



Review of Telecommunications Personal Property Taxation

**A Report Prepared for the
Joint Standing Committee on Taxation
Pursuant to 2009 Resolves, c. 202**

**Department of Administrative and Financial Services
Maine Revenue Services**

January 10, 2011

**Jerome D. Gerard
Acting State Tax Assessor**

INTRODUCTION

Pursuant to 2009 Resolves, Chapter 202 (the “Resolve”), the Department of Administrative and Financial Services, Bureau of Revenue Services (“Maine Revenue Services” or MRS”) was directed to convene a working group to review the State telecommunications personal property tax and other forms of taxation of telecommunications providers in this State and make recommendations for updating the telecommunications taxation laws. As required by the Resolve, the working group participants included the Maine Municipal Association and other interested stakeholders representing the telecommunications industry including the incumbent local exchange carriers, newer competitive phone services with no significant personal property in the State, wireless carriers, and the cable industry. A complete list of working group participants is located at the end of this report.

The working group was directed to review options for updating the telecommunications taxation laws that are revenue neutral for the State and provide for the equitable tax treatment of telecommunications providers. As directed, the options reviewed by the working group included, but were not limited to, options that replace the personal property tax on telecommunications personal property with a sales tax or a gross receipts tax. The working group was also asked to review the financial and administrative impact on state and local government as well as the impact on consumers. Following the conclusion of the study, the working group was required to submit a report and any recommended implementing legislation to the joint standing committee of the Legislature having jurisdiction over taxation matters.

The working group was established to address the concern raised by certain telecommunications service providers that the telecommunications personal property tax resulted in an inequitable tax burden on traditional land line telecommunication companies. While this concern was not held by all working group members, various representatives of the telecommunications industry participated in a broad discussion of the issues in the current telecommunications personal property tax law and potential options for addressing those issues. The working group met five times beginning on August 11, 2010 and ending on October 29, 2010.

HISTORY¹

For most of its history, the telecommunications industry in the United States functioned as a regulated monopoly. AT&T and its subsidiaries carried the vast majority of local calls and almost all long-distance calls. In its monopoly days the industry had little reason to object to high levels of taxation and complex administrative requirements, since it faced no meaningful price competition and was generally allowed to pass these government-imposed costs through to consumers within the government-regulated rate structure.

In recent years, a number of events have disrupted this arrangement. The first and most obvious was the court-mandated breakup of the Bell System (completed January 1, 1984) pursuant to a consent decree settling allegations of violations of federal anti-trust laws. Other important

¹ Excerpts from The Impact of Changes in the Telecommunications Industry on Maine State Revenues, Maine Revenue Services, December, 2004.

developments include the federal Telecommunications Act of 1996, which significantly reduced government regulation of the industry; the emergence and rapid expansion of the Internet; the “convergence” of telecommunications providers with providers of other kinds of information and entertainment services; and the development of competing technologies such as wireless telephony (cellular phones) and VoIP (Voice over Internet Protocol).

By most measures the size of the switched telephone network in the United States peaked around 2000 and has been in significant decline since. For example, according to the FCC, total toll service revenues for all carriers dropped from their all-time high of \$109.6 billion in 2000 to \$59.9 billion in 2008². The net value of plant assets of incumbent local exchange carriers in the U.S. dropped from a high of \$172 billion in 2000 to \$107 billion in 2007³. The total number of residential and nonresidential telephone lines in the U.S. dropped from 192.4 million in 2000 to 162.6 million in 2008⁴. Although weakness in the overall economy during the last few years is undoubtedly a factor, this decline is likely to prove permanent.

Movement by the telecommunications industry to less capital-intensive technologies such as wireless and VoIP means that the amount of telecommunications personal property subject to state taxation is declining. The value of existing telecommunications infrastructure is also declining, due to excess capacity and functional obsolescence. This means that, even with no change in the way this property is assessed, revenues derived from this source will likely continue to shrink.

CURRENT LAW

The current State tax on telecommunications personal property, enacted in 1987, was phased in over two years. Prior to that, telephone companies had been subject to a tax on the gross operating revenues from operations within the State during the prior calendar year. The rate of tax ranged from 1 ½ % to 7% depending on the amount of revenue.

Currently, the State assesses a property tax against the just value of qualified property of a telecommunication business. For FY10, the amount of tax assessed was \$17,678,938.20 against a total valuation of \$803,588,100. From 1989 through 2003, the rate of tax assessed against qualified telecommunications personal property was set at .027 or 27 mills in accordance with 36 M.R.S.A § 457(2). For FY04, the rate of tax was reduced to 26 mills and was scheduled to be reduced by one mill for each year until FY10 when the mill rate would have been 20 mills. However, in 2009, the Legislature amended the statute to set the rate of tax at 22 mills for FY09 through FY11. That rate is scheduled to fall to 19 mills for assessments made in 2012 and to 18 mills for assessments made in 2013 and all subsequent years. Under current law, each telecommunications business owning or leasing telecommunications personal property is required to file an annual return that lists all telecommunication personal property as defined by 36 M.R.S.A §457(1) owned by the entity and the property’s full value.

² Federal Communications Commission, *Trends in Telephone Service* (Washington DC, September 2010) 9-5.

³ Federal Communications Commission, *Statistics of Telecommunications Common Carriers 2006/2007* (Washington DC, September 2010) 222.

⁴ Federal Communications Commission, *Trends in Telephone Service* (Washington DC, September 2010) 7-3.

The telecommunications personal property tax is annually determined by applying the rate of tax as set by 36 M.R.S.A §457(2) to the just value of telecommunications personal property located in Maine and owned by a telecommunications business. “Telecommunications business” means a person “engaged in the activity of providing interactive 2-way communications services for compensation.” 36 M.R.S.A. § 457(1)(A). Pursuant to 36 M.R.S.A §457(1)(B), “telecommunications personal property” includes:

- personal property used for the transmission of any interactive 2-way communications, including voice, image, data and information, via a medium such as wires, cables, microwaves, radio waves, light waves or any combination of those or similar media;
- qualifying property used to provide telegraph service; and
- any interest of a telecommunications business in poles;

but does not include:

- property used solely to provide value-added non-voice services in which computer processing applications are used to act on the form, content, code and protocol of the information to be transmitted, unless those services are provided under a tariff approved by the Public Utilities Commission; or
- single or multiline standard telephone instruments.

Telecommunications personal property as defined in section 457 is exempt from local municipal property taxation. Telecommunications personal property that does not meet the definition under section 457(1) is taxed in the municipality or unorganized territory where it is located at the local property tax rate. A survey done by the Maine Municipal Association estimates that statewide municipalities are annually assessing approximately \$299,450,000 of telecommunications personal property that is exempt from the state tax.

In addition to the State and local property taxes on their real and personal property, businesses that provide telecommunications services in Maine are also subject to sales and use taxes and income tax in the same way as other business taxpayers. In addition, intrastate calls (local service and intrastate long distance) are subject to the 5% Service Provider Tax, which replaced the sales and use tax on this service as of July 1, 2004. This tax applies to wireless and internet telephone services as well as to traditional switched network telephone service. Interstate calls are exempt from the service provider tax. Finally, the telecommunications industry is subject to various fees which are generally passed through to the consumer (i.e. E911, education access surcharge, etc.).

DISCUSSION

One option proposed by members of the working group provided for a reduction in the State telecommunications personal property tax rate to a weighted average municipal mill rate for all assessments. Under this proposal, the reduced rate would be effective beginning on April 1st of the year following the enactment of the legislation and the average municipal mill rate would be determined using the municipal mill rates for the tax year immediately preceding the year of the assessment.

A second option proposed adjusting the definition of telecommunications personal property to encompass the telecommunications personal property that does not meet the definition under

section 457(1) and that is currently taxed by municipalities and the unorganized territory. Because this would result in an increase to the State telecommunications personal property tax base, there would be a corresponding reduction in the mill rate to ensure revenue neutrality. Also, because this option results in a loss of revenue to municipalities, the new mill rate calculation would include any costs incurred by the State to offset the revenue loss to the municipalities.

A third option proposed the repeal of the state telecommunication personal property tax resulting in the taxation of all telecommunications personal property by municipalities and the unorganized territory.

Finally, the working group considered a proposal to repeal the state telecommunications personal property tax and enact a sales or a gross receipt tax.

After extensive discussion, each of the above proposals was rejected by the working group for various reasons. Generally, the representatives of the wireless industry expressed opposition to any proposal that resulted in a new tax or an increase in the Service Provider Tax to make up any revenue shortfall. The representatives of the wireless industry also stated that they are not inclined to support replacing the current law, although they agree that the best tax policy is for all communications companies to be taxed at the same rates as other businesses. The Maine Municipal Association was opposed to any change that would result in a municipal revenue loss or an adjustment to the revenue sharing formula. Additional discussion focused on the administrative challenges for each proposal. For example, the land line companies have historically reported to the Property Tax Division of Maine Revenue Services an aggregate value of telecommunications personal property located in Maine, while a new system might require the entities to report the value of the property by its location.

RECOMMENDATION AND CONCLUSION

While the working group rejected the previously discussed proposals, they felt they could agree on an approach that addressed the disparity between the local municipal mill rates and the State mill rate on telecommunications personal property. Therefore, the working group members in attendance at the last meeting unanimously agreed to recommend that for assessments made beginning in 2012, the telecommunications personal property tax rate would be adjusted to apply the municipal tax rate where the property is located to the full just value of the property. The owners of telecommunications personal property will report to Maine Revenue Services the full value of all personal property and the jurisdiction in which it is located. MRS will apply the tax rate of the municipal jurisdiction where the property is located to the value of the personal property as adjusted by the certified ratio. If legislation implementing this recommendation is enacted, Maine Revenue Services will develop a reporting procedure as well as a method of valuing standard equipment that is administratively less burdensome for telecommunications businesses. MRS notes that this option may raise constitutional concerns with respect to the multiplicity of tax rates to be used if this proposal is pursued.

The working group estimates that the use of the municipal tax rate applied to the full value of the personal property will result in a \$1.3 million loss of revenue to the State of Maine in FY 12. In

the opinion of the working group, that estimated gap increases to \$2.3 million if the value of the property is adjusted for the certified ratio of the municipality where the property is located. If the mill rate continues to decrease as set forth in current law, the working group estimates that in FY 13 the shortfall is reduced to \$600,000 when comparing full values or an estimated \$1.5 million when applying municipal rates to the value of the property adjusted for the certified ratio. The working group concedes that there is an estimated revenue loss in the initial phasing in of this recommendation but predicts that over time this will change and may result in a revenue increase to the State.

The working group was unable to arrive at a unanimous solution to offset the potential State revenue loss. It was suggested, however, that a small temporary increase of not more than 0.5% to the Service Provider Tax for all taxable services could be implemented to offset the potential revenue loss.

WORKING GROUP PARTICIPANTS

James Cohen
Roy Drukker
Tom Federle
Jamie Fenwick
Geoff Herman
Steve Hudson
Michelle Jones
Kathleen Kittrick
Kimberly Condon Lane
David Ledew
Phil Lindley
Toby McGrath
Joseph Mackey
Michele Maclean
Thomas Murray
Beth Olser
Ben Sanborn
Michael Saxl
Rojean Tulk

Verrill Dana, LLP
FairPoint Communications
Federle Mahoney / TWC
Time Warner Cable
Maine Municipal Association
Preti Flaherty
Time Warner Cable
Northeast Verizon
Maine Street Solutions
Maine Revenue Services
ConnectMe
Maine Street Solutions
Public Affairs Group
NECTA
TDS Telecom
Unitel
Telephone Association of Maine
Maine Street Solutions
FairPoint Communications