

**New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Taxpayer Guidance Division**

TSB-A-09(17)C
Corporation Tax
TSB-A-09(60)S
Sales Tax
December 15, 2009

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. Z050829A

On August 29, 2005, a Petition for Advisory Opinion was received from International Business Machines Corp., 150 Kettletown Road, Southbury, Connecticut 06488.

The issues raised by Petitioner, International Business Machines Corp., are:

1. Whether Petitioner, a provider of value added network ("VAN") and application services which include (i) network services, (ii) multi-protocol conversion, (iii) dial-up access, (iv) dedicated (leased lines) access, (v), electronic data interchange ("EDI"), and (vi) e-mail, is providing telephony and telegraphy and telephone and telegraph services of whatever nature under section 1105(b)(1)(B) of the Tax Law.
2. If the services described in Issue 1 above are found to be telephony and telegraphy and telephone and telegraph services of whatever nature, whether those services are interstate or intrastate.
3. If the services described in Issue 1 above are found to be intrastate telephony and telegraphy and telephone and telegraph services of whatever nature under section 1105(b)(1)(B) of the Tax Law, whether Petitioner may use a reasonable method to apportion to New York State customer locations the receipts from its services of handling data and messages between New York State and out-of-state customer locations.
4. If the services described in Issue 1 above are found to be intrastate telephony and telegraphy and telephone and telegraph services of whatever nature under section 1105(b)(1)(B) of the Tax Law, whether Petitioner can make exempt purchases of the underlying assets and equipment acquired from vendors.
5. If the services described in Issue 1 above are found to be intrastate telephony and telegraphy and telephone and telegraph services of whatever nature under section 1105(b)(1)(B) of the Tax Law, whether Petitioner can make exempt purchases for resale of the underlying transmission services purchased from telecommunication carriers.
6. Whether Petitioner's services described in Issue 1 above are telecommunication services subject to the tax imposed by section 186-e of the Tax Law.
7. If the services described in Issue 1 above are telecommunication services subject to the tax imposed by section 186-e of the Tax Law, whether Petitioner is entitled to a credit under section 186-e.4(a)(1) of the Tax Law for the section 186-e taxes paid by Petitioner to telecommunication carriers for the underlying transmission service.
8. If the services described in Issue 1 above are subject to the tax imposed by section 186-e of the Tax Law, whether Petitioner may use a reasonable method to apportion to New York State the

receipts from its services of handling data and messages between New York State and out-of-state customer locations.

9. Whether the services described in Issue 1 above constitute an Internet access service and are, therefore, not subject to the tax imposed by section 186-e and the taxes imposed under Articles 28 and 29 of the Tax Law.
10. May Petitioner be allowed to allocate the portion of its service attributable to New York based on the capacity or "bandwidth" provided to New York service addresses for both sales and excise tax purposes?

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

Value added network (VAN) services

Petitioner's VAN services consist of network services, multi-protocol conversion services, and access services as described below.

Network services

Petitioner operates a global computer network consisting of a group of high capacity, computerized routers/switches that are interconnected by high-speed telecommunications facilities obtained from telecommunications carriers. Petitioner offers network services to its customers, primarily multi-state businesses. These services require substantial and continuous involvement by the service provider, beginning with a comprehensive network plan and implementation. After interviewing a customer and reviewing the customer's computer communications, conversions and capacity needs, Petitioner designs and implements a network solution that relies on the use of Petitioner's network. Petitioner's global computer network is a proprietary network that is distinct from the Internet.

When customers' data enter Petitioner's network, the network's computers convert (i.e., format) the data using various communication protocols and select destination relay routers through the use of proprietary routing algorithms. Communication protocols are the agreed rules and procedures for the orderly transfer of data between digital devices connected by communication lines. Protocol conversion, a translation between protocols, allows communication between dissimilar computer environments (e.g., personal computers, servers, local area networks, mainframe computers, peripheral devices).

Petitioner's routing algorithms take into account traffic volumes, line error rates, line failures and data priority, and result in economical routing, alternative routing for line or equipment failures, efficient allocation of bandwidth and error control. The relay routers owned and operated by Petitioner are interconnected by telecommunication lines leased from and controlled by local exchange carriers (LECs) and interexchange carriers (IXCs). LECs are companies that provide local transmission and dial tone services. IXCs are companies that carry calls between local exchange service areas. The IXCs and LECs perform the data transmission functions with respect to these lines. Petitioner is billed by and pays fees to these carriers (including applicable sales taxes and section 186-e taxes) for transmitting information between Petitioner's routers.

Multi-protocol conversion services

Petitioner provides a range of VAN services for data networking and interconnection of multiple private or virtual private networks, including interoperability gateways for multiple customer networks, support for local area networks (LANs) and numerous network protocols, including X.25 packet switching, IBM SNA, Novell IPX, and the public TCP/IP (the language of the Internet), among others. These VAN services include, among other things, the necessary translations between and among the various networking protocols to permit and to facilitate inter-network communications and interoperability. These services are furnished using a combination of computer hardware and software, supported by the underlying transmission facilities leased from telecommunications common carriers.

Access services

Petitioner's network services are accessed either on a dial-up or a dedicated (leased) access line basis. Petitioner provides dial-up access at approximately 500 service points throughout the United States, affording relatively low-volume customer locations with connectivity to Petitioner's global network backbone and its full range of services, including access to other networks and the Internet. Petitioner's dial-up services are used only to provide commercial customers with connectivity to Petitioner's network. Customers pay usage fees for such service based on elapsed time. Petitioner is billed by and pays fees to the LECs (including applicable sales taxes and section 186-e taxes) for the communications services used to connect to Petitioner's network.

For higher-volume customer locations, Petitioner offers dedicated access connections between individual customer sites and an entry point to Petitioner's network. Such leased line services support essentially the same functions as dial-up services, except that the leased lines handle substantially faster data rates and are typically more economical or more appropriate for deployment at relatively high-volume, mission critical, or high-security locations or applications. These leased line services do not involve dedicated point-to-point connectivity between individual customer locations. Customers pay a flat monthly fee for Petitioner's leased line services based on the underlying carrier charges and the VAN services provided by Petitioner.

Application Services

Petitioner's application services consist mainly of electronic data interchange (EDI) and electronic mail (e-mail).

Electronic data interchange ("EDI"). EDI is an international standard for the exchange of electronic commercial documents. It is provided using a server and software applications for transmittal, storage and retrieval services. It uses sophisticated electronic mailboxes located on servers for convenient and cost efficient commercial activity. EDI may be defined as the transfer of formatted data between computer applications, running on different machines and using agreed standards to describe and format the data contained in the messages, typically without any manual intervention.

EDI is used to facilitate a broad range of commercial transactions, including merchandise ordering and order processing, invoicing and payment processing, credit card authorizations and similar financial

transactions, and for transmitting shipping notices and bills of lading, among other commercial documents. EDI requires a common protocol for the mechanized exchange of highly structured formatted information transfers among a multiplicity of enterprises. The translation of customer proprietary data formats into and out of that common protocol involves a broad range of highly sophisticated management functions. These include software and software maintenance, network management, monitoring and maintenance, and various auditing, billing and security functions. Petitioner's EDI service functions as an electronic mailbox providing a way of sending, storing, and forwarding information electronically.

Electronic mail and messaging services. Petitioner's network supports proprietary electronic mail and information exchange services. In addition to performing functions such as format, code or protocol conversion where otherwise incompatible network protocols are involved, Petitioner's e-mail services also include gateway functions and other enhanced services, such as translating e-mail text to fax format, interfacing with other e-mail and messaging protocols, and various file and document transfer protocols.

With respect to both Petitioner's VAN and application services, the telecommunications links that are involved in delivering services to customers interconnect those customers' locations with one or more of Petitioner's three mainframe servers, none of which are located within New York State. Any of Petitioner's customers can initiate a connection to the network. Such origination points may be within or without New York State and the destination points of network communications may be within or without New York State. In order for data to get from one place in New York to another in New York it must first be sent to a Petitioner server outside the State, where it is stored until retrieved from the server by the intended recipient in a separate transaction.

Applicable law and regulations

Section 179 of the Tax Law provides:

1. For purposes of this article, Internet access service shall not constitute a telecommunication service, nor shall the provision of Internet access service constitute the carrying on of a telephone, local telephone, telegraph, or transmission business.

2. The term "Internet access service" shall have the meaning ascribed thereto in subdivision (v) of section eleven hundred fifteen of this chapter.

Section 186-e of Article 9 of the Tax Law provides for an excise tax on telecommunication services, in part, as follows:

1. Definitions. As used in this section, where not otherwise specifically defined and unless a different meaning is clearly required:

(a)(1) "Gross receipt" means the amount received in or by reason of any sale, conditional or otherwise, of telecommunication services or in or by reason of the furnishing of telecommunication services.... "Amount received" for the purpose of the definition of gross receipt, as the term gross receipt is used throughout this article, means the amount charged for the provision of a telecommunication service.

* * *

(c) "Person" means persons, corporations, companies, associations, joint-stock companies or associations, partnerships or limited liability companies, estates, assignee of rents, any person acting in a fiduciary capacity, or any other entity, and persons, their assignees, lessees, trustees or receivers, appointed by any court whatsoever, or by any other means, except the state, municipalities, political and civil subdivisions of the state or municipality, public districts and corporations and associations organized and operated exclusively for religious, charitable or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(d) "Private telecommunication service" means a dedicated telecommunication service that entitles the user or users to the exclusive or priority use of a communications channel or group of channels from one or more locations to one or more locations. "Exclusive" as used herein means that the user-subscribers have use of a communications channel to the exclusion of all others who are not authorized to use such channel, and "priority" as used herein means that only authorized user-subscribers, as opposed to unauthorized persons, receive preferential use of a communications channel, but not necessarily a preference to the use of such channel with respect to each other.

(e) "Provider of telecommunication services" means 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.

(f) "Service address" means the location of the telecommunication equipment from which the telecommunication is originated or at which the telecommunication is received from the provider of telecommunication services. The foregoing rule is amplified, but not limited, by the following special provisions, which are listed in order of priority of application so that only the first applicable special provision will apply, if more than one potentially applies: (i) if the telecommunication originates or terminates in this state and the service is charged to telecommunication equipment which is not associated with the origination or termination of the telecommunication (for example, by the use of a calling card or third party billing) and the location of such equipment is in this state, the service address of the telecommunication will be deemed to be in this state; (ii) if the service is obtained through the use of a credit or payment mechanism such as a bank, travel, credit or debit card or if the service is obtained by charging telecommunication equipment which is not associated with the origination or termination of the telecommunication (for example, by the use of a calling card or third party billing) and the equipment is not located in the state of origination or termination, then the service address is deemed to be the location of the origination of the telecommunication; and (iii) 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, service address shall mean the location of the subscriber's primary use of the telecommunication equipment as defined by telephone number, authorization code, or location in this state where bills are sent, provided, however, the location of the mobile telephone switching office or similar facility in this state that receives

and transmits the signals of the telecommunication will be deemed the service address where the mobile telephone switching office or similar facility is outside the subscriber's assigned service area.

(g) "Telecommunication services" means 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 (such as, but not limited to, dial tone, basic service, directory information, call forwarding, caller-identification, call-waiting and the like) 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.

* * *

2. Imposition. (a) There is hereby imposed an excise tax on the sale of telecommunication services by any person which is a provider of telecommunication services, to be paid by such person, at the rate of ... of gross receipt from: (1) any intrastate telecommunication services ... (2) any interstate and international telecommunication services ... which originate or terminate in this state and which telecommunication services are charged to a service address in this state, regardless of where the amounts charged for such services are billed or ultimately paid; (3) interstate and international private telecommunication services, the gross receipt to which the tax shall apply shall be determined as prescribed in subdivision three of this section, ...

* * *

3. Apportionment for certain private telecommunication services. (a) General. With respect to interstate and international private telecommunication services, the gross receipt, if not separately ascertainable for each use of such service, shall be determined as follows: (1) one hundred percent of the charge imposed at each channel termination point within this state, (2) one hundred percent of the charge imposed for the use of a channel between channel termination points within this state, and (3)(i) if each segment between each termination point is separately billed and the amounts so billed are fairly reflective of New York origination and/or termination traffic, then one hundred percent of the charge imposed at each termination point in New York and for service in New York between those points and fifty percent of the charge imposed for service between a channel termination point outside the state and a point inside the state measured by the nearest termination point inside the state to first termination point outside the state relative to such point inside the state, or (ii) if each segment of the interstate or international circuit between each channel termination point is not separately billed or if such billing does not fairly reflect the New York origination and/or termination traffic handled by such private telecommunication service, an allocated portion of the interstate and international channel charge with respect to points in New York and points outside the state based on the ratio which the number of channel termination points in this state bears to the total number of channel termination points within and without the state.

(b) Other allocation methods. Where the commissioner decides that, with respect to a certain provider of telecommunication services, the method prescribed in paragraph (a) of this subdivision does not fairly and equitably reflect the private telecommunication services attributable to this state, the commissioner shall prescribe methods of allocation which fairly and equitably reflect the private telecommunication services attributable to this state. Provided, further, that the commissioner may require that another allocation method be used so as to insure that the sum of the allocation factor of this state and the allocation factor of the other jurisdiction involved is not greater than one. In making this determination, the commissioner may take into account the reasonableness of the allocation prescribed by other states.

4. Credits against tax. (a) Allowance of credits. The following credits against the tax imposed under this section shall be allowed:

(1) Certain resold telecommunication services. A credit equal to the amount of tax imposed by this section, with respect to the sale of telecommunication services, shall be allowed the purchaser where such purchaser is a provider of telecommunication services which is not an interexchange or local carrier and where the telecommunication services purchased are later resold by such purchaser as telecommunication services....

Section 1105 of the Tax Law provides, in part:

Imposition of sales tax. On and after June first, nineteen hundred seventy-one, there is hereby imposed and there shall be paid a tax ... upon:

* * *

(b) (1) The receipts from every sale, other than sales for resale, of . . . (B) telephony and telegraphy and telephone and telegraph service of whatever nature except interstate and international telephony and telegraphy and telephone and telegraph service. . . .

Section 1115(a) of the Tax Law provides, in part:

Receipts from the following shall be exempt from the tax on retail sales imposed under subdivision (a) of section eleven hundred five and the compensating use tax imposed under section eleven hundred ten:

* * *

(12-a) Tangible personal property for use or consumption directly and predominantly in the receiving, initiating, amplifying, processing, transmitting, retransmitting, switching or monitoring of switching of telecommunications services for sale or internet access services for sale or any combination thereof. Such tangible personal property exempt under this subdivision shall include, but not be limited to, tangible personal property used or consumed to upgrade systems to allow for the receiving, initiating, amplifying, processing, transmitting, retransmitting, switching or monitoring of switching of telecommunications services for sale or internet access services for sale or any

combination thereof. As used in this paragraph, the term "telecommunications services" shall have the same meaning as defined in paragraph (g) of subdivision one of section one hundred eighty-six-e of this chapter.

Section 1115(v) of the Tax Law provides:

Receipts from the sale of Internet access service, including start-up charges, and the use of such service, shall be exempt from the taxes imposed under this article. For purposes of this subdivision, the term "Internet access service" shall mean the service of providing connection to the Internet, but only where such service entails the routing of Internet traffic by means of accepted Internet protocols. The provision of communication or navigation software, an e-mail address, e-mail software, news headlines, space for a website and website services, or other such services, in conjunction with the provision of such connection to the Internet, where such services are merely incidental to the provision of such connection, shall be considered to be part of the provision of Internet access service.

Section 1132(c)(1) of the Tax Law provides, in part:

For the purpose of the proper administration of this article and to prevent evasion of the tax hereby imposed, it shall be presumed that all receipts for property or services of any type mentioned in subdivisions (a), (b), (c) and (d) of section eleven hundred five . . . are subject to tax until the contrary is established, and the burden of proving that any receipt . . . is not taxable hereunder shall be upon the person required to collect tax or the customer..Except.as.provided.in subdivision.(h).or (k) of this section, unless (i) a vendor, not later than ninety days after delivery of the property or the rendition of the service, shall have taken from the purchaser a resale or exemption certificate in such form as the commissioner may prescribe, signed by the purchaser and setting forth the purchaser's name and address and, except as otherwise provided by regulation of the commissioner, the number of the purchaser's certificate of authority, together with such other information as the commissioner may require, to the effect that the property or service was purchased for resale.or.for.some.use.by reason.of.which.the.sale.is exempt from tax under the provisions of section eleven hundred fifteen, and, where such resale or exemption certificate requires the inclusion of the purchaser's certificate of authority number or other identification number required by regulations of the commissioner, that the purchaser's certificate of authority has not been suspended or revoked and has not expired as provided in section eleven hundred thirty-four . . . the sale shall be deemed a taxable sale at retail.

. . .

Section 1135(a)(1) of the Tax Law provides:

Every person required to collect tax shall keep records of every sale or amusement charge or occupancy and of all amounts paid, charged or due thereon and of the tax payable thereon, in such form as the commissioner of taxation and finance may by regulation require. Such records shall include a true copy of each sales slip, invoice, receipt, statement or memorandum upon which subdivision (a) of section eleven hundred thirty-two requires that the tax be stated separately.

Section 527.1(b) of the Sales and Use Tax Regulations provides, in part:

Taxable and exempt items sold as a single unit. When tangible personal property, composed of taxable and exempt items is sold as a single unit, the tax shall be collected on the total price.

Section 527.2(d) of the Sales and Use Tax Regulations provides, in part:

Telephony and telegraphy; telephone and telegraph service. (1) The provisions of section 1105(b) of the Tax Law with respect to telephony and telegraphy and telephone and telegraph service impose a tax on receipts from intrastate communication by means of devices employing the principles of telephony and telegraphy.

(2) The term *telephony and telegraphy* includes use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals.

Opinion

Issue 1

Section 1105(b) of the Tax Law imposes sales tax on sales of telephony and telegraphy and telephone and telegraph service of whatever nature except interstate and international telephony and telegraphy and telephone and telegraph service. “The words ‘of whatever nature’ indicate that a broad construction is to be given the terms describing the items taxed.” Sales and Use Tax Regulation § 527.2(a)(2); *see also Matter of Easylink Services International, Inc.*, Dec Tax App Trib, July 27, 2009, DTA No. 821440. Tax Law section 1105(b) imposes tax on receipts from “intrastate communication by means of devices employing the principles of telephony and telegraphy.” Sales and Use Tax Regulation § 527.2(d)(1). Section 527.2(d) of the Sales and Use Tax Regulations defines *telephony and telegraphy* as the use or operation of any apparatus for transmission of sound, sound reproduction, or coded or other signals. Petitioner’s services are telephone and telegraph and telephony and telegraphy services as described in section 1105(b) of the Tax Law and, unless excluded from tax as the purchase of interstate and international telephony and telegraphy services, charges for these services are subject to sales or compensating use tax.

Issue 2

Sales tax is imposed only on receipts from intrastate telecommunications. *See* Tax Law § 1105(b)(1)(B). Generally, intrastate telecommunications are transmissions that both originate and terminate in New York, regardless of where the transmission is routed or passes through. *See Matter of Western Union*, TSB-H-83(57)S. Services that are billed on a call-by-call basis are subject to tax as intrastate services if the service connects service addresses that are located solely in New York. Services that are billed on a flat fee basis (e.g., single monthly charge for unlimited usage), where the fee remains constant for a fixed billing period, regardless of usage, which among other customer locations connect multiple New York service addresses, are subject to New York State and local sales taxes, as such fees represent receipts from the sale of access to and the provision of telecommunications service provided in New York. *See New York Telephone Company*, Adv Op Comm T&F, January 5, 1988, TSB-A-88(8)S; *Rochester Telephone Corporation*, Adv Op Comm T&F, December 9, 1987, TSB-A-88(1)S. If intrastate services are

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provided in combination with interstate and/or international services for a single charge, the entire charge is subject to sales tax. Moreover, all charges for such services are presumed to be subject to sales tax until the contrary is established. See section 1132(c) of the Tax Law. Thus, unless there are reasonable, separately stated charges for the intrastate service and the interstate and/or international services on the invoice given to the customer, the total receipts are subject to the sales tax. See section 1132(c) of the Tax Law and section 527.1(b) of the Sales and Use Tax Regulations. If the services offered are exclusively interstate and/or international, such as a dedicated point-to-point EDI network solely linking a New York State location to a location outside New York State, the separately stated, reasonable charges for such service would be excluded from sales tax. See *Commonwealth Long Distance, Inc.*, Adv Op Comm T&F, July 29, 1994, TSB-A-94(33)S. This requirement is not satisfied by stating an allocated amount based on an estimate of one or more user's interstate and/or international usage; rather, it must be based on the actual charges to the customer for interstate and/or international service. Petitioner must maintain records to indicate the origination and termination of such services to document that such services are not subject to sales tax. See *Taxation of Internet Telephony*, June 20, 2007, NYT-G-07(3)S).

Issue 3

Petitioner charges its customers for the provision of its services on a flat fee or lump sum basis. These services are provided to customers with locations in multiple states and connect multiple in-state locations and multiple out-of-state locations. Telecommunication services provided to service addresses outside New York are not subject to State and local sales taxes. However, Petitioner does not separately charge for the services provided to out-of-state locations. Although there is no express provision that permits allocation of receipts for sales tax purposes, the Commissioner is empowered to prescribe methods for determining the amount of receipts and which of them are subject to sales tax. See Tax Law §1142(4). Accordingly, because Petitioner appears to be providing private telecommunication service, it may calculate the sales tax attributable to services provided to service addresses in New York using the special allocation rules in the telecommunications excise tax. See Tax Law § 186-e.1(d). To the extent that Petitioner cannot ascertain whether fees charged to a customer are attributable to services provided to service addresses in New York or services provided to service addresses outside New York, Petitioner may, for sales tax purposes, apportion its receipts by applying the ratio of customer channel termination points in New York to the total number of customer channel termination points within and without New York. See Tax Law §186-e.3(a). If this apportionment method does not fairly and equitably reflect the services provided to customer locations in New York, the Commissioner may require that another method be used. See Tax Law §186-e.3(b).

Issues 4 and 5

Petitioner, as a business engaged in the provision of telephone and telegraph services for sale, is eligible for the exemptions provided by section 1115(a)(12-a) of the Tax Law. This exemption applies regardless of whether Petitioner is engaged in the provision of interstate, international or intrastate telecommunications services. Under section 1115(a)(12-a), Petitioner is eligible to purchase tangible personal property (including machinery and equipment) that is for use or consumption directly and predominantly in the receiving, initiating, amplifying, processing, transmitting, retransmitting, switching or monitoring of switching of its telecommunications services for sale without the payment of sales tax. Petitioner should issue a properly completed Exempt Use Certificate (Form ST-121) to the supplier of such

tangible personal property within 90 days of the purchase of such property. Further, as a business engaged in the sale of telecommunications service, any telecommunications services purchased by Petitioner and resold to its customers as such may be purchased for resale. Petitioner should issue a properly completed Resale Certificate (Form ST-120) to the supplier of telecommunications services within 90 days of the purchase of such services. See section 1132(c)(1) of the Tax Law.

Issue 6

When section 186-e of the Tax Law was added by Chapter 2 of the Laws of 1995, the excise tax on receipts from telecommunications services was shifted to section 186-e from section 186-a of the Tax Law. The new section 186-e was not intended to change the tax base. The statement of legislative intent in section 24 of Chapter 2 of the Laws of 1995 notes that by enacting the new section 186-e, the Legislature did not intend to affect the existing distinction between telecommunications services and information services as established in prior court decisions such as *Quotron Systems v Gallman*, 39 NY2d 428 (1976), and *Holmes Electric Protective Co v McGoldrick*, 262 App Div 524 (1st Dep't 1941), *aff'd* 288 NY 635 (1942). However, the legislation did clarify the definition of telecommunications services in new section 186-e to clearly include any transmission of voice, image, data, information and paging through the use of wires, cable, satellite, fiber-optic, laser, microwave, radio wave or similar media, except any services which alter the substantive content of the message received by the recipient from that sent if the charge for such service is separately stated. See *1995 Legislation Affecting Telephone and Telegraph Businesses and Other Providers of Telecommunication Services*, December 13, 1995, TSB-M-95(3)C.

In *Matter of Stat Equipment Corp. and Matter of Bi-County Ambulance and Ambulette Transport Corp.*, Dec Tax App Trib, January 26, 1996, DTA Nos. 812095 and 812096, the Tax Tribunal stated the test for proper classification of business activities as follows:

“[i]t is well established that classification for corporation tax purposes is to be determined by the nature of the taxpayer’s business and not by the words in its certificate of incorporation, nor by focusing on one aspect of its business operations. The business must be viewed in its entirety and from the perspective of its customers – what they buy and pay for (*Quotron Sys. v. Gallman*, 39 NY2d 428; *Matter of Holmes Elec. Protective Co. v. McGoldrick*, 262 AD 514, *aff'd* 288 NY 635; *Matter of McAllister Bros. v. Bates*, 272 AD 511)” (*Matter of Capitol Cablevision Sys.*, *supra*).

Ernst & Young LLP, Adv Op Comm T&F, August 6, 1997, TSB-A-97(19)C, illustrates this principle. There, it was held that the enhanced fax services provided by a corporation constituted an office service. The corporation’s activities in providing the enhanced fax services included the use of telecommunication services in its efforts to perform the services requested by its customers, but the corporation was not a provider of telecommunication services because it was not furnishing or selling telecommunication services to its customers. In that case, the office functions that the corporation provided included: the merging and formatting of the data provided by the customer, the distribution of the data to multiple destinations and recipients, simultaneously, as required by the customer, and the generation of reports showing how and when documents are delivered. Even though documents were transmitted, the transmission was incidental activity to the overall office service the corporation provided.

Likewise, in the present case, the business activity of Petitioner “must be viewed in its entirety and from the perspective of its customers – what they buy and pay for.” Petitioner owns and operates a network, which consists of a group of high capacity, computerized routers/switches. Petitioner determines a customer’s network needs, and then designs and implements a network solution so that when a customer’s data enters Petitioner’s network, the network computers provide the orderly transfer of the data between relay routers owned and operated by Petitioner that are interconnected by telecommunication lines that Petitioner leases from other telecommunications providers. During such a transfer, Petitioner’s network ensures that the data will be secure, will maintain its integrity from beginning to end (i.e., the data sent will be the same as the data received), and will be reliable (i.e., the security and integrity will be maintained on a consistent basis). Petitioner’s customers access Petitioner’s network and data services via either dial-up or dedicated leased line connections. Petitioner ascertains the customer’s needs and obtains for its customers’ use dial-up or dedicated leased lines that Petitioner leases from other telecommunications providers. Petitioner’s network, EDI, and e-mail services provide a way for its customers to send, store, forward, and exchange information electronically. The transmission of a customer’s data, and the provision of network access service and information exchange service, through telecommunication lines leased by Petitioner, constitute the provision of telecommunication services pursuant to section 186-e of the Tax Law. Unlike the situation in *Ernst & Young*, these activities are not incidental to the enhanced features of Petitioner’s services, which consist of designing a network solution and ensuring that the data will consistently be secure and maintain its integrity during its transfer through Petitioner’s network.

It is thus the enhanced features that are incidental to the transmission of the data, network access service, and information exchange service constituting the telecommunication services. Accordingly, Petitioner is a provider of telecommunication services, and is subject to the tax imposed under section 186-e of the Tax Law on its gross receipts from the provision of its services as provided in section 186-e.2(a) of the Tax Law.

Issue 7

Petitioner is a reseller of telecommunication services. On and after January 1, 2009, when Petitioner purchases telecommunication services that will be resold as such, it may give the provider of telecommunication services a properly completed *Resale Certificate for Telecommunication Services* (Form CT-120) within 90 days after provision of the service. See section 186-e.2(b)(1) of the Tax Law. For purchases made before January 1, 2009, or if the resale exemption is not allowed, Petitioner may take a credit for the amount of tax passed through to Petitioner by its providers of telecommunication services on the return reflecting the resale of the telecommunication service by Petitioner to its customer. See section 186-e.4(a)(1) of the Tax Law. The credit operates such that the tax on the resale is applied to the difference between the gross amount charged by Petitioner on resale and the gross amount paid to acquire the resold service (see the instructions to Form CT-186-EZ, *Telecommunications Tax Return — Short Form*).

Issue 8

For purposes of the telecommunications excise tax, all charges for telecommunication services that originate and terminate within New York State are included in gross receipts, regardless of where the service address is located. Intrastate telecommunication services include all services that originate and terminate in New York State, even if routed out of state in making the connection. Gross receipts from interstate and

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international services are attributed in full to New York State if the service originates or terminates in New York State and the service is charged to a service address in New York State. Generally, the service address is the location of the telecommunication equipment from which the service is originated or at which it is received from the provider of telecommunication services. (*See* sections 186-e.2(a) and 186-e.1(f) of the Tax Law, and TSB-M-95(3)C, *supra*.) However, because Petitioner appears to be providing a private telecommunication service as defined in section 186-e.1(d) of the Tax Law, it may apportion its gross receipts, if not separately ascertainable for each use of such service, pursuant to section 186-e.3(a) of the Tax Law. If the apportionment method described in section 186-e.3(a) does not fairly and equitably reflect the private telecommunication services attributable to this State, the Commissioner may require that another method be used.

Issue 9

In order to qualify for the exemption for Internet access service under sections 179 and 1115(v) of the Tax Law, the service being provided must provide a connection to the Internet (*see Internet Access Charges Not Subject to Sales Tax and Telecommunications Excise Tax*, November 15, 1999, TSB-M-97(1.1)C and TSB-M-97(1.1)S). Moreover, federal law preempts state and local taxes on Internet access service. Under federal law, Internet access service includes service providing a connection to the Internet; the purchase, use, or sale of telecommunications by a provider of Internet access service to the extent those telecommunications are purchased, used, or sold to provide that service; and certain services that are furnished to users incidental to the provision of Internet access service, such as a home page, electronic mail and instant messaging (including voice- and video-capable electronic mail and instant messaging), video clips, and personal electronic storage capacity. The home page, electronic mail and instant messaging, video clips, and personal electronic storage capacity are exempt as Internet access service under federal law whether provided independently or in conjunction with other Internet access services. *See* section 1105(5) of the Internet Tax Freedom Act (47 USC § 151 (note)); *The Federal Internet Tax Freedom Act Amendments Act of 2007 and its Effect on the New York Sales Tax and Telecommunications Excise Tax*, May 2, 2008, TSB-M-08(4)C, (2)S and TSB-M-08(4.1)C, (2.1)S.

Petitioner's dial-up and leased line services are used to provide its customers with connectivity to Petitioner's network, which is a proprietary network distinct from the Internet. Accordingly, Petitioner's services do not generally qualify as Internet access service and Petitioner's gross receipts from such services are subject to the tax imposed by section 186-e of the Tax Law, and the sales taxes imposed by Articles 28 and 29 of the Tax Law, as discussed above. To the extent that Petitioner provided Internet access service, as defined in federal law or the Tax Law, that service would be exempt from tax. If Petitioner's VAN and application services are bundled with Internet access for a single charge, the entire charge will be subject to both sales and excise taxes, unless Petitioner can "reasonably identify the charges for Internet access from its books and records kept in the regular course of business." (*see* 47 U.S.C. § 151 (note §1106(a))). In order to be reasonably identified, such charges must be objective and verifiable, and reasonable in relation to the total charge. *See, e.g.*, Tax Law § 1111(1)(2); *see also Taxation of Internet Telephony*, June 20, 2007, NYT-G-07(2)C, (3)S.

Issue 10

As noted in the discussion of Issues 3 and 8 above, if apportionment by customer channel termination point does not fairly and equitably reflect the services provided to customer locations in New York, the Commissioner may require that another method be used. *See* Tax Law § 186-e.3(b). Consistent with that provision, Petitioner has requested that the Commissioner approve an alternate allocation method, which would allow it to allocate the portion of its private telecommunication services attributable to New York based on the capacity or “bandwidth” provided to service addresses in New York for purposes of both the sales and excise taxes. Petitioner has previously made a detailed showing that the method prescribed in Tax Law section 186-e.3(a) does not fairly and equitably reflect its private telecommunication service attributable to New York. The Department has had an opportunity to thoroughly examine Petitioner’s submission and is satisfied that, based on the detailed information provided and Petitioner’s specific facts and circumstances, allocation based on bandwidth more accurately represents the portion of Petitioner’s private telecommunication services delivered to service addresses in New York State. Petitioner has demonstrated that allocation by bandwidth is objective and verifiable, because it has shown that its contracts with customers indicate the amount of bandwidth to be provided to various customer locations, both inside and outside New York State, and that these contracts are periodically reviewed and updated to reflect changes in the service provided to its customers. Based on this showing, Petitioner’s request to allocate its private telecommunication services attributable to New York State based on bandwidth for both sales and excise taxes is approved. If the facts or circumstances upon which this approval is based change in the future, the approval is withdrawn, and Petitioner will be required to allocate based on the method prescribed in Tax Law section 186-e.3(a), or seek new approval of an alternate allocation method.

DATED: December 15, 2009

/S/

Jonathan Pessen
Director of Advisory Opinions
Office of Counsel

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.