



Institute For Policy Innovation

# ISSUE BRIEF

## HANGING UP ON LIBERTY:

### HOW PREPAID MOBILE LAWS RESTRICT FREEDOM, IMPOSE ONEROUS REGULATIONS AND FAIL TO STOP CRIMINAL BEHAVIOR

by Bartlett D. Cleland

An estimated 58 million Americans have embraced the convenience of prepaid wireless service, but the “Pre-Paid Mobile Device Identification Act,” sponsored by Senators Schumer (D-NY) and Cornyn (R-TX) would impose new regulations and costs on consumers of prepaid wireless service, and erode users’ privacy. These new burdens on consumers are not an acceptable tradeoff for what would likely be an ineffective tool against a handful of criminals.

#### Synopsis

Law enforcement is always at odds with “criminal innovation.” Criminals continuously deploy new tools, new strategies and new tactics to commit their acts, forcing law enforcement to adapt and to perform at a higher and higher level just to keep criminals at bay. Just as tending a garden to ward off pests, animals and invasive weeds is a process and not a destination, so too is guarding against crime and allowing freedom to flourish amongst those who abide by the laws.

As criminals adopt new technology, law enforcement often reflexively views new technology almost as an accomplice, and too often has tried to restrict the liberty of law-abiding citizens while accomplishing relatively little in curtailing the bad acts of bad people.

A recent example of this tendency is the “Pre-Paid Mobile Device Identification Act,” recently introduced by Senator Schumer (D-NY) and Senator Cornyn (R-TX). This legislation calls for federal regulation of the prepaid wireless device and service market.

There is a trend among government and law enforcement to “over criminalize” products and actions—using criminal law to solve every problem and punish every mistake. The end result is that, often trivial conduct is subject to criminal prosecution, and sometimes leads to imprisonment of even those who acted without criminal intent. And as a final insult, most often the criminalization of these trivial matters has no ultimate impact on actual behavior by criminals.

#### Introduction

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## Prepaid Mobile Service

Prepaid mobile service is, obviously, mobile device service which is paid for before consumption. These plans allow a consumer to buy a set number of minutes ahead of time, and once they have used them, to buy more via a refill card. Such cards are typically available at drug stores, convenience stores, filling stations and some department stores.

For any number of reasons these plans have grown in popularity, and today nearly 58 million consumers have chosen to go the prepaid route for their wireless service. While a typical mobile phone plan requires a long term commitment (often in return for a reduced price per minute), prepaid does not, which is attractive to some consumers who value prepaid in order to avoid the surprise of a larger mobile bill when they exceed their lower cost contracted minutes in a month. Others do not have a credit history sufficient to enter into a long term contract, or because of their poor credit could do so only by also paying a substantial deposit over and above the regular costs. Along those same lines, some consumers are particularly budget conscience and want to set a fixed amount in their budget so as to avoid spending more than they have or will have.

For many users, prepaid wireless is simply the better deal, at least at current price points. While a typical prepaid plan minute is often more expensive than a contract plan minute, the prepaid plan does not require a long term commitment because it does not include a handset subsidy from the service provider. But for limited users, such as those who perhaps have phones only for emergencies (e.g. women in abusive relationships or children apart from parents), this slight marginally higher price is of little concern considering that even minimal contract plans may be more than they need and hence very much more expensive than prepaid.

Of course, some criminals also use prepaid wireless service, which has led to the wrongheaded conclusion that “something must be done” to regulate a service enjoyed by 58 million law-abiding Americans and a handful of criminals.

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## The Pre-Paid Mobile Device Identification Act

The proposed legislation, S. 3427<sup>1</sup> is straightforward, requiring anyone who purchases a prepaid wireless device to provide their name, address and date of birth, along with photo identification, or various IRS tax documents such as a 1099 (independent contractor) form or a W-2 Wage and Tax Statement to the merchant.

Merchants are then required to transmit that information, along with information about the device bought, to the provider of the voice, or Internet, service. The merchant is then required to dispose of the information while the wireless service provider is required to build a sprawling database that it must retain for 18 months.

Failure to do this correctly leads to a cash fine. Also, a “non-authorized” reseller would pay a fine and serve time in jail. Presumably selling an old phone to a buddy would be such an offense. Perhaps even donating an old phone for use by an abused woman’s shelter would run a good Samaritan afoul of the new federal law.

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1. Available at <http://thomas.loc.gov/cgi-bin/query/z?c111:S.3427><http://thomas.loc.gov/cgi-bin/query/z?c111:S.3427>

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## Problems Associated With These Regulations

There are a number of fairly obvious problems associated with imposing such stringent new regulations upon the provision of prepaid wireless service.

As is widely recognized, regulation imposes costs and liabilities upon businesses as they try to offer goods and services to consumers. And the “Pre-Paid Mobile Device Identification Act” would clearly do so.

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### Rising Costs and Liability

In this case, the government would impose greater regulatory requirements on the prepaid mobile service market by mandating the collection and storage of personally identifying information. This collection and storage requires extra time, space (whether physical or electronic), security and of course is accompanied with a great deal of new liability, all borne by the merchant. All of these will increase costs on business, costs which must be borne in order to continue serving customers.

These costs, like all input costs to a business (such as raw materials, labor, taxes and regulations) increase the cost to the consumer, and in this case to a particularly cost sensitive demographic. The obvious result is to discourage sales.

State and local governments lose too, through less tax revenue as sales decrease.

Additionally, the legal liability for both the retail merchant and for the service provider will increase. Both entities are required to collect and store (for however brief a period in the case of the merchant) personal information. Absent any legal provision to hold them harmless in the case of a breach of that information, the end result is the need for new security measures. And new security measures means new expense. In addition to the costs of those security measures, additional costs will be borne in the event of any breach of a customer’s personal identity information. All told, this government-imposed liability exposure will translate into real costs, ultimately to be borne by the consumer as higher prices.

When considering federal responses to crime we must start from a basis of assumed freedom and liberty. This is, after all, the assumption made at the founding of the country and enshrined in the Declaration of Independence, the U.S. Constitution and the Bill of Rights. Practically, that means the standard for curtailing liberty should be quite high, regardless of the perceived benefit gained. The idea that because a criminal, gang leader, terrorist or hedge fund trader can be slowed in their nefarious works, that all should willingly give up freedom is offensive, and counter to the very idea of liberty. As Benjamin Franklin famously said, “They who can give up essential liberty to obtain a little temporary safety, deserve neither liberty nor safety.”<sup>2</sup>

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### Privacy Lost

Franklin’s quote appeals to a more fundamental justification than the legal argument, that is, we must approach such issues on moral grounds as well. In fact, this is the very foundation upon which our Founding Fathers wrote in the Declaration of Independence, “We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of Happiness. That to secure these rights, Governments are instituted among Men,...” Government was created to secure those rights, not to eliminate them in pursuit of other goals. Those rights are unalienable, not subject to limitation at the whim of government.<sup>3</sup>

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2. *Memoirs of the Life and Writings of Benjamin Franklin* (1818).

3. As the Bill of Rights illuminates. It lists the limitations on the power and authority of the federal government; “Congress shall make no law respecting an establishment of religion...,” or “...the right of the people to keep and bear Arms, shall not be infringed,” etc. Yet, our political leaders consistently speak about government protecting us from other, perhaps real, perhaps politically manufactured, threats. But the threat from which the Founders were protecting us was government itself.

So important were these principles (and they should still be just as revered) that the correction to be taken when these rights are infringed is dramatic. The Declaration continues, "...That whenever any Form of Government becomes destructive of these ends, it is the Right of the People to alter or to abolish it, and to institute new Government, laying its foundation on such principles and organizing its powers in such form, as to them shall seem most likely to effect their Safety and Happiness." The contrast of these thoughts with the current proposal is quite dramatic—the current proposal assumes that government is the means to reach "safety," whereas the Founders saw that government was a threat to safety itself.

So, how is this all relevant to this debate? The proponents of this erosion of liberty blatantly disregard that only a mere handful of consumers, amongst tens of millions, of prepaid plans are to blame for all of their mentioned bad acts. The simple truth is that their use of hyperbole is designed only to play on the fears of the public as a means to assert greater federal governmental control.

The legislation would require the keeping of records, multiple forms and in multiple copies, all of which is information that would make it easier to identify and track down individuals. The mere government requirement for such recordkeeping is, at least, an erosion of privacy, but the implementation poses equal danger. The increased threat to privacy is all but apparent. Fundamentally the challenge is human behavior, and desire of some to commit crime. Any tool could be used, such as rope, batteries, retail bought fertilizer, gasoline, screwdrivers, knives, guns, bats, box cutters, or rope. Should they all require mandated registration?

Recently, the sprawl of the U.S. intelligence industry has been made public. Yet, even with the great numbers of people and institutions, and with all of the money provided to the intelligence gathering complex, still the information readily available has many times failed to be assembled to effectively identify threats to public safety.

This new system of collecting and, presumably, assembling this information into usable form becomes yet more information layered on top of a already floundering system. But further, the sprawl of the data is in fact part of the problem in that the opportunity for infringement of consumer rights is even more likely.

Independent retailers (drug stores, convenience stores, filling stations, and some department stores) are responsible for the overwhelming majority of sales of prepaid services and products.<sup>4</sup> The typical retailer is not trained or otherwise experienced in implementing the legislative mandate to collect consumer information, and certainly is not adept at protecting and maintaining the confidentiality of consumers' personal information—all indications of an increased likelihood of a breach of privacy.

Specifically then, the legislation increases the potential for violations of 47 USC Section 222, Telegraphs, Telephones, and Radiotelegraphs, Privacy of Customer Information,<sup>5</sup> as well as its companion 47 CFR 64.2001 *et. seq.*, the Customer Proprietary Network Information (CPNI) regulations.<sup>6</sup> Taken together, this law and regulation create an apparatus of strict rules governing data access, use, disclosure and safeguarding applied to telecommunications service providers, and specifically holds carriers liable for the acts of their merchants. The bottom line? In all likelihood, this proposal unwittingly will increase the violations of these current federal laws.

4. In part suggested by "Unlimited Prepaid Wars Heating Up," Simon Flannery and Sean Ittel, August 10, 2009 Morgan Stanley report, which noted with respect to prepaid from Page Plus that "Distribution is fairly broad covering many of the major U.S. cities and is utilizing online, indirect small wireless and convenient store channels rather than big box retailers," while TracFone's Straight Talk was initially "available in 240 Wal-Marts in 11 markets and TracFone intends to roll out a more broad distribution after its six month trial period ends."

5. <http://law.onecle.com/uscode/47/222.html>

6. <http://frwebgate.access.gpo.gov/cgi-bin/get-cfr.cgi?TITLE=47&PART=64&SECTION=2001&YEAR=2002&TYPE=PDF>

Moreover, the proposal lacks any security requirements to protect such information. Of course with greater requirements for particular or specific security measures, obligations of training, etc., the costs to the retailer and legal liability would increase. Yet, without such requirements, consumers are provided no assurance that their detailed personal information will not be laid bare by criminals for nefarious purposes, hence providing the possibility for greater crime and limiting the scheme as a viable solution.

The thrust of the legislation, and the nature of the supporting statements, assumes that one significant motivation for purchasing prepaid mobile devices and service is an effort to facilitate some sort of wrongdoing.<sup>7</sup> And yet, whatever the motivation of individuals intent on bad acts, prepaid mobile was not designed as a tool for anonymity. Rather, the intent was to provide greater options to consumers—options which are as budget sensitive as they are diverse. In addition, the design enabled those with no, bad or little credit history to be able to attain what has become a critical tool for safety.

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## Ineffective Solutions

But still, the Senators' statements refer to such users as terrorists, drug sellers, mob figures, gang leaders and even hedge fund traders. They even cite the use of such devices as remote detonators for bombs.

Their bias is laid bare in that only one sentence acknowledges legitimate users. As already mentioned there are nearly 58 million Americans who actually use prepaid mobile<sup>8</sup> for a variety of reasons. Despite the Senatorial prejudice and assertions, prepaid mobile customers are not pre-disposed to criminal behavior, but rather, criminals are pre-disposed to the use of any tool that can further their destructive ends. Hence government schemes to collect names, addresses or tax information will ultimately fail. Criminals will either find a means to defeat those techniques or move on to use of other means of communications. And specifically, those engaged in any substantial criminal enterprise, the very criminals or terrorists of the most interest to law enforcement, already know not to use unprotected phones, much less handsets with accounts in their name whether prepaid or post-paid. In the end, the only things arrested are the rights of law-abiding citizens.

This is not to say that laws are meaningless. Frankly, that retort is a canard. What this does say is that government must act thoughtfully and carefully when pursuing criminals and not arrest the entire populace in hopes of snaring evil doers.

In this case, while government is busily collecting information from millions, the criminals may not be amongst that group at all. Law enforcement is not ultimately interested going after those who purchased the phones necessarily but rather those who use the phones. The current scheme does nothing to collect or force disclosure of that information.

In addition and importantly, the private market is already making moves to address this challenge. As noted in the press release from Senator Schumer, Wal-Mart is already collecting the information that the proposed regulation would require. More broadly, prepaid wireless companies have made clear that they routinely assist law enforcement. Virgin Mobile goes so far as to work directly with retailers on security measures as a hedge against these devices and services being misused. In addition, these companies provide mobile use records to law enforcement but, as they should, do so when asked appropriately. What does that mean? They require subpoenas or court orders, as is

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7. Press release from the Office of Senator Charles Schumer: Schumer, Cornyn: Prepaid Cell Phones Help Terrorists Like Times Square Bomber Evade Detection; Senators Propose First-Ever Federal Law To Require Phone Companies To Keep Records Of Buyer's Identities [http://schumer.senate.gov/new\\_website/record.cfm?id=325263&http://schumer.senate.gov/new\\_website/record.cfm?id=325263&](http://schumer.senate.gov/new_website/record.cfm?id=325263&http://schumer.senate.gov/new_website/record.cfm?id=325263&)

8. John C. Hodulik, et al., "US Wireless 411, Version 36.0," UBS Investment Research, 3 June 2010, at Table 5, there were 57,444,000 prepaid subscribers as of 1Q 2010. Further, it is instructive to note that that prepaid use in the U.S. is lower than in other places around the world. For example, on the African continent, 95 percent of mobile subscribers are prepaid wireless users precisely for the reasons that US customers enjoy the service – no contract, no sterling credit history needed, budget sensitivity, and the ease of changing plans without additional costs.

appropriate to protect all parties from lawsuits and to ensure due process. In the end, the proposed legislation seeks to end run the appropriate legal process—a process which we have come to expect, and depend upon, as a means of protecting individuals against the zeal of the public prosecutor.

For better or worse, most people have come to expect political opportunism rather than principle from our political class. Today, what does not seem to receive the same sort of tolerance is blatant political hypocrisy.

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## Congressional Malpractice?

### **BUDGET HYPOCRISY**

Senator Schumer presumably supports the idea of budgetary discipline, having been on record a number of times supporting “pay-go” rules for Congress and arguing that they in fact encourage fiscal discipline. While not precisely the same thing as pay-as-you-go financing, the principle is the same. That is, one should not be spending more money than they have, so that they are not spending themselves into debt, or into a budget deficit.

Putting aside whether “pay-go” rules provide any fiscal discipline for Congress or whether it is simply a political trick, the fact remains that Mr. Schumer would now discourage the same sort of tool for fiscal discipline as he has voted for himself. Pre-paid wireless services allows a consumer, million of consumers, to choose a plan that works for them because it offers them predictable expenses, something this group clearly values.

### **ETF HYPOCRISY**

But the flip-flopping does not end there. For quite some time, legislation has been introduced in the Senate to force mobile service providers to end early termination fees (ETF) for mobile plans.<sup>9</sup> ETFs are the charges collected if a customer terminates a contract for wireless service early. The economic necessity of these provisions in a traditional mobile service contract is pretty straightforward. In an attempt to drive down the upfront costs of pricey hardware, such as smart phones, the industry evolved their business model by shifting the large upfront costs, and risk, from the consumer to the industry. In these plans, the provider would bear that upfront cost, which would only be paid back over years by the customer.

The rhetoric opposing ETFs has been loud and devoid of understanding of business models and economics, but opponents of these contracts routinely made the assertion that this sort of arrangement somehow disadvantages the consumer. So, prepaid mobile devices with no ETF would seem to be the perfect industry response to these critics, as now those with fixed or limited incomes, or those who simply want predictable expenses each month, have yet another option to meet their needs.

In essence, the market found a way to please those who were railing against wireless service providers, and yet the U.S. Senate simply moved the goal posts and now complains about the solution via legislation which would make these options less convenient and more expensive.

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9. See <http://www.govtrack.us/congress/bill.xpd?bill=s111-2825S.2825>, Cell Phone Early Termination Fee, Transparency and Fairness Act and two years earlier, <http://www.govtrack.us/congress/bill.xpd?bill=s110-2033S.2033>, Cell Phone Consumer Empowerment Act of 2007

## TECHNO-PROFILING

Interestingly, while Senator Schumer has been on record opposing the Arizona immigration law because of the disputed potential for profiling, his statements supporting this legislation clearly stereotype and profile all users of prepaid mobile as scoundrels. Moreover, he has also voted against requiring the presentation of identification at polling places, and yet would force the same when a consumer sought to purchase a phone.

## GUNS DON'T KILL PEOPLE EITHER

For his part, Senator Cornyn is a staunch defender of 2nd Amendment rights. Often used among gun rights supporters is the saying “guns don’t kill people, people kill people,” but yet in this case the Senator seems to indicate that it is not people killing people but instead that prepaid mobile devices kill people.

Currently, several states, including Texas, Missouri, Massachusetts, Pennsylvania, Georgia and South Carolina are at work on laws to regulate prepaid wireless service in a similar way. With states acting, why would the Senators see a need for federal intervention? They assert weakly, “But in light of the increased reliance of terrorists on the devices, Schumer and Cornyn said it was time for a federal response.”<sup>10</sup> This seeming disregard for the 10<sup>th</sup> Amendment<sup>11</sup> and to the principles of federalism broadly, is corrosive.

Mobile phone service would certainly be considered interstate commerce<sup>12</sup> but the initial sale of hardware and plans, which is what the proposal covers, is clearly intrastate commerce. Trying to paint their assertion in its best light, the Senators must be arguing somehow for the Commerce Clause exception.

The fact that this mere assertion is placed at the very end of the statement following their acknowledgment of the many states taking action tells the tale—this is yet another federal power grab without a Constitutional basis. As stated in IPI’s “A Citizens Guide to the Tenth Amendment,”

*For 60 years—and many would say much longer—we have seen the federal government assume more and more powers that were never granted it by the Constitution. As it has assumed more powers, it has had to increase taxes and impose more regulations that the Founding Fathers never envisioned being controlled by Washington. And it has paid for those excesses by borrowing trillions of dollars. Those factors have awakened the public, which is looking for ways to recreate the balance of powers envisioned by the Founders. What can be done?...States must reinvigorate our federalist system by challenging federal violations of the Tenth Amendment, as many are currently doing in challenging the health care reform law’s demand that every American have health insurance or pay a fine...<sup>13</sup>*

The bottom line is that the federal government is limiting liberty, increasing prices and ratcheting up regulations while providing no tool for law enforcement, even while harming those most in need. The correct thinking is to have government step back when private

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## Federalism Considerations

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10. Ibid. 7

11. For further information, see Restore the Tenth, [http://www.restorethetenth.com/about\\_the\\_10th\\_amendment/](http://www.restorethetenth.com/about_the_10th_amendment/)

12. And hence the IPI support for such efforts as Mobile Wireless Tax Fairness Act of 2009, Library of Congress, THOMAS, <http://thomas.loc.gov/cgi-bin/query/z?c111:S.1192>: introduced by Senators Ron Wyden (D-OR) and Olympia Snowe (R-ME). For more see ‘No Tax on Talk’ at <http://www.ipi.org/IPI/IPIPressReleases.nsf/70218ef1ad92c4ad86256ee5005965f6/0323a2497ffec72e862575e7005ad4fa?OpenDocument> and “French Fried Communications Taxes” at <http://www.ipi.org/IPI/IPIPressReleases.nsf/70218ef1ad92c4ad86256ee5005965f6/a0d678cabce300fa8625751d0067f6c1?OpenDocument>

13. A Citizen’s Guide To The Tenth Amendment, William Murchison and Merrill Matthews, Ph.D, <http://www.ipi.org/IPI/IPIPublications.nsf/PublicationLookupFullText/FC8C8CA94C5927E9862577200069C685>

parties are heading toward a desired solution, letting the market operate effectively and efficiently to solve perceived problems. Because, after all, effective and efficient are not words often associated with big government.

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## Conclusion

Prepaid wireless plans are designed to provide flexibility to consumers and to address some of the complaints about previous mobile wireless service plans. They are particularly appealing to a underserved part of the marketplace and have enjoyed great success in those markets, allowing many who otherwise would not be able to have access to wireless services. The proposed legislation, and various other legislative or regulatory proposals, are a direct threat to this opportunity to serve customers previously unserved.

The zeal to capture those who would cause grievous harm is not enough to infringe the liberty of law-abiding citizens. But moreover, a variety of private sector and state efforts are underway, which suggests that the federal proposal may be mostly political opportunism. Such efforts are not only a threat to our freedom but also to our privacy, and the return on such efforts is slim, at best.

Certainly, criminals, gang leaders, terrorists or even hedge fund traders are worthy targets of law enforcement, but when the laws grant ever-increasing authority to law enforcement, ignore the breach of freedoms, raise costs and liabilities for merchants and the price point of the product thereby making it harder for underserved communities to attain, then some very real scrutiny should be brought. But worse, when liberty will be infringed and yet the effectiveness will be limited or fail, then such ideas should be rejected.

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## About the Author

Bartlett Cleland is the Director of the IPI Center for Technology Freedom at the Institute for Policy Innovation. He joined the Ashcroft for Senate campaign as a research assistant in 1994. Cleland went to Washington, D.C. in 1995 to work for Senator John Ashcroft, serving as the Senator's technology counsel from 1996 to 1998. From 1998 to 2000, he worked for Americans for Tax Reform as technology and policy counsel, and advised Commissioner Grover G. Norquist on the Advisory Committee on Electronic Commerce. From 2000 to 2005, he served as the Associate General Counsel and VP, Software, at the Information Technology Association of America. He is a licensed attorney and has also received his MBA.

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