPENDIX B**

**LOCAL GOVERNMENT PERSPECTIVE ON TELECOMMUNICATIONS TAXES  
A RESPONSE TO INDUSTRY'S 2004 COST STUDY  
SUMMER 2006**

**APPENDIX C**

**TESTIMONY OF JOANNE HOVIS ON BEHALF OF THE NATIONAL ASSOCIATION  
OF TELECOMMUNICATIONS OFFICERS AND ADVISORS, THE NATIONAL  
ASSOCIATION OF COUNTIES, THE NATIONAL LEAGUE OF CITIES, THE UNITED  
STATES CONFERENCE OF MAYORS, AND THE GOVERNMENT FINANCE  
OFFICERS ASSOCIATION, BEFORE THE HOUSE SUBCOMMITTEE ON  
COMMERCIAL AND ADMINISTRATIVE LAW  
JUNE 9, 2009**

**APPENDIX D**

**TESTIMONY OF TILLMAN L. LAY ON BEHALF OF THE UNITED STATES  
CONFERENCE OF MAYORS, THE NATIONAL LEAGUE OF CITIES, THE  
NATIONAL ASSOCIATION OF COUNTIES, THE NATIONAL ASSOCIATION OF  
TELECOMMUNICATIONS OFFICERS AND ADVISORS, AND THE GOVERNMENT  
FINANCE OFFICERS ASSOCIATION, BEFORE THE HOUSE SUBCOMMITTEE ON  
COMMERCIAL AND ADMINISTRATIVE LAW  
SEPTEMBER 18, 2008**

**APPENDIX E**

**LETTER FROM TILLMAN L. LAY TO SUBCOMMITTEE CHAIR SANCHEZ  
OCTOBER 24, 2008**



**LOCAL GOVERNMENT PERSPECTIVE  
ON TELECOMMUNICATIONS TAXES**

*A Response to Industry's 2004 COST Study*

Summer 2006

Sponsored by:

National Association of Counties  
National League of Cities  
United States Conference of Mayors  
Government Finance Officers Association  
National Association of Telecommunications Officers and Advisors



## 1.0 Introduction

The telecommunications industry is conducting a multipronged effort to reduce the level of taxes it pays to local governments. Large sums of money are being poured into national and local advertising in a highly targeted media and lobbying campaign. In addition, the telecommunications industry is litigating against local governments to contest taxes and fees. The industry is also lobbying the federal and state governments to obtain favorable legislation to accomplish the same result.

As with any business, telecommunications companies need to pay their fair share of taxes.

As with any business, telecommunications companies need to pay their fair share of taxes. Recognizing the convergence among different types of telecommunications services, local governments generally favor the imposition of taxes on a nondiscriminatory basis, regardless of the technologies used, on competing communications service providers that offer functionally equivalent services. They also favor reforms that will create a level playing field for competition among existing and new service providers. Further, they favor simplifying the administration of state and local taxes on communications services to encourage continued investments and innovations.

In this context, it is critical that industry viewpoints be carefully scrutinized. The industry commissioned a study, published in March 2005 by the Telecommunications Tax Task Force of the Council on State Taxation (COST), titled *2004 State Study and Report on Telecommunications Taxation* (the COST Study).<sup>1</sup>

As it states, the COST Study is intended to persuade policymakers to lower the tax burdens on the telecommunications industry:

The state and local tax laws continue to impose high levels of industry-specific taxation on telecommunications services. While some states have begun the process of reforming the state and local tax structure, much more is needed to reduce the high levels of telecommunications taxation...<sup>2</sup>

The COST Study summarizes its most important finding as follows:

The 2004 State Study shows that the average effective rate of state and local transaction taxes is 14.71%, compared to only 6.12% for general businesses nationwide.<sup>3</sup>

<sup>1</sup> The following companies participated in the study: ALLTEL Corporation, AT&T Corporation, BellSouth Corporation, Cingular Wireless LLC, Level 3 Communications, Nextel Communications, Qwest Communications, SBC Communications, Sprint Corporation, Telephone and Data Systems, Inc., T-Mobile USA, Verizon Communications, and Verizon Wireless.

<sup>2</sup> *2004 State Study and Report on Telecommunications Taxation*, Council on State Taxation, 2005, p. 7.

<sup>3</sup> *Ibid.*, pp. 3-4.

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The COST Study contains serious methodological flaws that make it an inappropriate basis for policy decisions.

This White Paper presents a preliminary response from local governments to the 2004 COST Study and that core finding. The COST Study contains serious methodological flaws that make it an inappropriate basis for policy decisions, especially the industry's proposals to make widespread changes to local tax structures. The COST Study presents a selective summary of state and local fees and taxes that omits important analytic issues. Moreover, it neglects to highlight parts of the tax system that favor telecommunications companies compared to other businesses.

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## 2.0 Local Government Response to 2004 COST Study: A Summary

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The following problems were identified by the local government organizations that examined the 2004 COST Study:

- ❖ **“Transaction Taxes:”** The COST Study's analysis of “transaction taxes” is flawed because it mixes *taxes*, which apply to a broad range of businesses, with *user fees*, which are the charges that local governments levy for use of public rights-of-way by private users such as telecommunications companies. The COST Study fails to define “transaction taxes” consistently for telecommunications companies and other businesses.
- ❖ **Income Taxes:** The COST Study fails to disclose that telecommunications companies pay significantly lower corporate income taxes than other businesses.
- ❖ **Property Taxes:** The COST Study's analysis of property taxes shows, by its own numbers, that there is no discrimination against telecommunications companies in real property taxes and little disparity, if any, in other property taxes.
- ❖ **Overall Impact on Local Governments:** Because of the flaws of the COST Study with respect to (1) user fees and other fees and (2) income taxes, its estimates of relative tax burdens are incorrect. However, even if taken at face value, the COST Study's data show a tremendous impact on the ability of local governments to provide needed services to their constituents due to lost revenue if the telecommunications industry's recommendations were followed.
- ❖ **The Effects of Changing Technology:** Currently, technological convergence is creating new forms of competition among different types of telecommunications as voice, data, and video are offered over a much broader range of media, including traditional land lines, wireless, cable, satellite, and voice-over-Internet-protocol (VoIP) services. Each of these services is subject to a different set of state and local taxes. In addition, the federal government is showing a disturbing pattern of intervention in state and local revenue policy that has the potential to exacerbate rather than reduce these tax differentials. In this context, negotiations among state and local government groups and telecommunications companies represent the best way to reduce administrative burdens and promote equitable taxation.

The sections that follow consider each of these points in turn.

### 3.0 “Transaction Taxes”

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As stated above, the COST Study’s analysis of “transaction taxes” mixes *taxes*, which apply to a broad range of businesses, with *user fees*, which are the charges that local governments levy for use of public rights-of-way by private users such as telecommunications companies. The COST Study raises significant methodological issues when it fails to define “transaction taxes” consistently for telecommunications companies and other businesses. The result of this shortcoming is that the numbers produced by the COST Study indicate much heavier relative burdens on telecommunications companies, compared to other business companies, than are actually the case.<sup>4</sup>

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The COST Study as a whole is based on a fallacious argument.

Before discussing these individual issues, however, it should be noted that the COST Study as a whole is based on a fallacious argument. The COST Study argues that tax burdens should be applied consistently across different companies. Of course, this is not really true. The Supreme Court has repeatedly upheld the power of state legislatures to classify taxpayers according to local needs and conditions. In the 1983 case of *Regan v. Taxation With Representation*, the court reiterated that “legislatures have especially broad latitude in creating classifications and distinctions in tax statutes.”<sup>5</sup> Indeed, many types of businesses are subject to their own special taxes, including not only the so-called “sin taxes” of tobacco and alcohol but also travel, hotel, entertainment, petroleum distribution, transportation, and non-telecom public utilities.<sup>6</sup> Therefore, claiming that the tax burden for the telecommunications industry should be comparable with other businesses is not a valid argument. Nevertheless, this White Paper considers the COST Study’s other claims.

#### 3.1 Significant Portions of So-Called “Taxes” Are User Fees

The COST Study creates an artificial construct that it calls “transaction taxes.”<sup>7</sup> It applies this term to the tax burden on telecommunications companies compared to the tax burden on other businesses.

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The COST Study defines “transaction taxes” inconsistently.

The COST Study undercuts its own call for consistency by defining “transaction taxes” differently for telecommunications companies and for other businesses. The COST Study defines “transaction taxes” on telecommunications companies as the total of “any state and local taxes applied to the cost of service or the

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<sup>4</sup> This methodological shortcoming also means that the COST Study includes user fees in its calculations for telecommunications companies to produce a higher total *number* of transaction taxes compared to the calculation for other businesses, where the definition of “transaction tax” does not include user fees.

<sup>5</sup> 461 U.S. 540, 547 (1983). The court went on to quote with approval the following language from *Madden v. Kentucky*, 309 U.S. 83, 87 -88 (1940):

The broad discretion as to classification possessed by a legislature in the field of taxation has long been recognized.... [T]he passage of time has only served to underscore the wisdom of that recognition of the large area of discretion which is needed by a legislature in formulating sound tax policies. Traditionally classification has been a device for fitting tax programs to local needs and usages in order to achieve an equitable distribution of the tax burden. It has, because of this, been pointed out that in taxation, even more than in other fields, legislatures possess the greatest freedom in classification.

<sup>6</sup> Tillman L. Lay, “Some Thoughts on Our System of Federalism in a World of Convergence,” *Law Review of Michigan State University-Detroit College of Law*, Spring 2000, pp. 223-237, at p. 231-2.

<sup>7</sup> 2004 *State Study and Report on Telecommunications Taxation*, Council on State Taxation, 2005, pp. 3-4.

provision of the line to the consumer.” By contrast, the COST Study defines transaction taxes on general businesses much more narrowly, as merely “the traditional sales tax imposed on sales of tangible personal property and comparable transaction taxes.”<sup>8</sup>

Thus, “transaction taxes” for telecommunications include not only sales taxes but also user fees that states and localities may impose on companies in return for their use of public rights-of-way. Other businesses—in general—do not use the public rights-of-way to nearly the extent that telecommunications companies do.

### 3.2 User Fees

For telecommunications companies, user fees are required when a company uses streets or overhead wires or other parts of public rights-of-way in its business. These user fees include payments for use of public rights-of-way that sometimes, but not always, may be denominated as “taxes.” User fees may be assessed as franchise fees, permit fees, infrastructure maintenance fees, or gross receipts taxes, for example, depending on the jurisdiction. Other businesses that use public rights-of-way, such as gas and electric companies, also pay user fees.

In addition to charging for use of public rights-of-way, federal law permits states and localities to impose 911 emergency system surcharges or universal service fees. Both of these are used to help build and maintain the public telecommunications network. They directly benefit the users of telecommunications services. This is similar, for example, to the use of gasoline taxes to help build and maintain the network of roads and other infrastructure that are needed to serve automobile traffic.

In preparing this White Paper, officials from a number of local and state governments and local government associations contributed their insights to help identify which charges were improperly categorized in the COST Study as taxes instead of user fees.

As can be expected from the different revenue policies adopted across the country, the results vary from state to state and locality to locality. New York State published a study in 2001 that shows the gap between sales taxes and other transaction revenues that can be considered user fees rather than taxes. That study concluded as follows:

Computations from governmental sources indicated that the total amount of local telecommunications taxes and fees was slightly over \$1 billion [in 1998]. Nearly two-thirds of these revenues came from two sources—the sales tax and the real property tax.<sup>9</sup>

Setting aside the \$306.5 million in property taxes from the \$1.039 billion in local fees and taxes that year, this means that New York State’s local governments collected some \$732 million from telecommunications companies that year, of

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<sup>8</sup> *Ibid.*, p. 4.

<sup>9</sup> New York State Department of Taxation and Finance and New York State Office of Real Property Services, *Local Telecommunications Taxes and Fees in New York State*, report to Governor George E. Pataki and the New York State Legislature, January 2001, p. 3.

which the state attributes only \$350 million, or 47 percent, to sales taxes.<sup>10</sup> The remainder of the revenues collected can be attributed to user fees rather than the kind of tax revenues paid by other businesses.

In another example, data from the State of Florida indicate a significant but somewhat lower percentage of user fees. In 2000, the Florida legislature passed the Communications Services Tax Simplification Law.<sup>11</sup> The legislation created a new tax structure for communications services, combining seven different state and local taxes or fees and replacing the revenues with a two-tiered tax composed of a state tax and a local option tax on communications services. According to one estimate, somewhat less than 25 percent of the new Communications Services Tax represents user-fee revenues while the remainder represents tax revenues.<sup>12</sup>

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User fees reflect the special burdens that telecom companies impose on the public and local governments.

Thus, in two major jurisdictions that have reviewed this question, it has been found that a substantial fraction of local government revenues comes from user fees rather than taxes on telecommunications companies. User fees, especially for the public rights-of-way, reflect the special burdens that telecommunications companies impose on the public and local governments. Telecommunications companies also derive special benefits from the use of the public rights-of-way.

### 3.3 Impact on Constituents

Telecommunications companies burden the public in ways that general business does not. For example:

- ❖ Telecommunications companies frequently cut open sections of street pavements either to install new services or to access existing infrastructure. Even though the companies fill in the cuts, the pavement within and beside the cuts often fails prematurely. For example, a City of Cincinnati study found that “street pavements with cuts exhibit a 33% loss in their remaining service life.”<sup>13</sup>
- ❖ Installation of telecommunications infrastructure, such as cables, causes lane closures and significant delays to the traveling public.
- ❖ Closing of street lanes due to installation of telecommunications infrastructure costs both public and private revenues (e.g., parking meter revenues, disruption of private commercial businesses).
- ❖ Installation of telecommunications infrastructure has led to serious accidents and damage to water mains, power lines, gas lines, phone lines, steam lines, and sewers.<sup>14</sup>

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<sup>10</sup> See Table 1, *ibid.*, p. 4. The distribution of a small amount of listed taxes and fees collected by New York City is not clear from this table.

<sup>11</sup> Codified at Chapter 202, Florida Statutes.

<sup>12</sup> Interview with Christian Weiss, Chief Economist, Office of Tax Research, Department of Revenue, State of Florida, October 2005.

<sup>13</sup> Arudi Rajagopal, “A Rational Permit Fee Structure for the Street Right-of-Way Permit Program,” *Public Works Management and Policy*, vol. 8, no. 3, January 2004, pp. 203-215, at p. 210.

<sup>14</sup> See, e.g., TeleCommUnity, “The Case for Rights-of-Way Management: A Collection of Illustrative Incidents Arising from Street Cuts,” available at <http://www.TeleCommUnityAlliance.org>.

Occupation of public rights-of-way by infrastructure of a telecommunications company denies use of that space, and potentially space above and below it, for other uses. For example, the need for access to underground cables and other infrastructure limits the location of light rail lines, transit-related infrastructure such as stations and shelters, foundations for overpasses, streetlight foundations, etc.

In other words, it is entirely appropriate for local governments to charge user fees for use of the public rights-of-way. The portion of “transaction taxes” attributable to user fees should be deducted from the COST Study numbers to make the comparison consistent between telecommunications companies and other businesses that do not impose the same burdens on the public.

### **3.4 User Fees and Taxes Are Enacted for Different, Legitimate Purposes**

The point is well settled that taxes and fees are quite different sources of revenue. In a case involving a gross receipts tax that the City of St. Louis imposed on telegraph companies, the Supreme Court decided over a hundred years ago that it is legitimate for a locality to impose such user fees:<sup>15</sup>

All that we desire or need to notice is the fact that this use is an absolute, permanent, and exclusive appropriation of that space in the streets which is occupied by the telegraph poles. To that extent it is a use different in kind and extent from that enjoyed by the general public. Now, when there is this permanent and exclusive appropriation of a part of the highway, is there in the nature of things anything to inhibit the public from exacting rental for the space thus occupied? Obviously not.<sup>16</sup>

The court had little difficulty with the fact that the rental fee had been denominated as a gross receipts “tax.” It clearly distinguished the difference between taxes and fees on analytical grounds, something that the 2004 COST Study fails to do:

“A tax is a demand of sovereignty; a toll is a demand of proprietorship.” [citations omitted] If, instead of occupying the streets and public places with its telegraph poles, the company should do what it may rightfully do, purchase ground in the various blocks from private individuals, and to such ground remove its poles, the section would no longer have any application to it. That by it the city receives something which it may use as revenue does not determine the character of the charge or make it a tax. The revenues of a municipality may come from rentals as legitimately and as properly as from taxes.<sup>17</sup>

It should be added that the distinction between taxes and user fees remains a feature of current law. For example, *TCG Detroit v. City of Dearborn*, 206 F 3d 618 (6th Cir, 2000) upheld a franchise fee imposed by the City of Dearborn on a telecommunications company as “fair and reasonable” under the terms of the Federal Telecommunications Act of 1996.<sup>18</sup>

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<sup>15</sup> *City of St. Louis v. Western Union Tel. Co.*, 148 U.S. 92 (1893)

<sup>16</sup> 148 U.S. at 99

<sup>17</sup> 148 U.S. at 97

<sup>18</sup> The 1996 Act, as codified at 47 U.S.C. Section 253, provides in pertinent part that:  
(a) In general: No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.

Following the established legal distinction, the U.S. Government Accountability Office (formerly the General Accounting Office) has rendered an opinion that distinguishes the immunity of the U.S. government from local taxes under the Supremacy Clause of the U.S. Constitution and rights-of-way charges that the U.S. government is obligated to pay when they are imposed by the District of Columbia government.<sup>19</sup>

### 3.5 *User Fees Are Not Limited to Cost*

The question then becomes whether it is somehow improper for localities to impose user fees that are higher than the locality's own costs for use of public rights-of-way. Here too the answer is well settled: The owner of property, whether a private owner or a governmental one, may charge market rates for the use of its property.

Similar to the state and local governments that are the focus of the 2004 COST Study, the federal government also has spoken clearly in this regard. The U.S. Office of Management and Budget (OMB) issued Circular No. A-25 in 1998, establishing federal policy regarding fees assessed for government services and for sale or use of government goods or resources. That circular prescribes:

Except [for exceptions as a courtesy to foreign governments or as may be approved by OMB], *user charges will be based on market prices...* when the Government, not acting in its capacity as sovereign, is leasing or selling goods or resources, or is providing a service (e.g., leasing space in federally owned buildings). Under these business-type conditions, *user charges need not be limited to the recovery of full cost and may yield net revenues.*<sup>20</sup> (emphasis added)

In summary, the 2004 COST Study fails to add to the policy debate because it inappropriately mixes user fees and state and local taxes when calculating the "transaction tax" burden on telecommunications companies and other users of public property for private gain. User fees, especially when collected on the basis of market prices, are a substantial part of the revenues that local governments collect from telecommunications companies. These user fees, as the U.S. Supreme Court observed long ago, are as legitimate as tax revenues; similar to tax payments, telecommunications companies may either pass these costs of doing business on to their customers or deduct them from their income taxes.

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(b) State regulatory authority: Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254 of this title, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers.

(c) State and local government authority: Nothing in this section affects the authority of a State or local government to manage the public rights-of-way or to require fair and reasonable compensation from telecommunications providers, on a competitively neutral and nondiscriminatory basis, for use of public rights-of-way on a nondiscriminatory basis, if the compensation required is publicly disclosed by such government.

<sup>19</sup> U.S. General Accounting Office, "911 Emergency Surcharge and Right-of-Way Charge," B-288161, April 8, 2002.

<sup>20</sup> U.S. Office of Management and Budget, "User Charges," OMB Circular A-25, July 8, 1993.

## 4.0 Income Taxes

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The COST Study fails to disclose that telecommunications companies pay significantly lower corporate income taxes than other businesses.

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Telecommunications companies on average pay substantially lower corporate income taxes than other companies.

The 2004 COST Study concedes in the section on methodology and assumptions that it “does not include income taxes.”<sup>21</sup> This glaring omission undermines the usefulness of the COST Study, since it fails to provide an accurate picture of state and local taxation of telecommunications companies. Importantly, it omits a significant benefit that telecommunications companies receive under current tax policy. Telecommunications companies on average pay substantially lower corporate income taxes than other companies.

Many telecommunications companies own substantial infrastructure. They claim income tax deductions on the basis of those assets. Because of income tax treatment that permits the telecommunications companies to claim depreciation and investment tax credits on their property, some major telecommunications companies pay far less income taxes, as a percent of income, on average than do other businesses. The 2004 COST Study, which seeks to compare telecommunications tax burdens with those of other businesses, omits this important aspect of state and local taxation.

A look at the public reports of Verizon Communications, a major company with both land-line and wireless lines of business, shows the corporate income tax benefits received by this participant in the 2004 COST Study.

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In 2004, Verizon reported that its state and local tax burdens amounted to an effective rate of only 2.9%.

Verizon’s 2004 Form 10-K filed with the Securities and Exchange Commission reports the company’s tax burdens.<sup>22</sup> In 2004, the company reported that its state and local tax burdens amounted to an effective rate of only 2.9 percent. The company reported a total income tax expense of \$2.851 billion for 2004.<sup>23</sup> Moreover, the lion’s share of this—\$1.850 billion—was deferred. Deferred taxes are much less costly than taxes one must pay immediately.<sup>24</sup>

Verizon reported that much of its state and local income tax burden is deferred. In 2004, the company owed \$335 million in state and local taxes; however, \$123 million was deferred. These are tax revenues for current services, which will not be received by state and local governments for many years to come.

## 5.0 Property Taxes

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The COST Study analysis of property taxes shows, by its own numbers, that there is no discrimination against telecommunications companies in real property taxes and little disparity, if any, in other property taxes.

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<sup>21</sup> 2004 State Study and Report on Telecommunications Taxation, Council on State Taxation, 2005, p. 19.

<sup>22</sup> 2004 Form 10-K for Verizon Communications, Inc., Note 17, “Income Taxes,” pp. 192-193 (Internet version), March 2005

<sup>23</sup> The company’s income statement, also found in the Form 10-K, shows that Verizon’s net income that year was \$7.8 billion.

<sup>24</sup> If a company can defer paying taxes, it can invest the money and obtain investment income for years before the money must actually be paid to the tax authorities. As a result, government is deprived of this money during the intervening years. Other taxpayers such as general businesses generally must pay their full taxes promptly and therefore lose the benefit of deferral.

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The COST Study shows that telecommunications companies pay roughly the same percentage of property taxes as do other businesses.

The 2004 COST Study itself shows that telecommunications companies on average pay roughly the same percentage of property taxes as do other businesses. The COST Study finds that telecommunications companies pay an effective tax rate on real property (i.e., land and buildings) of 2.26 percent, compared to an effective tax rate for other businesses of 2.19 percent.<sup>25</sup> In other words, there is virtually no difference in real property tax burdens.

The effective tax rate for telecommunications companies on tangible property (e.g., furniture, fixtures, equipment) is 1.85 percent, compared to an effective tax rate for other businesses of 1.70 percent.<sup>26</sup> Again this difference, if statistically significant, is small. Taken together, the effective tax rates for real and tangible property are essentially the same between telecommunications companies and other businesses.

The COST Study does show that about one-third of the states, mostly in the Midwest and West, impose taxes on intangible property (e.g., patents, copyrights, licenses, trademarks) at somewhat higher effective rates for telecommunications companies. However, the study also shows that tax rates for intangible property are on average across the country much lower than the other property tax rates on real and tangible property.<sup>27</sup>

In addition, there is the problem of tax avoidance behavior by telecommunications companies that allows them to reduce their property tax burdens even further. As *The Boston Globe* reported,

In total, telecoms have cut their city tax bills by over \$14 million since 2003, through moves such as transferring legal title to equipment to paper companies based in Bermuda and Delaware that get more favorable tax treatment...Verizon Wireless, for example, shifted legal ownership of assets to a Bermuda-based corporation to get more favorable tax treatment and cut its Boston tax bill by 99 percent, to \$9,307 this year from over \$3 million two years ago, according to city figures.<sup>28</sup>

The different tax treatment of telecommunications companies and other utility companies also creates significant inequities:

In the case of thousands of roadside poles jointly owned by Verizon and the local electric utility, the utility pays tax on its half-interest in the pole, but Verizon doesn't. In many cases wireless companies don't pay tax on computerized switches, but they do on backup electrical generators sitting just feet away from the switches.<sup>29</sup>

Boston's Mayor Thomas M. Menino is backing a bill in the Massachusetts legislature to tax telecommunications equipment the same as the property of electric utilities and other industrial companies. This bill would raise \$140 million in revenues statewide.<sup>30</sup>

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<sup>25</sup> *2004 State Study and Report on Telecommunications Taxation*, Council on State Taxation, 2005, p. 12.

<sup>26</sup> *Ibid.*

<sup>27</sup> *Ibid.*

<sup>28</sup> Peter J. Howe, "Telecoms Slash Their Property Tax Burden," *The Boston Globe*, June 10, 2005.

<sup>29</sup> *Ibid.*

<sup>30</sup> *Ibid.*

## 6.0 Overall Impact on Local Governments

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Because of the flaws of the COST Study with respect to (1) user fees and other fees and (2) income taxes, its estimates of relative tax burdens are incorrect. However, even if taken at face value, the COST Study's data show a tremendous impact on the ability of local governments to provide needed services to their constituents due to lost revenue if the telecommunications industry's recommendations were followed.

In addition to the 2004 COST Study, the Telecommunications State and Local Tax Coalition (an industry group) prepared a study in 2001. The 2001 study quantified the amount of state and local revenues that the telecommunications industry seeks to eliminate:

An estimated 39 percent of all telecom taxes, \$7.0 billion, are *excess taxes that exceed taxes generally imposed on other businesses and their customers...*<sup>31</sup> (emphasis in original)

In other words, as of the year 2001, the telecommunications industry was suggesting that their taxes to state and local governments should be reduced by \$7 billion. If we accept the flawed study and its outcomes, as well as project the 39 percent reduction to the telecommunications industry's current state and local taxes, around \$20 billion annually, that number has now grown to around \$8 billion.

To offset the loss of \$8 billion, governments would be faced with difficult choices. They could (1) increase rates on all other taxpayers, (2) cut services, or (3) undertake a combination of both. In today's environment of resistance to increased taxation, budget cuts are the more likely scenario. There are already fiscal pressures on cities. For example, nearly one-half of all city finance officers in 2005 increased fees and charges for services to offset revenue shortfalls.<sup>32</sup>

The magnitude of these cuts is seen in the potential impact on four of the largest and most essential categories of local government employees: police officers, firefighters, elementary school teachers, and high school teachers. Figure 1 shows the median salaries and the number of each that would correspond to the financial impact of the type proposed by COST.

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It would be foolhardy to enact federal laws based upon the flawed and incomplete information in the COST Study.

In other words, if governments lost \$8 billion in revenue, they would need to shift tax burdens from telecommunications companies to other taxpayers or else cut budgets by an amount equal to the combined salaries of more than 150,000 teachers, police, and firefighters. It would be foolhardy to enact federal laws with the kind of impact that the telecommunications industry seeks, especially if based upon the flawed and incomplete information provided in the COST Study.

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<sup>31</sup> *Telecommunications Taxes: 50-State Estimates of Excess State and Local Tax Burden*, prepared by Ernst & Young LLP for the Communications State and Local Tax Coalition, November 2001, p. 1.

<sup>32</sup> Michael A. Pagano, Christopher W. Hoene, *City Fiscal Conditions in 2005*, National League of Cities, January 2006.

**Figure 1: Potential Impacts of an \$8 Billion Reduction in Telecommunications Taxes**

	Elementary School Teachers <sup>a</sup>	Secondary School Teachers <sup>a</sup>	Police Officers <sup>b</sup>	Firefighters <sup>c</sup>
<b>Median salary</b>	\$45,658	\$46,119	\$34,738	\$32,162
<b>Median salary plus benefits<sup>d</sup></b>	\$59,584	\$60,185	\$46,896	\$40,524
<b>No. corresponding to a \$0.25 billion revenue reduction</b>	4,196 teachers	4,154 teachers	5,331 police officers	6,169 firefighters
<b>No. corresponding to a \$1 billion revenue reduction</b>	19,850 teachers, police officers, and firefighters			
<b>No. corresponding to an \$8 billion revenue reduction</b>	158,800 teachers, police officers, and firefighters			

a. Source: *Mini-Digest of Education Statistics 2003*, National Center for Education Statistics, U.S. Department of Education, October 2004, Table 16, p. 20.

b. Source: *2004 Municipal Yearbook*, International City/County Managers Association (ICMA), 2004, Table 3/5. The median is for the entrance salary for police officers.

c. Source: *2004 Municipal Yearbook*, ICMA, 2004, Table 3/6. The median is for the entrance salary for firefighters.

d. Figures for police and fire benefits, as a percentage of salary, are calculated from ICMA's *Police and Fire Personnel, Salaries, and Expenditures, 2005*; figures for teacher benefits are projected to be the average, as a percent of salary, of the police and fire benefits.

## 7.0 The Effects of Changing Technology

Technological convergence is creating new forms of competition among different types of telecommunications as voice, data, and video are offered over a much broader range of media, including traditional land lines, wireless, cable, satellite, and VoIP services. Each of these services is subject to a different set of state and local taxes. In addition, the federal government is showing a disturbing pattern of intervention in state and local revenue policy that has the potential to exacerbate rather than reduce these tax differentials. In this context, negotiations among state and local government groups and telecommunications companies represent the best way to reduce administrative burdens and promote equitable taxation.

### 7.1 Shifting Technologies

This analysis would be incomplete without recognition of the larger context of the COST Study. There is no question that telecommunications companies are under serious pressure from competing technological applications that are rendering old business models increasingly vulnerable. As *The Wall Street Journal* reported, “more Americans now have cellular phones than traditional phones in their homes. Cable companies are selling phone service, while phone companies

plan to offer video in coming years. And high-speed connections make it possible to use computer software to make calls over the Internet.”<sup>33</sup>

Consider, for example, voice communications. In the interviews conducted for this White Paper, a number of respondents commented on the rapid reduction in access lines in their jurisdictions. This trend is borne out by the statistics. For example, the Federal Communications Commission reports that from year-end 2000 to year-end 2004 the number of mobile wireless telephone subscribers increased by almost 80 percent, from 101 million to 181 million subscribers.<sup>34</sup> Many of these subscribers formerly were land-line customers. The result, perceptible to local and state governments, has been a reduction in revenues that previously had been received by land-line companies and ultimately by the governments that tax those companies.

These trends are accelerating with new technologies, and especially the Internet, forcing further changes in business models. *The Economist* magazine published two reports that essentially conclude that, “There is no longer any question of whether VOIP (“voice over Internet protocol,” i.e., telephone services provided via Internet) will wipe out traditional telephony, but a question of how quickly it will do so.”<sup>35</sup>

The result of this pressure is being felt not only by telecommunications companies but also by state and local governments that are trying to adjust their tax base to take account of the migration of telecommunication services from traditional forms. State and local governments have begun to levy taxes on cell phones in addition to sales taxes, leading to industry complaints that wireless telephone services are subject to special taxes.<sup>36</sup>

## 7.2 *Shifting Tax Burdens*

On the other side, telecommunications companies are able to use the new technologies and other techniques to try to avoid their traditional tax burdens. In Massachusetts, for example, telecommunications companies, including several that participated in the 2004 COST Study, have engaged in special corporate transactions that permit them to avoid paying their usual share of property taxes. *The Boston Globe* reported:

Making aggressive use of fine print in Massachusetts tax law, telecommunications companies have managed to get \$1.3 billion in property off local tax rolls in the last two years, including \$438 million worth in Boston alone.<sup>37</sup>

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<sup>33</sup> Anne Marie Squeo, “Phone Companies Push Telecom Overhaul; Industry Wants Revamp of 1996 Act to Level Playing Field, but Cable Firms Are Cautious,” *The Wall Street Journal*, January 18, 2005, p. A4.

<sup>34</sup> Federal Communications Commission, *Local Telephone Competition: Status as of December 31, 2004*, July 2005, Table 13 (“Mobile Wireless Telephone Subscribers”).

<sup>35</sup> “How the Internet killed the phone business,” *The Economist*, September 15, 2005, p. 11. See also, “The meaning of free speech,” *ibid.*, pp. 69-71).

<sup>36</sup> Ken Belson, “The Cellphone Becomes a Taxpayer,” *The New York Times*, May 14, 2005.

<sup>37</sup> Peter J. Howe, “Telecoms Slash Their Property Tax Burden,” *The Boston Globe*, June 10, 2005.

Of course, to the extent that telecommunications companies shed their tax burdens, other businesses and consumers must pick up the slack if local governments try to avoid draconian cuts in services:

The tax-minimizing moves by companies, including Verizon Communications Inc. and its wireless affiliate, MCI Inc., Sprint Corp., and AT&T Corp., mean Boston businesses are paying 2 percent higher property tax bills, and the average single-family homeowner is paying \$185 more each year, city Assessor Ronald Rakow said yesterday.<sup>38</sup>

The impact on local and state revenues of tax avoidance behavior by these companies is exacerbated by an increasing pattern of federal intervention to preempt state and local tax systems. The most recent example is the so-called Internet Tax Nondiscrimination Act,<sup>39</sup> which expanded an earlier federal moratorium on state and local taxation of Internet access and other taxes on electronic commerce.

Selectively omitting certain services within the telecommunications sector from taxation does nothing to improve the quality or consistency of our tax policies nationwide. Technology will cause enough disruption; artificial discrimination, through yet further expansion of the Internet Tax Nondiscrimination Act,<sup>40</sup> will add to that problem.

## 8.0 Conclusion

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Both the federal and local governments are considering how to levy taxes fairly, without discriminating among companies that provide different forms of the same service. These debates are appropriate, and local government has been a willing partner in attempting to consider potential reforms that would continue to ensure continued growth of technology use and development. However, these goals cannot be achieved if the telecommunications industry continues to produce and circulate among members of Congress findings such as those set forth in 2004 COST Study, which contains serious methodological flaws and omits essential analytic information, and to focus more on obtaining inappropriate advantages than on creating rational tax policy.

First, the study fails to reduce the calculated “transaction taxes” by the substantial amount that is attributable to the user fees. Second, it fails to reduce the calculated “transaction taxes” by the amount used to fund the 911 emergency system and universal service. These help the public telecommunications network (and the profits of telecommunications companies). None of these are separated out from the study’s comparisons with the tax burdens borne by general businesses. Moreover, the COST Study fails to include a comparison of corporate income tax burdens, where other businesses pay more on average than telecommunications companies. Policymakers would be foolhardy to undertake major policy shifts of the type urged by COST on the basis of the weak COST Study.

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<sup>38</sup> Ibid.

<sup>39</sup> Public Law 108-435, enacted December 3, 2004.

<sup>40</sup> See, e.g., S. 849 and H.R. 1684, both introduced April 19, 2005, in the U.S. Senate and House of Representatives, respectively.

## From the Sponsoring Organizations

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We wish to express our thanks to Washington, D.C., attorney Thomas H. Stanton, who teaches at the Center for the Study of American Government at Johns Hopkins University, for his assistance in helping to prepare this report. The National Association of Counties presented Mr. Stanton with its Distinguished Service Award for his past work in strengthening the intergovernmental partnership.

Testimony Of

**Joanne Hovis**

On Behalf Of

The National Association of Telecommunications Officers and Advisors  
The National Association of Counties  
The Government Finance Officers Association  
The United States Conference of Mayors  
The National League of Cities

Before the  
U.S. House of Representatives  
Committee on the Judiciary  
Subcommittee on Commercial and Administrative Law

On  
“Cell Tax Fairness Act of 2009”  
(H.R. 1521)

June 9, 2009

2141 Rayburn House Office Building  
Washington, D.C.

**Statement of Joanne Hovis**

**Before the  
Subcommittee on Commercial and Administrative Law  
U.S. House of Representatives**

**H.R. 1521  
“Cell Tax Fairness Act of 2009”**

**June 9, 2009**

Chairman Cohen and distinguished members of the House Subcommittee on Commercial and Administrative Law:

My name is Joanne Hovis. I am the President of Columbia Telecommunications Corporation, a national, public interest, communications engineering and business consulting firm. CTC is a 26-year old company that advises state and local governments and non-profits regarding broadband communications, fiber and wireless network design, market analysis, and business planning. Our current clients include the cities of San Francisco, Seattle, Tucson, and Portland, Oregon; the District of Columbia; the Knight Center of Digital Excellence; the William Penn Foundation; the Institute for Next Generation Internet; the University of Illinois; Case Western Reserve University; and many others.

I serve as a member of the Board of Directors of the National Association of Telecommunications Officers and Advisors (NATOA), which represents local governments and promotes community interests in communications matters.

I am also a longtime advocate of the need for greater broadband communications deployment in the United States.

I appreciate the opportunity to appear before you today on behalf of NATOA, as well as the National Association of Counties (NACo), the Government Finance Officers Association (GFOA), the United States Conference of Mayors (USCM), and the National League of Cities (NLC).

I am here to correct some of the misunderstanding surrounding the economics of the wireless industry and the actual barriers to deployment of wireless broadband services to all areas of our country.

First and foremost, the current tax treatment of wireless services by federal, state, and local authorities has not hindered product innovation, service growth, or industry profitability.

The wireless communications industry is a strong and successful industry. Growth has been explosive in the high-density areas of the country where the carriers have chosen to invest and deploy networks. In 1995, there were 33.8 million cell phone subscribers in the United States; by 2008, that figure had jumped to 270.3 million, representing 87 percent of the nation's total population.

Indeed, it is wireless that represents the greatest growth and opportunity for the communications industry in a variety of ways: first, customers are acquiring wireless phones in addition to the landlines they have in their homes; second, a growing number of customers are dropping their landline phones in favor of having just one, wireless phone;<sup>1</sup> and third, wireless data services – that enable mobile email, text messaging, and Internet use – are growing exponentially.<sup>2</sup>

By its own account, the wireless industry is very strong. Verizon, the country's largest mobile service provider, posted profits of \$1.65 billion in the first quarter of 2009, representing wireless revenue growth of almost 30 percent.<sup>3</sup> On June 12, 2008, in written testimony presented to the Federal Communications Commission, Verizon Executive Vice President Thomas Tauke stated: "The wireless marketplace is working well . . . for consumers and the American economy."

AT&T also clearly sees continued strength in its wireless data services. AT&T is not only attempting to double its wireless data network speeds, but also expanding from 350 to 370 metropolitan areas.<sup>4</sup> Other major wireless carriers, including Verizon Wireless and Clearwire Corp., are also pursuing network technology upgrades in attempts to capture a larger share of the lucrative wireless data market.

Given the strength and profitability of the wireless industry, one wonders why these companies are seeking preferential tax treatment. Some believe that the wireless industry needs preferential tax treatment because such a benefit will help them deploy and provide affordable broadband access for all Americans.

Let me note that, in my experience, most local governments are actively involved in a range of activities designed to spur broadband communications deployment in their communities – for purposes of education, public safety, economic development, and digital literacy. Local government initiatives range from, in a few cases, seeking to build such networks themselves, to – in many more cases – petitioning and negotiating with

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<sup>1</sup> A May 2009 survey released by the Centers for Disease Control and Prevention concludes that for the first time the number of households in the U.S. with only a cell phone exceeds the number of households in the U.S. with only a landline phone.

<sup>2</sup> In a news report after first-quarter earnings were released, an industry analyst pointed out that AT&T's first-quarter wireless-data revenue soared by almost 40 percent, with average revenue per user up two percent, because of increased wireless Web, e-mail, and text messaging use. <http://www.msnbc.msn.com/id/30431872/>, accessed June 8, 2009.

<sup>3</sup> Associated Press, <http://www.msnbc.msn.com/id/30431872/>, accessed June 8, 2009.

<sup>4</sup> "AT&T says to double mobile data speeds by 2011," Reuters, May 27, 2009, <http://www.reuters.com/article/technologyNews/idUSTRE54Q4TS20090527>

private communications companies to deploy networks in their jurisdictions. America's local governments have been at the forefront of advocating for more, better broadband for many years.

As I just discussed, the wireless voice and data industries are both profitable and growing at extraordinary rates in metropolitan areas of the United States. This is unfortunately not the case in many rural areas, and America's local governments are as concerned and troubled by this as is this Subcommittee. While I commend those who believe our nation should find new models for expanding deployment of wireless broadband in less densely-populated areas, it is important to understand the real economic reasons why we have not achieved the level of broadband wireless deployment we would ideally like.

State and local taxes of wireless service are not an obstacle to wireless broadband deployment. On the contrary, it is the broader economics of the wireless communications industry that is the reason for this slower (or nonexistent) deployment in rural areas. Deployment of communications networks is extremely costly; communications carriers are private, for-profit companies and they quite rationally allocate their investment resources to areas of the country where they are likely to achieve the highest return on investment – those areas that have relatively dense populations and thereby greater potential penetration and higher revenues per mile of construction.

This basic reality of the economics of this industry will not be changed by preemption of state or local taxes or, frankly, by removal of any single cost of doing business, such as a tax. Even in an environment of lower tax costs, the wireless carriers will, quite rationally, still invest their resources in the most potentially lucrative areas and will still set their prices at the highest aggregate rates they believe the market will bear. **Relieving them of local tax costs is unlikely to change investment choices and may simply serve to convert into carrier profits those funds that would otherwise have accrued to localities in this critical economic environment.**

Finally, let me point out that this legislation, to the extent it attempts to impact broadband deployment through one mechanism, is not timely and should await the results of a proceeding currently underway at the Federal Communications Commission. As directed by the American Recovery and Reinvestment Act, the FCC is currently engaged in an extensive, year-long proceeding to develop a National Broadband Plan. That Plan will be delivered to the Congress in February 2010. As part of this proceeding, the FCC's Notice of Inquiry indicates that it plans to evaluate contentions that taxes and other expenses may impact broadband deployment – as well as evaluating the many economic, financial and other factors that could be hindering broadband deployment in the United States. Public comments to the FCC were due just yesterday, and thousands of public, private, and non-profit entities throughout the country are participating in the proceeding by filing comments. Given the breadth and scope of the FCC's charge under the Recovery Act – as well as the February deadline by which it will report its findings to the Congress – this Subcommittee would be wise to wait to see the expert agency's conclusions before proceeding with this legislation.

Local governments and their associations have long advocated for a cohesive, nationwide broadband policy that would bring *affordable* broadband services to all Americans. At last, it appears that the nation is on the verge of achieving what has been necessary for so long – a coordinated federal, state, and local effort to ensure that advanced communications services are available to all. The charge to the FCC under the Recovery Act is a significant and impressive means to this goal.

I commend this Subcommittee for its attention to the essential issue of broadband deployment for all Americans, but I ask you to await the outcome of this important proceeding, and to refrain from a piecemeal attempt to stimulate broadband deployment with a tax policy that would shift a greater burden onto the backs of America's cities, towns, and counties.

Last September, a witness testified before this Subcommittee that “excessive new wireless taxes imposed piecemeal by thousands of state and local governments are a deterrent to new broadband network investments.” But a more accurate understanding of the economics of wireless broadband deployment demonstrates that this argument is actually smoke and mirrors, and that this argument for preferential tax treatment is more likely to benefit the wireless communications industry than to change investment decisions regarding wireless broadband.

I urge you to speak out against this measure.

Thank you for the opportunity to provide testimony before the Subcommittee today.



Testimony Of

**Tillman L. Lay**

On Behalf of

The U.S. Conference of Mayors,  
The National League of Cities,  
The National Association of Counties  
The National Association of Telecommunications  
Officers and Advisors,  
and  
The Government Finance Officers Association

Before the  
U.S. House of Representatives  
Committee on the Judiciary  
Subcommittee on Commercial and Administrative Law

On  
"Cell Tax Fairness Act of 2008"  
(H.R. 5793)

September 18, 2008

2141 Rayburn House Office Building  
Washington, D.C.

Good afternoon, Chairwoman Sanchez and Members of the Subcommittee. I am Tillman Lay, partner in the Washington, D.C., law firm of Spiegel & McDiarmid LLP, and I am here to testify on behalf of the U.S. Conference of Mayors (“USCM”), the National League of Cities (“NLC”), the National Association of Counties (“NACo”), the National Association of Telecommunications Officers and Advisors (“NATOA”), and the Government Finance Officers Association (“GFOA”) concerning H.R. 5793. I have represented these organizations and several individual municipalities on telecommunications and telecommunications tax matters for a number of years.

Thank you for the opportunity to testify on behalf of these organizations, which represent our nation’s local governments, their telecommunications staff and advisors, and their finance officers. We oppose H.R. 5793. Its proposed moratorium on state and local wireless taxes would represent an unwarranted federal intrusion into the long-recognized authority of state and local governments to make tax classifications and open the door to unprecedented federal control and oversight of state and local tax authority.

Moreover, the legislation is a solution in search of a problem: Industry presents no data indicating that state and local wireless taxes have had any adverse effect on wireless service subscribership, revenue or investment. To the contrary, wireless industry subscribership, revenue and investment have soared during the same period that it suffered from the supposedly onerous state and local tax burden about which it complains. In addition, when stripped of universal service fund (“USF”) and E-911 fees and other user-specific fees, industry’s own data concerning the supposed burden of state and local taxes on the wireless industry fail to show any appreciable or widespread higher tax burden on wireless than on other business sectors. In fact,

wireless service enjoys a lower state and local tax burden than some other industry sectors, such as public utilities.

Local governments are more than willing to discuss reform of telecommunications taxes with industry.<sup>1</sup> Given the increasing convergence of telecommunications-related services, revising service definitions and simplifying taxes is a goal state and local governments share with industry. But by compelling favorable treatment of the wireless industry versus the many other sectors of the telecommunications industry, this bill would not further state and local telecommunications tax reform; it would instead create a new obstacle to such reform.

Local governments oppose any federal preemption of state and local governments' taxing authority, and any federally-compelled special tax favoritism of one industry. Yet that is what the wireless industry seeks in this bill.

The wireless industry's plea for federally mandated tax favoritism will open the door to other industries asking Congress for similar special exemptions or protections from state and local tax authority. That poses a dire threat not merely to state and local tax revenues, but to the entire existence of independent state and local taxation authority in our system of federalism.

Congressional policymakers who are basing their decision on wireless industry tax studies are being misled by the wireless industry's flawed data and unsound policy analysis. By requiring that "discriminatory taxes" on a specific business sector must be measured against, and not exceed, the taxes imposed by state and local governments on "general" businesses, H.R. 5793 would, if enacted, open the door to unchecked federal oversight, and rewriting of, all state and local tax laws and classifications. And since most state and local governments, unlike the federal government, must balance their budgets, such a federalization of state and local tax

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<sup>1</sup> As an example, just eight years ago USCM, NLC, NACo, NATOA and GFOA worked with the wireless industry to enact the Mobile Telecommunications Sourcing Act of 2000, 4 U.S.C. §§ 116-126 (2000) ("MTSA"). I discuss MTSA in Part 3 below.

classifications would not even lower total taxes paid by state and local taxpayers; it would just redistribute the tax burden among those taxpayers.

**1. H.R. 5793 Represents An Unprecedented, and Dangerous, Intrusion on State and Local Tax Authority That Would Threaten Our System of Federalism.**

The Supreme Court has long recognized that state and local governments have broad discretion in the field of taxation, where they possess “the greatest freedom in classification.”<sup>2</sup> The reason should be obvious: “It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments,”<sup>3</sup> and our system of federalism therefore requires “scrupulous regard for the rightful independence of state governments” in matters of tax classification.<sup>4</sup>

H.R. 5793 departs radically from these longstanding principles of federalism. It would single out not just one sector of industry, but one subpart of the telecommunications industry sector – wireless services – for preferential federal preemptive protection from state and local tax classifications. That would set a precedent that would endanger state and local taxing authority in at least two very disturbing ways.

First, it would move us further away from state and local government efforts at telecommunications tax reform. The bill would essentially require that state and local governments treat wireless services more preferentially than their landline telecommunications service competitors. Narrowing the permissible tax base for telecommunications to landline telecommunications would put upward pressure on state and local landline telecommunications service taxes (and likely on public utility taxes as well). It does not take a prophet to figure out

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<sup>2</sup> *Madden v. Kentucky*, 309 U.S. 83, 87-88 (1940).

<sup>3</sup> *Dows v. City of Chicago*, 78 U.S. (11 Wall) 108, 110 (1871) (quoted in *DirecTV, Inc. v. Tolson*, 513 F.3d 119, 123 (4th Cir. 2008)).

<sup>4</sup> *Fair Assessment in Real Estate Ass’n, Inc. v. McNary*, 454 U.S. 100, 108 (1981) (quoted in *Tolson*, 513 F.3d at 123).

the next shoe to drop: The landline telecommunications industry will then demand from Congress similar preferential, preemptive protection from state and local taxes.

Second, and more generally, the bill would set an unprecedented, and dangerous, new standard for federal intervention into state and local government tax classifications. Under the bill, “discrimination” is defined as any tax imposed on a particular industry (in this case, the wireless industry) that “is not generally imposed, or is generally imposed at a lower rate,” than that imposed generally on all businesses. If the standard for federal intervention into supposedly “discriminatory” state and local taxation becomes that every industry sector and every service has to be taxed at the same rate, then there would be no limit at all to federal intervention in state and local tax classifications. And you can expect other industries that are subject to different, and often higher state and local tax classifications – such as the utilities industries, the petroleum distribution industry, the entertainment industry, and others – to ask Congress for similar preemptive relief from state and local taxes.<sup>5</sup> Indeed, such a standard for “discriminatory” state and local taxes would mean, contrary to long-established precedent, that the federal government has the power to preempt *all* state and local tax classifications and to impose a federally-mandated state and local tax code of only a single tax rate for all businesses.

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<sup>5</sup> The wireless industry’s claim that its state and local tax burden is inappropriate given its non-monopoly status rests on the mistaken assumption that the telecommunications industry’s historical monopoly status is the only rational tax policy justification for taxing different industry sectors at different rates. There are a variety of tax policy justifications for having different business tax classifications. To use but one example, telecommunications and utility services have different demand characteristics than many other consumer goods; demand for telecommunications and utility services tends to be less elastic, and less volatile in economic downturns, therefore providing a more stable, predictable tax base than taxes on most consumer goods. Telecommunications and utility services taxes also have different tax distribution effects than general sales taxes. Businesses tend to consume relatively larger amounts of telecommunications and utility services than residential consumers, meaning that the burden of telecommunications and utility taxes falls relatively more on businesses and less on residential consumers. If utility taxes and general sales taxes were equalized, the result would be a shift of the relative tax burden away from business taxpayers to residential taxpayers. See Tillman Lay, “Some Thoughts on Our System of Federalism in a World of Convergence,” 2000 L. Rev. M.S.U.-D.C.L. 223, 233-34.

That would mean the end of state and local tax classification authority. The power of the federal government to preempt state and local taxes is ultimately the power to destroy state and local governments – a power that cannot be reconciled with our basic system of federalism.

**2. There Is No Factual Basis for the Wireless Industry’s Claims of Excessive State and Local Tax Burdens.**

The remarkable and unprecedented intrusion into state and local tax classification H.R. 5793 would represent far outweighs any plausible benefit the bill would offer. In fact, when the arguments and data underlying the wireless industry’s claims about state and local wireless taxes are assessed objectively, the bill is nothing more than a very drastic solution in search of an illusory problem. It is also nothing more than a self-interested plea by a single industry for its own special federal protection from state and local tax classifications.

**a. There Is No Evidence That State or Local Taxes Have Had Any Adverse Effect on Wireless Industry Subscribership, Revenue or Investment.**

The only plausible justification for such a dramatic federal intrusion into state and local tax classifications would be if it could be shown that state and local wireless taxes were having a uniquely harmful effect on the growth and health of the wireless industry. But there is no evidence of that at all.

To the contrary, allegedly excessive state and local wireless fees and taxes notwithstanding, the wireless industry has enjoyed remarkable growth, in terms of subscribers and revenues, over the past seven years. According to the FCC, wireless industry subscribership has grown 158% since 2000, and wireless industry revenue has grown 124% over that same period:

MOBILE WIRELESS TELEPHONE SUBSCRIBERS  
and  
TELECOMMUNICATIONS INDUSTRY WIRELESS SERVICE REVENUES

Year	No. of Mobile Wireless Telephone Subscribers <sup>6</sup> (in millions)	% Increase From Prior Year	Total Telecommunications Industry Wireless Service Revenues (in billions)	% Increase From Prior Year
2000	99.0	n/a	\$ 62.0	n/a
2001	128.5	30 %	\$ 74.7	20 %
2002	141.8	10 %	\$ 81.5	9 %
2003	160.6	13 %	\$ 89.7	10 %
2004	184.7	15 %	\$ 98.6	10 %
2005	213.0	15 %	\$ 107.1	9 %
2006	241.8	14 %	\$ 115.3	8 %
2007 <sup>7</sup>	255.4	6 %	\$ 138.9	20 %
Total Cumulative 7-Yr Increase	156.4	158 %	\$ 76.9	124 %

What these figures reveal is that, regardless whether one subjectively believes that a particular individual state or local tax or fee on the wireless industry is “too high,” “too low,” or “just about right,” there is no evidence that collectively, those taxes and fees have had any measurable or even discernable impact at all on wireless industry growth. Nor have supposedly onerous wireless taxes stalled wireless industry investment; wireless providers “have been

<sup>6</sup> *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services*, Twelfth Report, 23 FCC Rcd 2241 (2008) (“*Twelfth Report*”). This report is available on the FCC’s web site at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-08-28A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-08-28A1.pdf), and also at [http://wireless.fcc.gov/index.htm?job=cmrs\\_reports#d36e145](http://wireless.fcc.gov/index.htm?job=cmrs_reports#d36e145), which provides links to all the previous Annual Competition Reports beginning with the first report in 1995. See also Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, *Trends in Telephone Service* (August 2008), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-284932A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-284932A1.pdf).

<sup>7</sup> The FCC has not yet published year-end data for 2007. The *Twelfth Report*, although adopted on January 28, 2008, and released on February 4, 2008, is retrospective and focuses on the marketplace for Commercial Mobile Radio Services as of the end of calendar year 2006. The total number of wireless subscribers and total industry wireless service revenues shown here for 2007 are those reported by CTIA-The Wireless Association® in its *Semi-Annual Wireless Industry Survey for Year End 2007* (2008), available at [http://files.ctia.org/pdf/CTIA\\_Survey\\_Year\\_End\\_2007\\_Graphics.pdf](http://files.ctia.org/pdf/CTIA_Survey_Year_End_2007_Graphics.pdf).

spending about \$20 billion per year over the past five years on network upgrades and service expansions.”<sup>8</sup>

That wireless industry growth and investment seems little affected by state and local taxes is not a surprising conclusion. Wireless service growth in recent years has been characterized by large-scale, “macro” demand curve-shifting characteristics – decreasing cellphone unit size, increased convenience, and increasing number of services provided over cellphones – that would overwhelm any marginal effects of taxes on the industry’s cost curve.

**b. The Wireless Industry’s Tax and Fee Data Shows Nothing Onerous or Excessive about the State and Local Wireless Taxes It Seeks to Preempt.**

The wireless industry’s claims of supposedly excessive taxes and fees are based upon an apples-and-oranges mix of federal, state and local fees and taxes, many of which would not be affected or limited by H.R. 5793 at all. CTIA, for instance, has claimed that “about 15 percent of each customer’s monthly bill already [goes] to taxes and fees.”<sup>9</sup> But this 15% figure includes federal taxes and federal USF charges.<sup>10</sup> The 15% figure also includes state USF fees and state or local E-911 fees, two categories of fees that H.R. 5793 exempts from its reach.<sup>11</sup> And the 15% figure also includes state and local general sales taxes, which of course would not be subject to the bill’s moratorium.<sup>12</sup> Furthermore, the 15% figure also includes some state fees

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<sup>8</sup> Scott Mackey, “Excessive Taxes and Fees on Wireless Service: Recent Trends,” 47 *State Tax Notes*, 519, 521 (Feb. 18, 2008) (“2008 Wireless Service Trends”).

<sup>9</sup> “CTIA – The Wireless Association® Calls for Passage of Cell Tax Fairness Legislation” (Apr. 15, 2008) available at <http://www.ctia.org/media/press/body.cfm/prid/1752>.

<sup>10</sup> 2008 *Wireless Service Trends* at 519.

<sup>11</sup> See *id* at 519 & 523-531.

<sup>12</sup> See *id* at 523-531.

imposed generally on telecommunications service providers, such as telecommunications relay service for the deaf fees and state public utility commission fees.<sup>13</sup>

When these various federal and state fees and taxes are stripped away, what the wireless industry's own data show is that the level of true state and local taxes imposed on wireless service (that is, general revenue-raising state and local taxes) is not that significant at all.<sup>14</sup> And of the true state and local wireless taxes that remain, most are either telecommunications or utility taxes that apply not only to wireless services, but to landline services (and sometimes utility services and/or cable and satellite services) as well. Preempting the further application of such taxes to wireless service would simply create a new form of tax "discrimination" between wireless and landline telecommunications services and between wireless and other communications services generally. By federally mandating such discrimination, H.R. 5793 would frustrate the ability of state and local governments to reform telecommunications taxes by broadening the tax base. And it also will inevitably lead to new pleas by yet other sectors of industry – the landline telecommunications service sector, and possibly video service providers and utilities as well – for the same preemptive, federally-favored tax treatment. That, in turn, could only lead to further erosion of state and local tax bases for already cash-strapped state and local governments that must balance their budgets.

Thus, the wireless industry's claims about supposedly excessive state and local wireless taxes are based in large part on federal and state fees that H.R. 5793 would *not* preempt in any way. The perverse effect is obvious: By seeking to preempt state and local wireless taxes, industry seeks to blame local governments, and their general fund budgets, *not* for the taxes they

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<sup>13</sup> See *id.* Indeed, if these latter categories of wireless or telecommunications-specific user fees were included in H.R. 5793's classification of "discriminatory taxes," the bill would give the wireless industry a tax *break* relative to other "general businesses."

<sup>14</sup> See *2008 Wireless Service Trends* at 525-531.

have imposed, but for various user fees imposed by the federal and state governments that the bill saves from preemption.

The wireless industry presents no reliable aggregate data concerning the amount and number of the state and local taxes to which the bill actually would apply, pointing instead to an average “total tax and fee burden” on wireless, a substantial portion of which is composed of fees to which the bill would not apply at all. That is not evidence of excessive taxation of wireless services by local or state governments. It is instead evidence of a skewed and misleading manipulation of data to lead policymakers astray.

**3. The Mobile Telecommunications Sourcing Act Ensures That State and Local Elected Officials Are No Less Sensitive and Responsive To Constituents Concerns About Wireless Taxes Than Congress.**

Eight years ago, USCM, NLC, NACo, NATOA and GFOA and the wireless industry worked together to develop and support enactment of MTSA. Among other things, MTSA provides a simplified and uniform method for the imposition of state and local taxes on wireless service. It ensures that only a single state and a single local jurisdiction may tax wireless service: The state and locality where the wireless customer’s “place of primary use” (either the customer’s home or business address) is located. MTSA thus eliminates the possibility of double or inconsistent taxation of wireless by multiple jurisdictions.

MTSA also did something else: By permitting taxation only at a customer’s place of primary use, it also ensures that a customer knows precisely what jurisdiction is responsible for a state or local wireless tax and thus what elected state or local officials to hold responsible if the wireless customer does not like the tax. Put a little differently, MTSA assures political accountability: A state or local wireless tax will end up being paid by the constituents of the state or local government that imposed the tax.

No more can be asked of a tax in our system of federalism. No elected official enjoys imposing, or increasing, any tax, and that is just as true of state and local elected officials as it is of members of Congress. There is one difference, however: State and local governments usually must balance their budgets. And political accountability ensures that if state or local government constituents who pay a wireless tax feel that the tax is excessive, there is a very effective cure: the election process.<sup>15</sup>

The federal preemption approach in H.R. 5793, in contrast, violates all principles of political accountability. It would enable the federal government to place a preemptive ceiling on state and local taxing authority, while leaving to state and local elected officials the difficult task of deciding what other taxes to raise, or services to cut, to compensate for the federal limitation. For political accountability to exist, the same governmental body that cuts or limits taxes must also be responsible for raising other taxes or cutting government services to pay for the tax cut. That principle of political accountability is a foundation on which the federal government's longstanding historical respect for state and local government tax classifications rests. And it is that foundation which H.R. 5793 would upset.

We therefore ask that the Subcommittee vote against approving H.R. 5793.

Thank you for your time, and I would be happy to answer any questions you may have.

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<sup>15</sup> Indeed, a wireless industry spokesperson has elsewhere conceded as much. *See 2008 Wireless Service Trends* at 521, 523 & 524 (“the state-local [tax and fee] burden on wireless fell slightly between July 2006 and July 2007,” “for the first time since 2003, no states imposed a new [industry-specific] tax or increased the rate of an existing [wireless-specific] tax,” and “if state lawmakers and local officials target wireless consumers for new taxes and fees, they can expect more resistance [from their constituents] than in the past”).

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October 24, 2008

**Via Email to (Adam.Russell@mail.house.gov)**

The Honorable Linda T. Sánchez  
Chair, Subcommittee on Commercial  
and Administrative Law  
Committee on the Judiciary  
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2138 Rayburn House Office Building  
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Re: September 18, 2008, Hearing on H.R. 5793,  
the "Cell Tax Fairness Act of 2008"

Dear Chairwoman Sánchez:

On behalf of the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties, the National Association of Telecommunications Officers and Advisors and the Government Finance Officers Association, I write in response to your letter to me of October 9, 2008.

Attached is a copy of the portion of the September 18 hearing transcript encompassing my testimony with my proposed corrections to errors in transcription marked by hand. I respectfully request that these errors in transcription be corrected in the record.

The balance of this letter responds to the additional questions directed to me in your letter of October 9.

- H.R. 5793 simply imposes a five-year moratorium on new discriminatory taxes on wireless services. State and local governments will still be able to tax wireless services and providers as long as they are not discriminatorily applied. Why should Congress not impose such a simple moratorium when it is not banning all taxes on wireless services?**

A federal moratorium giving one industry special protection from state and local tax classifications poses problems at two fundamental levels.

The general problem is that H.R. 5793 represents a federal intrusion into historically-protected state and local tax classifications. Such an intrusion would inevitably lead to other industries seeking similar special federal protection from state and local taxes. (After all, lots of industries can claim that they are important to the nation's economy.) And that, in turn, would lead to the federalization of state and local tax classifications, the undermining of our entire system of federalism, and a direct threat to the fiscal health of state and local governments.

The more specific problem stems from H.R. 5793's definitions of "new discriminatory tax" and "generally imposed," coupled with the question's apparent assumption that all state and localities already tax wireless services and landline telecommunications services at the same rate. Under § 2(b)(4) of H.R. 5793, any wireless tax is a "new discriminatory tax," and thus prohibited, if it is "not generally imposed, or is generally imposed at a lower rate," on "other services" or "tangible personal property," or on "other persons that are engaged in businesses other than the provision of mobile services." This definition, when coupled with § 2(c)(3)(A)'s definition of "generally imposed," means that state and local governments would be prohibited from making *any* tax classification at all, no matter how reasonable, with respect to wireless services. Instead, wireless providers and services would be exempt from any state or local taxation unless they are taxed at a rate equal to the tax rate that is imposed on *all* other services, goods or businesses (assuming there is such a single general tax rate in a given locality, which is not always true). Indeed, read literally, H.R. 5793's "new discriminatory tax" definition would arguably exempt wireless services even from many state and local general sales and use taxes because many such taxes exempt food and other items and thus might not meet H.R. 5793's tests of applying to all "other" goods, services or businesses and of being "generally imposed."

H.R. 5793's "new discriminatory tax" definition would actually lead to *increased* tax discrimination in the sense that term is normally understood. "Tax discrimination" usually means taxing like, and competing, services differently. Landline and wireless telecommunications are clearly "like," and competing, services. Yet for those states and localities that subject landline telecommunications, and often all utility services, to higher tax rates than the general sales tax rate, H.R. 5793 would actually *compel* discriminatorily preferential tax treatment of wireless services vis-à-vis landline telecommunications services and other utility services.

Moreover, the tax discrimination between wireless and landline services that H.R. 5793 would create would be exacerbated by the current trend of declining landline telephone access lines. The landline telecommunications service tax base is shrinking, and because H.R. 5793 would bar states and localities from broadening that tax base to include "like" wireless services, there would be upward pressure on state and local landline telecommunications and utility tax rates to offset tax revenue losses stemming from the shrinking tax base. The resulting expanding tax rate differential between wireless and landline services would put us further away from the goal of telecommunications tax reform: To tax telecommunications services at uniform rates.

Finally, please forgive state and local governments if they are more than a bit skeptical of the notion that, if enacted, H.R. 5793 would result only in a five-year moratorium. The history of the Internet Tax Freedom Act (“ITFA”) shows that once Congress imposes a supposedly temporary moratorium on certain types of state and local taxes, the moratorium tends to become all-but-permanent due to Congress’ apparent fear of being accused of “raising taxes” if it allows the moratorium to expire. As you may recall, in 1998 the ITFA was originally justified as a temporary measure due to the supposedly embryonic nature of Internet services. The Internet can in no sense still be considered embryonic. Furthermore, there is no evidence that the ITFA has promoted Internet growth: Internet availability and subscribership are just as robust in states with grandfathered pre-ITFA Internet taxes as they are in states with no pre-ITFA grandfathered taxes. Yet the ITFA persists, extended again last year until 2014. So let there be no misunderstanding about what is at stake in H.R. 5793: The risk of an all-but-permanent, federally-compelled state and local discrimination between wireless and landline telecommunications services.

2. **In his written statement, Mr. Mackey contends that “excessive new wireless taxes imposed by thousands of state and local governments are a deterrent to new broadband network investments.” When the United States is falling behind other developed countries in broadband access, we need to do all that we can to improve this country’s broadband reach. Why should Congress not pass this legislation to ensure that there are no excessive discriminatory taxes imposed on wireless services and providers which may slow broadband growth?**

As an initial matter, as noted in my testimony, Mr. Mackey’s claim about supposedly “excessive” state and local wireless taxes is not supported by his own factual evidence. To pump up his figures for supposedly “excessive” state and local wireless tax rates, he includes a series of federal, as well as state and local, fees and taxes – such as federal excise taxes, federal universal service fund (“USF”) charges, state USF charges, state and local E-911 fees and even generally applicable state and local taxes – that H.R. 5793 exempts from its reach. When these fees and charges are removed from Mr. Mackey’s calculations, the true state and local tax rates for wireless that his evidence shows are far lower than he claims.

Second, there is no evidence remotely supporting the notion that state and local wireless taxes have slowed or deterred wireless, or wireless broadband, deployment or subscribership. In fact, the evidence is directly to the contrary. As set forth in my testimony, wireless subscribership has grown by leaps and bounds over the last decade, supposedly “excessive” state and local wireless taxes notwithstanding.

Likewise, there is no evidence that wireless service, or wireless broadband, deployment or subscribership is lower in states or localities with higher wireless tax rates than it is in states and localities with lower wireless tax rates. Mr. Mackey’s own data indicate that among the states with the highest weighted average wireless service tax rates are Washington, Florida, New

York, Texas, Missouri, Pennsylvania, Illinois and California.<sup>1</sup> I doubt anyone would seriously suggest that those states are the laggards among the states in wireless subscribership or deployment. Nor is there any evidence suggesting that wireless tax rates in the U.S. exceed wireless tax rates in all of the other countries that have greater broadband deployment and subscribership than the U.S.

Local governments share the Subcommittee's concerns about the pace of broadband access and deployment in the U.S. We resent, however, the wireless industry's attempt to portray state and local government taxes as the scapegoat for our nation's disappointing world standing in broadband access. State and local elected officials, every bit as much as members of Congress, recognize the economic importance of broadband access and very much want their constituents to have affordable broadband access. But state and local elected officials also must balance their budgets and therefore recognize that, without adequate tax revenues to pay for police, fire, schools, health care, roads and streets, and other critical local economic infrastructure, broadband access would be nothing more than an economic engine with no chassis.

I would like to add a final note on this topic to correct an apparent misunderstanding about wireless taxes and wireless broadband Internet access that occurred at the September 18 hearing. Rep. Lofgren suggested that wireless taxes might slow or deter wireless broadband Internet access deployment and subscribership. For reasons noted above, the evidence does not support that hypothesis. But there is another misperception underlying that claim. The ITFA applies to all Internet access services, whether landline or wireless. Thus, while for reasons noted above and elsewhere, local governments do not support the ITFA, the Internet tax moratorium nevertheless applies to wireless Internet access services. Therefore, to the extent that one believes that the ITFA promotes broadband Internet access deployment and subscribership (which we do not), wireless broadband Internet access providers already enjoy the federal tax preemption benefit of the ITFA. In contrast, H.R. 5793, when coupled with the ITFA, would give wireless service providers a unique, and discriminatorily preferential, federal tax preemption benefit that landline broadband Internet access service providers lack: double-preemption from not only state and local Internet access taxes but also telecommunications taxes as well.

**3. At the hearing, during one of your responses to a question posed by Mr. Cannon, you delved into the issue of regressive taxes. You were unable to finish your discussion on that issue, so please expound on your response.**

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<sup>1</sup> Scott Mackey, "Excessive Taxes and Fees on Wireless Service: Recent Trends," 47 *State Tax Notes*, 519, 522 at Table 2 (Feb. 18, 2008). See also Written Testimony of Scott R. Mackey, Hearing on H.R. 5793, the "Cell Tax Fairness Act of 2008," at 4 (Sept. 18, 2008).

My basic point was that, contrary to the claims of some of H.R. 5793's proponents, forcing state and local governments to move toward a single transaction tax rate, as H.R. 5793 tends to do, would make those governments' transaction-based tax systems *more*, not less, regressive. Because most local governments and some state governments are restricted by state law or state constitution to relying on more regressive transaction tax systems rather than more progressive income tax systems, their ability to create different tax classifications among transaction taxes (in other words, having different transaction tax rates for different categories of goods and services) is typically the only means available for local and state governments to soften the inherent regressivity of their transaction-based tax systems.

Taxing utility services at a higher rate than general sales taxes is a classic example. Unlike the case with many other consumer goods and services, businesses consume proportionately more utility services than do residential taxpayers. As a result, imposing a higher utility tax than a general sales tax tends to shift the overall local tax burden more to business taxpayers and away from residential taxpayers, thereby lessening somewhat the regressivity of a transaction-based tax system. On the other hand, requiring that utility-type services be taxed at the same rate as all other consumer goods and services, as H.R. 5793 would do with respect to wireless services, has the opposite effect: It would shift the overall local tax burden away from business taxpayers and toward residential taxpayers, making a transaction-based tax system more regressive.<sup>2</sup>

Telecommunications services generally are often subject to utility tax rates, or at least to higher tax rates than general sales taxes, because much like other utility services, businesses typically are proportionately larger consumers of telecommunications services than residential households. Whether that is also true of wireless services may not be as clear, but there is no compelling reason to believe it is not. It is certainly not irrational or unreasonable for a state or local government to classify wireless services for tax purposes based on an assumption that wireless services share this attribute with landline services, especially when such a classification also would eliminate any tax discrimination between landline and wireless services that compete with one another.

Mr. Cannon also suggested that telecommunications services are different from other utility services, such as electricity, in that telecommunications services "are profoundly important to the development of society" and are "the foundation for progress for people." I respectfully take issue with that distinction between telecommunications and other utility services. It is true that telecommunications services are vitally important, but that is no less true of other utility services. Indeed, absent electric service, the classic utility service, there would be

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<sup>2</sup> I note that, for somewhat different reasons, the ITFA likely has regressive tax effects as well. Typically older and/or less well-to-do residents continue to rely more heavily on plain old telephone services to communicate and thus must continue to pay local telecommunications taxes, while businesses, as well as typically younger and/or more well-to-do residents, tend to rely on Internet access for most of their communications needs and are thus largely shielded by the ITFA from local telecommunications taxes.

no telecommunications or broadband services at all. Yet the fact remains that essential utility services, including electric services, are typically taxed at a higher rate than the general sales tax. (Indeed, non-telecommunications utility services on average are also taxed at a significantly higher rate by state and local governments than telecommunications services.)

**4. If there is anything to which you would like to respond or clarify from the hearing, please do so.**

In addition to lessening the inherent regressivity of a transaction-based tax system, imposing higher taxes on utility services, including telecommunications, also serves another perfectly rational and important tax policy interest: relative stability in anticipated tax revenue. Demand for utility services, including telecommunications services, tends to be less elastic than demand for many other consumer goods and services, especially during economic downturns. Thus, utility taxes provide a more stable and predictable tax base for local government tax revenue budgeting and planning. That is an important tax classification policy goal in any circumstance, but especially so in this economic environment. The current economic downturn has placed an enormous strain on state and local government budgets, which are caught in a vise of declining property tax bases, sales tax revenue declines, the tight municipal bond market, and higher interest rates, on the one hand, and increased demand for the essential services they provide, on the other.

I do not mean my answers to suggest that imposing a higher tax rate on utility services, or wireless or other telecommunications services, is the only rational tax policy for state and local governments to follow. To the contrary, while some local governments follow that tax policy, others do not impose any tax at all on wireless or other telecommunications services, or impose the same tax on telecommunications services as on many other goods and services. That is precisely what our system of federalism envisions with respect to state and local tax classification policy: Each state and locality tailors its tax classification system to best meet the needs and preferences of its residents, and retains the flexibility to revise or change its tax classifications and/or rates in response to changing revenue needs and economic conditions.

What I do mean to suggest is that there are perfectly sound and reasonable tax policy justifications to tax telecommunications services, including wireless services, at something other than the general sales tax rate, and that there has been no rational or factually supported justification offered for federal intrusion into such state and local tax classifications.

It bears emphasizing that the intrusion into state and local tax classifications that H.R. 5793 represents would have significant adverse consequences not only for local governments and their residents, but for the nation as a whole. Given that there is no correlation, much less any causation, between local wireless tax rates and wireless and broadband subscription or deployment, the most likely result of a wireless tax moratorium would *not* be to spur wireless growth further, but rather to transfer money out of already-strapped state and local government budgets and into the pockets of the wireless industry. And the moratorium also would mean that residents would see either an increase in the other local taxes they must pay to offset the

The Honorable Linda T. Sánchez

October 24, 2008

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resulting tax revenue loss, or a decrease in funding for police, fire, schools, local infrastructure and other essential services that local governments provide to their residents and to the nation as a whole. This is certainly not the time for Congress to be considering ways to tie the fiscal hands of state and local governments.

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Please accept my thanks for the opportunity to testify at the September 18 hearing, and to respond to your additional follow-up questions. Should you or any other Subcommittee member or member of the Subcommittee staff wish to ask further questions or seek further information, please feel free to contact me.

Very truly yours,

/s/

Tillman L. Lay

*On behalf of the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties, the National Association of Telecommunications Officers and Advisors and the Government Finance Officers Association*

Attachment

cc: Ron Thaniel  
Larry Jones  
Carolyn Coleman  
Lars Etzkorn  
Jeff Arnold  
Steve Traylor  
Libby Beaty  
Barrie Tabin Berger