



TAX ALERT

JULY 31, 2006

THE IRS WILL REFUND LONG-DISTANCE TELEPHONE EXCISE TAXES

The IRS, after repeatedly losing in one court after another, has finally conceded that the 3% federal excise tax doesn't apply to long-distance calls for which the charges are computed on an elapsed time basis regardless of distance. Remarkably, the IRS has also conceded that the excise tax doesn't apply with regard to Voice over Internet Protocol service, prepaid telephone cards, and plans that provide both local and long distance service for either a flat monthly fee or a charge that varies with the elapsed transmission time. These other issues were not even litigated and lost by the IRS.

Taxpayers no longer have to pay the tax and can request a credit or refund for amounts paid for service billed to them after February 28, 2003 and before August 1, 2006. Individuals (including Schedule C filers), but not other taxpayers, have an option to use either the actual amount of tax paid for services or use a safe harbor amount (which the IRS has yet to specify) when requesting their refund or credit. Other taxpayers must use the actual amount of excise tax paid. The refund or credit for the above billing period must be requested on the taxpayer's 2006 income tax return (or tax year including December 31, 2006 for fiscal year taxpayers).

Taxpayers will have to certify that they haven't already received a refund from their telephone provider and won't ask their telephone provider for a credit or refund. In addition, taxpayers, other than individuals using the safe harbor amount, must retain records that substantiate the request. Required records include bills showing the tax charged for each month, cancelled checks, or other evidence showing that the tax was paid.

Any part of the credit or refund attributable to taxpayers that were deducted as an ordinary and necessary business expense must be included in income for the tax year in which the refund is received or accrued. If the taxpayer requests a refund of the actual amount of tax paid, the IRS will pay interest which also must be included as income on the taxpayer's return for the tax year in which it is received or accrued.

For more information, please do not hesitate to call us.

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