

## MEMORANDUM

From: Samuel A. Mitchell  
Date: September 24, 2004  
Re: Telephone Excise Tax

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Another district court has held that the 3-percent telephone excise tax does not apply to long-distance telephone charges that do not vary by distance. National R.R. Passenger Corp. v. United States, No. 03-431 (RMC) (D.D.C. Sept. 20, 2004). The district court held that the statutory language in I.R.C. § 4252 applies only to charges that vary by time and distance, as was the custom in 1965 when the law was enacted, and not to charges that vary only by elapsed time. As we have reported before, two other district courts have split on this issue. Office Max, Inc. v. United States, 309 F. Supp. 2d 984 (N.D. Ohio 2004) (tax does not apply) and American Bankers Ins. Group, Inc. v. United States, 308 F. Supp. 2d 1360 (S.D. Fla. 2004) (tax applies). The Office Max and American Bankers cases are on appeal to the 6th and 11th Circuits, respectively, and it is expected the IRS will appeal this latest case to the D.C. Circuit here in Washington, D.C.

In August, the IRS released Notice 2004-57, 2004-35 I.R.B. 376, stating that it will continue to assess and collect the telephone excise tax in spite of the American Bankers case and that failure to pay the tax (payments are made to the carrier) may result in the imposition of penalties and interest. The IRS acknowledged in the Notice that taxpayers may file claims for refund to preserve their claims but clarified that it will not act on the claims until the appeals courts decide the issue. The IRS also released temporary, proposed regulations (T.D. 9149; REG-163409-02) detailing carriers' obligations to report the failure of their customers to pay the tax.

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We recommend that companies continue to track the excise tax on telephone billing systems and file protective refund claims pending the outcome of the appeals court decisions. It will be important to maintain the telephone charge records to support the claims, as it may be some time before the appeals courts sort out this issue.