

IS STATE TAXATION OF THE WIRELESS INDUSTRY COUNTERPRODUCTIVE?

A FACT SHEET BASED ON A NEW STUDY BY J. GREGORY SIDAK

In a new study examining the economic impact of state taxation of the wireless industry, economist J. Gregory Sidak, the F.K. Weyerhaeuser Fellow in Law and Economics Emeritus at the American Enterprise Institute for Public Policy, argues that current **state tax rates on wireless services harm consumers and are slowing the growth of the U.S. economy**. Sidak believes states should lower their tax rate on the wireless industry to boost consumer – and taxpayer – benefits.

As the California Public Utilities Commission considers issuing a sweeping set of new regulations that would impose a series of mandates on wireless providers, Sidak's findings underscore the need for review and analysis. As Governor Gray Davis has suggested, major regulatory proposals such as the CPUC's require a sober assessment of the possible impact to "the economy, infrastructure and job creation." Sidak's findings suggest the potential economic impact of the proposed regulations to be significant and deserving of serious examination.

THE \$65 BILLION QUESTION

- “[S]tate taxation on wireless service causes more economic harm per dollar raised than do other forms of taxation.”
- “State taxes on existing wireless services are high and thus dampen consumers’ subscriptions to, and usage of, those services . . . a result that will harm consumers and impede growth in the wireless industry and in the U.S. economy more broadly.”
- Bringing state wireless tax rates in the U.S. down to the prevailing rates for general business taxes would increase the nation’s Gross Domestic Product by between **\$53.6 billion and \$65.6 billion over ten years**.

EXCESS BURDEN ON WIRELESS CONSUMERS

Thirty-nine states and the District of Columbia impose taxes on wireless services at a higher rate than they impose on the average business.

- “The average state tax rate for wireless services at the end of 2002 was 8.6 percent. The median state tax rate on business services in general was 6.0 percent.”
- New York State imposes the nation's highest tax rate on wireless services: 17.9 percent. New York taxes general business services at 8.13—“an excess burden” of 9.77 percent which consumers of wireless services must pay.
- The excess burden for Florida is 8.64; for the District of Columbia, 6.68; for Texas, 6.10; for **California, 5.74**.

“Weighing the state tax on wireless services by the number of subscribers in each state, one finds that **the average wireless consumer pays a 14.8 percent tax to the states.**”

WIRELESS: A CONSUMER SUCCESS STORY

“Since 1993, when the wireless industry was effectively deregulated, the price of wireless service has fallen, and the consumption of wireless minutes has risen.”

- “[I]n June 1993, the average cost per minute for wireless voice service, expressed in 2002 currency, was 69 cents. By June 2002, the cost of wireless service had fallen to 12 cents per minute of use—an 82 percent decrease in price.”
- “Consumption of wireless services increased over 3,000 percent between 1993 and 2002.”

SO WHAT’S THE PROBLEM?

“These trends have prevailed despite high state taxes for wireless services, a trend that would indicate, on the surface, that the demand for wireless services is insensitive to the price. However, as the usage of wireless services expands, each successive consumer who begins to use wireless services is increasingly sensitive to price.”

Just how sensitive are consumers to changes in price? “[A] one percent increase in the price of wireless service causes a reduction in the demand for wireless services that exceeds one percent.”

- High rates of taxation deter consumers from subscribing to wireless services, and from consuming minutes.

“If states were to reduce their taxation of the wireless industry, consumers would use wireless services with greater intensity.”

MULTIPLICATIVE EFFECTS

Using a formula from the Bureau of Economic Analysis, U.S. Department of Commerce, for every dollar wireless service providers invest in expanding and improving their networks, U.S. GDP increases by \$2.51.

- Similarly, **lowering wireless taxes by one dollar will boost US GDP by as much as \$3.00.**
- Although a cut in the wireless tax would result in initial losses in state taxes, these losses would eventually be offset by a boost in state and federal taxes caused by the stimulative effects of a tax cut. In this way, states can recoup as much as 79 cents on the dollar.
- **“The increased revenue would permeate through the economy and cause U.S. GDP to increase by up to \$65.6 billion.”**

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