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**Another Court Sacks IRS  
on Communications Tax**

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In the previous edition of this newsletter we reported on the IRS's refusal to heed two Circuit Court decisions holding that excise taxes should not be assessed on long distance charges that do not vary by distance (December 2005, page 8). The IRS lost yet another battle on this issue in the D.C. Circuit.

The Communications Excise tax has been on the federal books for more than a century and was introduced as a revenue stream to fund the Spanish American War. However, the last time that Congress changed the language of the tax was forty years ago in 1965. At that time, telecommunications toll services were billed by time and distance. The latest court reviewed the circumstances of the tax and declared that the language no longer applies to many long distance services and neither can the tax.

Previous courts have ruled against the IRS on this issue after conducting extensive analysis regarding the placement of "and" in the tax law. The issue arises due to the specific language in the tax code that assesses tax for telephone charges that vary based upon time *and* distance. Previous courts found the use of the word "and" to require that both factors be present in order to assess the tax. The recent court agreed with previous courts that "and" requires both time *and* distance to be a factor in the calculation of the phone charges. However the most recent court, located in the shadow of the Supreme Court, also spent time analyzing the state of telephone service in 1965 - - when Congress crafted the language.

The Court provided a detailed description of the state of telecommunications in 1965, the monopoly held by AT&T and the methods used to bill for long distance calls. In the intervening years, AT&T lost its monopoly and long distance bills significantly changed. The Court found that the tax law was written for 1965 telephone bills and have not yet been updated. As such, the tax no longer can apply to a service that is not described. The Court found that the IRS should not be assessing the tax.

Readers of the previous article also may recall that the IRS refused to abide by other court holdings telling it that the tax could not be assessed. However, there is no indication as to what the IRS's next move will be. As the IRS continues to lose case after case - - the latest court referred to seven other losses - - they should defer to the court decisions. Yet the IRS remains pigheadedly obstinate on this issue -- their hope at this point must be either that Congress will change the law to clarify its application or that one Circuit Court somewhere will rule in its favor, thus necessitating Supreme Court

review. In the meantime, large excise tax payers should keep track of their payments since refunds may very well be available.