

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-00(8)C
Corporation Tax
April 4, 2000

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C981026A
C990114D

On October 26, 1998 and January 14, 1999, Petitions for Advisory Opinion were received from the School and Municipal Energy Cooperative, c/o Christopher L. Doyle and James R. Maloney, Hodgson, Russ, Andrews, Woods & Goodyear, LLP, 1800 One M&T Plaza, Buffalo, New York 14203-2391. The Petitions, which raise related issues, have been consolidated and are addressed in this advisory opinion. Additional information was submitted by Petitioner on July 2, 1999 and December 6, 1999.

The issues raised by Petitioner, the School and Municipal Energy Cooperative, are:

- (1) whether sales of natural gas involving the School & Municipal Energy Cooperative, as described below, are subject to the gross receipts tax under section 186-a of the Tax Law, and
- (2) whether the School and Municipal Energy Cooperative, an entity formed pursuant to Article 5-G of the General Municipal Law, is exempt from tax under section 186 of the Tax Law.

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

The School & Municipal Energy Cooperative ("Cooperative") is an unincorporated association formed in the Fall of 1998 to cooperatively purchase energy pursuant to Article 5-G of the New York General Municipal Law ("GML"). The Cooperative qualifies as an exempt organization pursuant to section 501(c)(3) of the Internal Revenue Code ("IRC"). Its members are 30 public school districts (as defined in section 119-n(a) of the GML). By law, private interests will not be permitted to be members of the Cooperative.

The members become authorized to join the Cooperative through a vote of their governing bodies. Each member may resign from the Cooperative at any time. The members elect a Board of Trustees to control and manage the business affairs of the Cooperative.

Petitioner indicates that the Cooperative's purpose involves the purchase of natural gas and electricity on an aggregation basis. By aggregating its members' energy purchases, the Cooperative can successfully lower costs through enhanced purchasing power and elimination of redundant administrative efforts. The Cooperative will not be the ultimate consumer. All of the Cooperative's activities take place in New York.

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Petitioner states that the Cooperative will purchase natural gas and certain related services from a supplier ("Supplier"), and resell all such natural gas and related services to the school districts that are members of the Cooperative. It is intended that all gas purchased by the Cooperative from the Supplier would be purchased in New York, and that all gas sold by the Cooperative to its members would be sold in New York, at cost. The members will consume the energy purchased from the Cooperative in New York State. The Cooperative will not consume any of the natural gas purchased from the Supplier.

The Supplier's prices are not subject to regulation by New York's Public Service Commission ("PSC") (*i.e.* the Supplier is not a "regulated utility").

The Cooperative purchases from an unrelated entity ("Marketer") certain services necessary for effectuating the sale and delivery of gas to the Cooperative and its members. Such services include the provision of billing, payment processing, monthly gas nominations, etc.

The Cooperative has not elected to be classified as an association for Federal income tax purposes, nor is it taxable as a corporation under any provision of the IRC.

Applicable Law

Section 186-a of the Tax Law imposes an excise tax on the furnishing of utility services measured as a percentage of the gross income of a utility that is subject to the supervision of the PSC or the gross operating income of every other utility doing business in New York State. For purposes of section 186-a, a "utility" includes a person subject to the supervision of the PSC and every person (whether or not such person is subject to such supervision) who sells or furnishes gas or electricity, by means of mains, pipes, or wires; regardless of whether such activities are the main business of such person or are only incidental thereto.

Gross operating income, as defined in section 186-a.2(d) of the Tax Law, means and includes receipts received in or by reason of any sale made for ultimate consumption or use by the purchaser of gas or electricity, or in or by reason of the furnishing for such consumption or use of gas or electric service in New York State, without any deductions.

The word "person" as defined in section 186-a.2(b) of the Tax Law includes persons, corporations, companies, associations, joint-stock companies or associations, partnerships and LLCs, 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 education purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

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Section 186 of the Tax Law imposes an annual franchise tax upon every corporation, joint-stock company or association formed for or principally engaged in the business of supplying gas, when delivered through mains or pipes, or electricity, "for the privilege of exercising its corporate franchise or carrying on its business in such corporate or organized capacity in this state". For purposes of section 186 of the Tax Law, the term "corporation" includes an association within the meaning of section 7701(a)(3) of the IRC.

Section 7701(a)(3) of the IRC provides that the term "corporation" includes associations, joint-stock companies and insurance companies. Section 301.7701-2(a) of the Treasury Regulations states that "for purposes of this section and §301.7701-3, a *business entity* is any entity recognized for federal tax purposes ... that is not properly classified as a trust ... or otherwise subject to special treatment under the Internal Revenue Code." Section 301.7701-2(b)(2) of the Treasury Regulations provides that the term *Corporation* includes an association (as determined under section 301.7701-3).

Discussion

With respect to Issue "1", section 186-a of the Tax Law imposes an excise tax measured by the gross operating income of utilities not subject to PSC supervision. A "utility" includes a "person" which includes corporations, associations, partnerships and LLCs as well as natural persons. Gross operating income includes receipts received by reason of any sales of gas or electricity or furnishing of gas or electric service for ultimate consumption or use by the purchaser. Accordingly, sales for resale, as distinguished from sales for consumption, are not taxable. Additionally, section 186-a(2) excludes, among others, charitable organizations from the definition of "person" subject to tax.

Petitioner asserts that Supplier is not selling the natural gas for ultimate consumption, but is selling the natural gas to the Cooperative for resale, and that the Cooperative, as an exempt organization under section 501(c)(3) of the IRC, would not be a "person" subject to tax under section 186-a. Accordingly, Petitioner reasons, no receipts from sales of natural gas in this manner would be subject to tax under section 186-a of the Tax Law. This reasoning presumes a sale from Supplier to the Cooperative and a resale from the Cooperative to the members. Petitioner submitted certain documentation relating to the described transactions. It cannot be concluded from the submission that the Cooperative is indeed purchasing and reselling the natural gas. It would therefore appear that Supplier's sales of natural gas are for ultimate consumption and are subject to tax under section 186-a of the Tax Law.

With respect to Issue "2", section 186 of the Tax Law provides that the term "corporation" includes an association within the meaning of section 7701(a)(3) of the IRC. Section 301.7701-2 excludes from the definition of "business entity" certain entities subject to special treatment under the IRC. Section 501(a) of the IRC provides that an organization described in section 501(c) or (d)

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or section 401(a) of the IRC shall be exempt from taxation under Subtitle A unless the exemption is denied under section 502 or 503 of the IRC. Petitioner asserts that an organization that is described in section 501(c) of the IRC is subject to special treatment, and is not a business entity pursuant to section 7701(a)(3) of the IRC. Accordingly, Petitioner reasons that an organization that is exempt from federal income tax pursuant to section 501(c)(3) of the IRC is not a corporation for purposes of section 186 of the Tax Law. However, under section 301.7701-3(c)(v) of the Treasury Regulations, an organization under section 501(c)(3) of the IRC is treated as having made an election to be classified as an association within the meaning of section 7701(a)(3) of the IRC, and is therefore included within the entities which may be subject to tax under section 186 of the Tax Law.

DATED: April 4, 2000

/s/
John W. Bartlett
Deputy Director
Technical Services Division

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