

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-86 (20) C
Corporation Tax
October 16, 1986

STATE OF NEW YORK
STATE TAX COMMISSION

ADVISORY OPINION

PETITION NO. C850730A

On July 30, 1985, a Petition for Advisory Opinion was received from ITC Entertainment, Inc., 115 East 57th Street, New York, New York 10022.

Petitioner, a Delaware corporation doing business in New York State, is engaged in the business of theatrical and television film distribution. In connection with the distribution of films, Petitioner enters into license agreements with various television networks for the nationwide television exhibition of films. Petitioner has several prints of each film for use in fulfilling its distribution obligations and makes available to the network a copy of the film for the network's use in the transmission of nationwide broadcasts.

Petitioner raises two issues with respect to the receipts factor of the business allocation percentage used to allocate entire net income as provided in Section 210.3 of Article 9-A of the Tax Law.

Issue (1)

What is the appropriate method to be used to allocate to New York State receipts from the distribution of theatrical and television films to various television networks?

Petitioner maintains that payments received under agreements with the networks for the television exhibition of films result from the distribution of a licensing right (an intangible asset). It is the Petitioner's contention that such payments should be classified as either a rental or royalty. Petitioner states that the receipts at issue represent income from the nationwide broadcast (as opposed to the mere New York broadcast) of the films and accordingly, has allocated such receipts to New York State by reference to viewing audience. This method is consistent with the rules prescribed for the allocation of broadcasting receipts. 20 NYCRR 4-4.3(f)(2) and Technical Services Bureau Memorandum TSB-M-79(5)C. Petitioner contends that it is merely one step removed from the actual broadcasting of the films and thus the viewing audience method of allocation properly reflects its film distribution activity in New York State.

Initially, it must be noted that regulation section 4-4.3(f)(2) does not apply to receipts from the distribution of films since, by its terms, it applies only to the broadcasting of radio and television programs and commercial messages by way of radio or television antennae pursuant to a license granted by the Federal Communications Commission.

Section 210.3 of the Tax Law states:

"The portion of the entire net income of a taxpayer to be allocated within the state shall be determined as follows:..."

Section 210.3(a)(2) of the Tax Law, in pertinent part, states that receipts allocable to New York State include:

"...(B) services performed within the state,...

(C) rentals from property situated, and royalties from the use of patents or copyrights, within the state...."

Section 4-4.3(b) of the Franchise Tax Regulations provides for the allocation of receipts from compensation for services, as follows:

"Commissions received by a taxpayer are allocated to New York State if the services for which the commissions were paid were performed in New York State. If the services for which the commissions were paid were performed for the taxpayer by salesman attached to or working out of a New York State office of the taxpayer, the services will be deemed to have been performed in New York State."

Thus, where a distributor is acting as an agent of the producer of a film, its receipts are receipts for services performed. In such a case, the distributor must allocate its commissions from the sale of distribution rights pursuant to section 4-4.3(b) above.

Section 4-4.4(c) of the Franchise Tax Regulations provides for the allocation of receipts from royalties, as follows:

"Receipts of royalties from the use in New York State of patents and copyrights are allocated to New York State. Royalties include all amounts received by the taxpayer for the use of patents and copyrights, whether or not such patents or copyrights were issued to or are owned by the taxpayer. A patent or copyright is used in New York State to the extent that the activities thereunder are carried on in New York State.

Where a producer of a film sells the rights to the film to a distributor and the distributor sells its rights to a television network, the distributor must allocate its receipts from the sale of such rights on the basis of audience participation. Technical Services Bureau Memorandum TSB-M-86(4)C. Similarly, where a distributor sells its rights to a cable network, then the distributor must allocate its receipts from the sale of such rights to New York State by the ratio of New York subscribers to total subscribers everywhere. However, if there are unique circumstances where the viewing audience concept does not properly reflect the receipts allocable to New York State, the distributor may request that the Tax Commission permit the use of some other method of allocation. Technical Services Bureau Memorandum TSB-M-86(4)C.

Accordingly, the method of allocation to be used by Petitioner will depend upon whether Petitioner is acting as the agent of producers of films or is acting in its own behalf. This is inherently a question of fact which, since it arose within the context of an audit, must be resolved within the context of such audit.

However, the following guidelines should be considered in resolving this issue of fact.

The purchase by Petitioner of distribution rights from a producer for subsequent resale to networks does not indicate in and of itself that Petitioner is acting as the agent of the producer. All of the facts and circumstance in each case must be considered in determining whether a principal/agent relationship exists.

Two of the primary characteristics of a principal/agent relationship are the ability of the agent to affect or alter the legal relationship between the principal and third persons and the ability of the principal to control the conduct of the agent with respect to matters entrusted to him. 2 NY Jur 2d, Agency, § 2. Within the instant context, a principal/agent relationship would be evidenced by the ability of Petitioner to bind producers to contractual liability with the networks and the ability of producers to control the specifics of Petitioner's negotiations with the networks. If Petitioner is not the agent of the producers, it will have no authority to bind producers to legal obligations with the networks and it will not be subject to the direction and control of producers in its negotiations with the networks.

Finally, it should be noted that Petitioner may act as an agent for some producers while acting in its own behalf with respect to other producers.

Issue (2)

What is the appropriate treatment of income from the sale of the taxpayer's right to future billings for purposes of calculating the receipts factor of the business allocation percentage?

Petitioner states that in 1981 it sold to various banks its rights to receive payments on certain un-billed syndication contracts. Amounts received from the banks incident to the sale (such amounts representing the discounted present value of the future income stream due under the contract) were included in both Federal taxable income and New York entire net income in 1981. In determining its receipts factor for 1981, Petitioner included the income recognized on the sale of its future income stream in the denominator of the receipts factor. No amount was included in the numerator of the receipts factor on the basis that title to the contracts transferred outside New York State.

Petitioner states that it essentially "factored" receivables it otherwise would have collected in the ordinary course of its business. Petitioner inquires as to whether or not this is the appropriate treatment of the income from the sale.

Section 210.3(a)(2) of the Tax Law states that the receipts factor of the business allocation percentage is determined by ascertaining the percentage which receipts of the taxpayer from New York sales, services, rentals, royalties and other business receipts bears to all such receipts from both within and without the state.

Section 4-4.1(a) of the Franchise Tax Regulations states:

"(a) The percentage of the taxpayer's business receipts allocable to New York State is determined by:

- (1) ascertaining the taxpayer's business receipts within New York State during the period covered by the report; and
- (2) dividing the sum of the New York State business receipts by the taxpayer's total business receipts within and without New York State during such period.

For purposes of this section, the term "business receipts" means gross income received in the regular course of the taxpayer's business, provided such receipts are includible in the computation of the taxpayer's entire net income for the taxable year."

Petitioner has stated that the amounts received from the banks for the sale of rights to future billings were included in entire net income for 1981. Petitioner has also stated that the sales transaction essentially "factored" receivables that Petitioner would have collected in the ordinary course of its business. The fact that Petitioner chose to accelerate the collection of such receivables through their sale to various banks does not alter the essential nature of these receipts. The amounts received from the banks are business receipts and must be included in the computation of the receipts factor of the business allocation percentage. The receipts are to be included in total in the denominator of the receipts factor. The portion of the receipts allocable to New York State are to be included in the numerator of the receipts factor. Petitioner must allocate these receipts to New York State in the manner previously set forth in this Advisory Opinion.

DATED: October 16, 1986

s/FRANK J. PUCCIA
Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth herein.