

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

TSB-A-99(25)C
Corporation Tax
October 7, 1999

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C980916A

On September 16, 1998, a Petition for Advisory Opinion was received from PricewaterhouseCoopers, LLP, 1301 Avenue of the Americas, New York, New York 10019.

The issues raised by Petitioner, PricewaterhouseCoopers, LLP, are:

1. Whether an alien corporation ("FORCO") that provides international callback services is doing business in New York State for purposes of Articles 9 or 9-A of the Tax Law.
2. If FORCO is subject to tax under Article 9 of the Tax Law, how are FORCO's telecommunication receipts sourced to New York State?
3. Whether FORCO's United States subsidiary ("USCO") is engaged in a telecommunication business that is subject to Article 9 of the Tax Law, in lieu of taxation under Article 9-A of the Tax Law.
4. If USCO is subject to tax under Article 9 of the Tax Law, how are USCO's telecommunication receipts sourced to New York State?

Petitioner submits the following facts as the basis for this Advisory Opinion.

FORCO is the parent of a group of companies that is principally engaged in the provision of international telecommunications services. FORCO is primarily engaged in the business of providing international callback services at competitive rates to extraterritorial, non-U.S. subscribers (hereinafter referred to as "overseas customers"). These overseas customers may access FORCO's services outside their country of residence. It is possible that these overseas customers may occasionally access such services from a site in the U.S. through use of a remote access code.

FORCO's international callback service provides a way for overseas customers to take advantage of the more preferential U.S. telecommunication rates. In this service, the overseas customer dials a special phone number in the U.S. A switch attached to that line instantaneously connects the customer to another U.S. phone line. The overseas customer then dials a phone number just as it would if it were dialing from the U.S. For example, a Pacific Rim overseas customer calling from Canada to France dials the special phone number and the phone number of the person or entity the customer wants to reach. The call is routed through the switch in the U.S. using a non-U.S. long lines carrier, and the overseas customer is billed, using U.S. telecommunication rates, in

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the customer's country of residence in the Pacific Rim. Overseas customers can also access FORCO's international callback service using an access number or code while traveling in the U.S.

FORCO does not have any presence in the U.S. or carry on any other U.S. activities. FORCO advertises and provides services only to overseas customers. FORCO's customer payments are made and collected outside the U.S. in foreign currency.

Petitioner states that FORCO does not provide local telephone service. Petitioner also states that it appears that FORCO will not be subject to the supervision of the New York State Public Service Commission ("PSC"), but it is assumed that FORCO will register with the PSC as a reseller of telecommunications services.

FORCO formed USCO, a Delaware corporation, in 1997. USCO's sole function is to own and operate a switching system located in Buffalo, New York. The switching system will be used to connect calls between two non-U.S. locations or, occasionally, to connect calls between the U.S. and an international location or between two U.S. locations (but not between two locations within New York State). Calls placed from the U.S. occur only when an overseas customer is traveling in the U.S. USCO does not provide local telephone service.

USCO has registered for sales tax purposes in New York State. (However, Petitioner states that USCO expects to receive no telecommunications revenue subject to New York State sales and use tax, which is imposed only on telecommunications transmissions both beginning and ending in New York State.) All marketing and sales functions are performed by an affiliated alien entity that has no presence in the U.S. USCO ultimately will employ approximately 3 or 4 employees, all of whom will be located inside the U.S. Petitioner states that it does not know if USCO will be subject to the supervision of the PSC.

Petitioner states that USCO's sole business is the operation of the switch used in providing the switching service for FORCO in FORCO's international callback service. In return for the use of the switching system, FORCO pays USCO a monthly fee. The fee is at "arm's length", determined by FORCO's activity level (time used, number of switch ports used, etc.). Occasionally, FORCO will pay a commission to USCO for services rendered as FORCO's telecommunications equipment purchasing agent for the purchase of equipment, not related to the callback services, to be used in FORCO's business outside the U.S.

Law and Regulations

Section 209.1 of Article 9-A of the Tax Law imposes an annual franchise tax on domestic or foreign corporations for the privilege of exercising a corporate franchise, doing business, employing capital, owning or leasing property in a corporate or organized capacity, or maintaining an office in New York State. Section 209.4 of the Tax Law, provides that a corporation liable for

tax under sections 183 and 184 of Article 9 of the Tax Law is not subject to tax under Article 9-A of the Tax Law.

To determine the classification and proper taxability of a corporation under either Article 9-A or sections 183 and 184 of Article 9, an examination of the nature of the corporation's activities is necessary, regardless of the purposes for which the corporation was organized. See Matter of McAllister Bros., Inc. v Bates, 272 AD 511, 517. Ordinarily, a corporation is deemed to be principally engaged in the activity from which more than 50 percent of its receipts are derived. See, e.g., Re Joseph Bucciero Contracting Inc., Adv Op St Tax Commn, July 23, 1981, TSB-A-81(5)C.

Section 183 of Article 9 of the Tax Law imposes a franchise tax on a domestic or foreign corporation formed for or principally engaged in the conduct of a telephone business, for the privilege of exercising its corporate franchise, doing business, employing capital, owning or leasing property in a corporate or organized capacity or maintaining an office, in New York State.

Section 184.1 of the Tax Law provides that a corporation is subject to the franchise tax under section 184 for the privilege of exercising its corporate franchise, doing business, employing capital, owning or leasing property in a corporate or organized capacity or maintaining an office, in New York State, if it is formed for or principally engaged in local telephone business. The term "local telephone business" means the provision or furnishing of telecommunication services for hire wherein the service furnished by the provider thereof consists of carrier access service or the service originates and terminates within the same local access and transport area ("LATA"). The term "telecommunication services" has the same meaning for purposes of section 184 as for section 186-e of the Tax Law.

Section 186-e.1(g) of the Tax Law defines "telecommunication services" as "telephony or telegraphy, or telephone or telegraph service, including, but not limited to, any transmission of voice, image, data, information and paging, through the use of wire, cable, fiber-optic, laser, microwave, radio wave, satellite or similar media or any combination thereof and shall include services that are ancillary to the provision of telephone service ... and also include any equipment and services provided therewith. Provided, the definition of telecommunication services shall not apply to separately stated charges for any service which alters the substantive content of the message received by the recipient from that sent."

Technical Services Bureau Memorandum TSB-M-82(13)C, March 24, 1982, provides that for purposes of sections 183 and 184 of the Tax Law the term "doing business" is used in a comprehensive sense and includes all activities which occupy the time and labor of men for profit. Regardless of the nature of its activities, every corporation organized for profit and carrying out any of the purposes of its organization is deemed to be "doing business" for purposes of the tax. Whether a foreign transportation or transmission corporation is doing business in New York State is determined by the facts in each case. Consideration is given to such factors as:

- (i) the nature, continuity, frequency and regularity of the activities in New York State;
- (ii) the purposes for which the corporation was organized;
- (iii) the location of its offices and other places of business;
- (iv) the employment in New York State of agents, officers and employees;
- (v) the location of the actual seat of management or control of the corporation.

Section 186-a of the Tax Law imposes a tax on the furnishing of utility services that is equal to three and one-quarter percent, from October 1, 1998 through December 31, 1999, of the gross income of a utility that is subject to the supervision of the PSC. For purposes of section 186-a, a "utility" includes a person, and the word "person" includes corporations, companies, associations, joint-stock companies or associations, partnerships and LLCs. The receipts from the provision of telecommunication services that are subject to tax under section 186-e of the Tax Law are not subject to tax under section 186-a of the Tax Law. However, a provider of telecommunication services that is a utility subject to the supervision of the PSC continues to be subject to the tax imposed under section 186-a on its gross income.

Gross income, as defined in section 186-a.2(c) of the Tax Law, consists of the following elements:

1. receipts from any sale made or service rendered for ultimate consumption or use by the purchaser in New York State; however, with respect to a provider of telecommunication services, such receipts shall not include receipts from the sale of telecommunication services as such services are defined in section 186-e of the Tax Law;
2. profits from the sale of securities;
3. profits from the sale of real property;
4. profits from the sale of personal property (other than inventory);
5. receipts from interest, dividends, and royalties, derived from sources within New York State; and
6. profits from any transaction (except sales for resale and rentals) within New York State whatsoever.

Section 186-e.2(a) of the Tax Law imposes an excise tax on the gross receipts from the sale of telecommunication services by any person which is a provider of telecommunication services.

Section 186-e.1(e) of the Tax Law defines "provider of telecommunication services" as "any person who furnishes or sells telecommunications services regardless of whether such activities are the main business of such person or are only incidental thereto."

Section 186-e.2(a) of the Tax Law provides that the tax is imposed on gross receipts from: (1) any intrastate telecommunication services; (2) any interstate and international telecommunication services (other than interstate and international private telecommunication services) which originate or terminate in New York State and which telecommunication services are charged to a service address in New York State, regardless of where the amounts charged for such services are billed or ultimately paid; and (3) interstate and international private telecommunication services as determined in section 186-e.3 of the Tax Law.

Section 186-e.1(f) of the Tax Law provides that generally the service address is the location of the telecommunication equipment from which the service is originated or received, such as a phone or computer terminal that is associated with the billing. However, special rules define the service address if the telecommunication service is obtained through a credit or payment mechanism (such as a credit card, calling card or third party billing), or the service address is not a defined location. The special rules are applied in a specific order, and if more than one rule applies, the first rule to apply should be used to determine the service address. The special rules for determining the service address are:

1. If the telecommunication originates or terminates in New York State and is charged to telecommunication equipment that is not associated with the origination or termination of the telecommunication (for example, the use of a calling card or third party billing) and the location of the equipment is in New York State, the service address will be deemed to be in New York State.

2. If the service is obtained by charging a calling card, third party billing, or other method, that is associated with telecommunication equipment not located in the state of origination or termination of the telecommunication, then the service address is deemed to be the location of the origination of the telecommunication.

3. If the service is obtained through a credit or payment mechanism such as credit or debit card, then the service address is deemed to be the location of the origination of the telecommunication.

4. If the service address is not a defined location, as in the case of mobile telephones, paging systems, maritime systems, air-to-ground systems and the like,

the service address is defined as the location of the subscriber's primary use of the telecommunications equipment as determined by telephone number, authorization code, or location in New York State where bills are sent. However, the location of the mobile telephone switching office or similar facility in New York State that receives and transmits the signals of the telecommunication (such as the cell antenna location which transmits the call) will be deemed to be the service address if the mobile telephone switching office or similar facility is outside the subscriber's assigned service area.

Section 186-e.2(b)(1) of the Tax Law provides that certain sales-for-resale of telecommunication services are excluded from tax. In order to qualify for this exclusion, the purchaser must sell the purchased telecommunication services as telecommunication services. Moreover, the purchaser must be an interexchange carrier or local carrier. Pursuant to Technical Services Memorandum TSB-M-95(3)C, December 13, 1995, a provider may accept a *Certificate of Public Convenience and Necessity* issued by the PSC as evidence that a carrier is eligible for the resale exclusion.

Section 186-e.4(a)(1) of the Tax Law provides that if the reseller of telecommunication services is not an interexchange carrier or local carrier, a credit is allowed to the reseller for tax paid when the services are actually resold. The credit operates such that the tax on the resale is applied to the difference between the gross charge imposed on resale and the gross amount paid to acquire the resold service.

Section 186-e.4(a)(2) of the Tax Law provides that in order to prevent multijurisdictional taxation, a credit is allowed on any interstate or international telecommunication service upon proof that a telecommunication services provider paid a like tax to another state or country on the same service. The amount of the credit will be the amount lawfully due and paid to the other state or country, but it may not exceed the amount of tax actually imposed in New York State. The credit is determined on the basis of each individual transaction.

Discussion

Issue 1. Petitioner states that FORCO is "primarily" engaged in the business of providing international callback services to overseas customers. The overseas customer dials a special phone number in the U.S. that connects the customer to USCO's switch, located in Buffalo, New York. The switch connects the customer to another U.S. phone line, and the overseas customer then dials a phone number just as it would if it were dialing from the U.S. The overseas customers can also access the service using an access number or code while traveling in the U.S. The overseas customer is billed for the call in the customer's country of residence. Based on the facts presented, it is assumed that FORCO is "principally" engaged in a telephone business, that is, more than 50 percent of its receipts are from such business. Accordingly, FORCO would be classified as a corporation subject to tax under section 183 of Article 9 of the Tax Law rather than Article 9-A of the Tax Law. However, based on the facts presented, the provision of FORCO's international callback services

does not constitute "doing business" in New York, and FORCO would not be subject to tax under section 183 of the Tax Law.

Since Petitioner states that FORCO is not principally engaged in a local telephone business, FORCO would not be subject to tax under section 184 of the Tax Law.

Petitioner states that it appears that FORCO is not subject to the supervision of the PSC. Therefore, assuming FORCO is not subject to the supervision of the PSC, FORCO would not be subject to tax under section 186-a of the Tax Law.

Pursuant to section 186-e.1(e) of the Tax Law, FORCO is a provider of telecommunication services. Based on the facts presented, FORCO, is selling telecommunication services in New York State, and therefore, FORCO would be subject to tax under section 186-e of the Tax Law.

Issue 2. Pursuant to section 186-e.2(a) of the Tax Law, the tax imposed under section 186-e would be imposed on FORCO's gross receipts from any interstate and international telecommunication services (other than interstate and international private telecommunication services) which originate or terminate in New York State and which telecommunication services are charged to a service address in New York State, regardless of where the amounts charged for such services are billed or ultimately paid. The service address is determined pursuant to section 186-e.1(f) of the Tax Law.

With respect to the international callback services described above, if the overseas customer originates the international call outside of the U.S., (for example, Canada) and the call terminates outside of the U.S. (for example, France), and the call is billed to the overseas customer's country of residence (for example, the Pacific Rim), the call is an international call that does not originate or terminate in New York. Therefore, the receipts from these calls would not be included in FORCO's gross receipts taxable under section 186-e(2)(a) of the Tax Law.

However, if the overseas customer, while traveling in New York State, initiates the international callback services by using an access code from a site within New York State, such call would originate in New York, and under special rule "2" of section 186-e.1(f) of the Tax Law, the service address would also be in New York State. Therefore, the gross receipts from such interstate or international call would be included in FORCO's gross receipts taxable under section 186-e(2)(a) of the Tax Law.

Section 186-e.2(b)(1) of the Tax Law provides that certain sales-for-resale of telecommunication services are excluded from the tax. In order to qualify for the exclusion, FORCO must be an interexchange carrier, and it must purchase telecommunication services that are resold as telecommunication services to its customers. If FORCO is not an interexchange carrier but is reseller of telecommunication services, it would be allowed a credit for tax paid when the services are actually resold. The amount of the credit would be determined under section 186-e.4(a)(1) and (2) of the Tax Law.

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Issue 3. Petitioner states that USCO's sole business is owning and operating the switch, located in Buffalo, New York, that is used in providing switching service for FORCO's international callback service. Such operation constitutes the conduct of a telephone business, and USCO is principally engaged in this business. Accordingly, USCO would be classified as a corporation subject to tax under section 183 of the Tax Law rather than Article 9-A of the Tax Law.

Since Petitioner states that USCO is not principally engaged in a local telephone business, it would not be subject to tax under section 184 of the Tax Law.

Petitioner states that it does not know if USCO is subject to the supervision of the PSC. Assuming USCO is not subject to the supervision of the PSC, USCO would not be subject to tax under section 186-a of the Tax Law. However, if USCO is subject to such supervision, USCO would be subject to tax under section 186-a of the Tax Law on its gross income from non-telecommunications receipts, such as the receipts from FORCO for services rendered as FORCO's telecommunications equipment purchasing agent for the purchase of equipment to be used in FORCO's business outside of the U.S.

USCO sells its telecommunication services to FORCO, which then resells the service as part of FORCO's sale of international callback service to its customers. Therefore, USCO is subject to tax under section 186-e of the Tax Law because it is a provider of telecommunication services that is selling telecommunication services in New York State.

Issue 4. Pursuant to section 186-e.2(a) of the Tax Law, the tax imposed under section 186-e would be imposed on USCO's gross receipts from any interstate and international telecommunication services (other than interstate and international private telecommunication services) which originate or terminate in New York State and which telecommunication services are charged to a service address in New York State, regardless of where the amounts charged for such services are billed or ultimately paid. The service address is determined pursuant to section 186-e.1(f) of the Tax Law.

With respect to the international callback services described above, if the overseas customer originates the international call outside of the U.S., (for example, Canada) and the call terminates outside of the U.S. (for example, France), and the call is billed to the overseas customer's country of residence (for example, the Pacific Rim), the call is an international call that does not originate or terminate in New York. Therefore, the receipts from the switching services for these calls would not be included in USCO's gross receipts taxable under section 186-e(2)(a) of the Tax Law.

However, if the overseas customer, while traveling in New York State, initiates the international callback services by using an access code from a site within New York State, such call would originate in New York, and under special rule "2" of section 186-e.1(f) of the Tax Law, the service address would also be in New York State. Therefore, the gross receipts from the switching service with respect to such interstate or international call would be included in USCO's gross receipts taxable under section 186-e(2)(a) of the Tax Law.

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However, section 186-e.2(b)(1) of the Tax Law provides that certain sales-for-resale of telecommunication services are excluded from the tax. In order to qualify for the exclusion, FORCO must be an interexchange carrier, and it must purchase telecommunication services that are resold as telecommunication services to its customers.

DATED: October 7, 1999

/s/
John W. Bartlett
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NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.