STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. C881014A

On October 14, 1988, a Petition for Advisory Opinion was received from The Partners of Buffalo Telephone Company, 1600 Rand Building, Buffalo, New York 14203.

The issues raised are whether (1) the corporate partners of a partnership providing telephone utility services in New York State would be considered utilities subject to franchise tax under section 183 and section 184 of Article 9; and (2) for purposes of section 186-a of Article 9 would New York State allow the partners of the partnership providing the telephone utility service resulting in gross receipts to report and pay the tax based on each partner's pro-rata share of the applicable partnership receipts, rather than the partnership.

Facts

The Federal Communications Commission (hereinafter "FCC") has the authority to license the use of the radio frequency spectrum including band widths used in the provision of cellular telephone service. The FCC found a need for public cellular radio-telecommunication services throughout the nation (Report and Order, CC Docket No. 79-318, 8g FCC 2nd 469 (1981), Memorandum Opinion and Order on Reconsideration, 89 FCC 2nd 58 (1982)). To encourage the development of this new service, the FCC decided to split the band width available for cellular telephone service into two equal portions, one portion to be licensed to the land-line carrier or carriers serving the specific area (often referred to as the "wireline carrier" or "wireline licensee") and the license for the other portion to be awarded to an applicant based upon legal, technical, financial and other qualifications (often referred to as the "non-wireline carrier" or "non-wireline licensee").

In order to expedite the availability of cellular services to the public and to avoid comparative hearings, the FCC encouraged competing applicants, for the non-wireline license, to settle their differences in a manner in which each could participate in providing cellular services in each proposed cellular service area (often referred to as a "CGSA"). As a result, in every CGSA, applicants for the non-wireline license formed partnerships so that while there would be essentially one remaining applicant, each of the original applicants would be able to participate. The applicants selected partnerships as the vehicle for ownership instead of corporations for a number of reasons: liability and cost sharing, financial reporting and federal tax reporting. Notwithstanding the form in which the partners have elected to do business, the operating partnerships providing service are "utilities" subject to the jurisdiction of the New York State Public Service Commission and the Public Service Law.

Herein, the corporate partners are corporations formed solely for the purposes of participating in the cellular telephone business, either as the sole licensee or to hold the partnership interest in the partnership licensee in each CGSA. As originally established, these corporations were wholly owned subsidiaries of the original applicants in the CGSA. No applicant corporation applied for a license in more than one market because a separate corporation was formed for each.

The corporate partners of Petitioner feel that they are subject to franchise taxes under section 183 and section 184 of Article 9 of the Tax Law on the basis of the general theory of partnership taxation, the statutes themselves and regulations promulgated thereunder. The operating partnership would serve as a conduit for incidents of taxation. The tax attributes and characteristics of the partnership would flow to the corporate partners, treating them as utilities providing telephone services.

Petitioner contends that passing partnership attributes to the partners of a partnership is consistent with Federal and New York State Law. Subchapter K of the Internal Revenue Code (hereinafter "IRC") relating to the taxation of partnerships, is a combination of the conduit and entity concept of partnerships. Although it is clear that a partnership is neither exclusively a conduit nor exclusively an entity, the conduit theory governs in many of the aspects of partnership taxation. Section 701 of the IRC provides that partnerships are not liable for income tax. Rather, persons carrying on partnership activities are liable for tax in their separate capacities. The partnership merely acts as an income reporting unit, not a tax paying unit. Section 601(b) of the Tax Law provides the same concept. Further, section 702 of the IRC generally provides that the character of income and deductions passed to a partner by a partnership be retained.

Petitioner further contends that taxing the corporate partners in the manner proposed will result in the equitable taxation of the competitors in the given market. The land line competitors, which were awarded the necessary FCC license automatically, operate the new service in the corporate form. Thus they are subject to the section 183 and section 184 taxes. Were it not for the FCC requiring joint application for the second license in the market, a similar type of corporate structure most likely would have been formed for the non-land line provider, which also would be subject to the section 183 and section 184 taxes.

Taxing the corporate partners of the second provider, which had its structure effectively thrust upon it by a governmental agency, in any manner other than that proposed would result in a lack of uniformity, and perhaps equity, in the taxation of competing businesses.

In addition, section 186-a of Article 9 of the Tax Law, and section 500.1 and 500.2 of the Tax on the Furnishing of Utility Services regulations, promulgated thereunder, broadly imposes the gross receipts tax on all entities, including co-partnerships, providing utility services, whether or not the rendering of such service is the primary business of the entity. Through strict application of this law, the operating partnerships providing the telephone utility service would be required to report and pay the section 186-a tax on their applicable receipts.

Petitioner freely acknowledges that a tax on the applicable gross receipts would be incurred under section 186-a and would be properly submitted to New York State.

Petitioner seeks, however, authority to allow the partners, at the partnership's option, to report and pay this tax on the partners pro-rata share of taxable receipts.

There are several reasons for this request. These include:

(1) Consistency of tax treatment - allowing the partners to report and pay the section 186-a tax would be consistent with the conduit theory of partnership taxation. The general thrust of Subchapter K of the IRC and section 601(b) of the Tax Law is to hold partnerships as tax-reporting entities, rather than tax paying entities.

(2) Clear performance measurement - by allowing the partners to report and pay this tax, they would be recording, for financial statement purposes, the full tax effect on the results of operations inclusive of all federal and state taxes that are income based.

(3) Administrative ease - the partners in most instances, rather than the partnership, have the necessary staffing to prepare and submit tax reports. Allowing the partners to report the section 186-a tax would provide them the opportunity to take advantage of their staffing. Petitioner states that if question 1 is decided in favor of Petitioner, this point is particularly significant in light of the similarities between the tax basis of section 184 and section 186-a. Further, as several of the operating partnerships are in cash deficit situations, having the partners pay the section 186-a tax would eliminate the need for them to contribute cash for the partnership to pay the tax liability.

Petitioner contends the ability of the partners to report and remit the section 186-a tax would extend only to those partners that hold a direct interest in the utility partnership. In essence, this would halt the attribution of the conduit theory for purposes of section 186-a at the ownership level immediately above the operating utility partnership. New York State would continue to have full recourse for collection of the section 186-a tax through the utility partnership. The statute of limitations would commence with the filing of the necessary section 186-a tax report by the partners.

Issue 1

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. In interpreting this section, the Business Corporation Franchise Tax Regulations section 1-3.2(a)(5) sets forth a general rule which holds that if a partnership is exercising any of the privileges of section 209.1, then all of its corporate partners are subject to the tax imposed by Article 9-A. Section 209.4 of the Tax Law, provides that corporations liable to tax under sections 183 and 184 of Article 9 of the Tax Law are not subject to tax under Article 9-A.

Sections 183 and 184 of Article 9 of the Tax Law impose franchise taxes, 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.

To determine the classification and proper taxability of a corporation under either Article 9 or Article 9-A, 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 A.D. 511, 517 (3d Dept. 1947). Ordinarily, a corporation is deemed to be principally engaged in the activity from which more than 50% of its receipts are derived. See, e.g. Joseph Bucciero Contracting Inc., TSB-A-81(24)S August 27, 1981.

Herein, Buffalo Telephone Company is a general partnership that operates as a telephone utility subject to the jurisdiction of the State Public Service Commission and the Public Service Law. As such, Buffalo Telephone Company is doing business in New York State. Accordingly, the corporate partners of Buffalo Telephone Company are subject to tax under Article 9-A of the Tax Law, unless such corporate partners are subject to tax under sections 183 and 184 of Article 9 of the Tax Law.

Every partner in a partnership is an agent of the partnership for the purpose of its business, and the act of every partner, including the execution in the partnership name of any instrument, for apparently carrying on in the usual way the business of the partnership of which he is a member binds the partnership. Partnership Law, § 20.1. Since Buffalo Telephone Company is engaged in a telephone business in New York State, each corporate partner, as agent of the partnership, is also engaged in a telephone business in New York State. Therefore, each corporate partner of Buffalo Telephone Company that is principally engaged in such telephone business is subject to tax under sections 183 and 184 of Article 9.

The determination of whether a corporate partner of Buffalo Telephone Company is principally engaged in a telephone business is a question of fact not susceptible of determination in an Advisory Opinion. An Advisory Opinion merely sets forth the applicability of pertinent statutory and regulatory provisions to "a specified set of facts" Tax Law, § 171, subd. twenty-fourth; 20 NYCRR 901.1(a).

Accordingly, each corporate partner of Buffalo Telephone Company that is principally engaged in a telephone business is subject to tax under sections 183 and 184 of Article 9 of the Tax Law. Moreover each corporate partner of Buffalo Telephone Company that is subject to franchise 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.

Issue 2

Section 186-a of the Tax Law provides:

> 1. Notwithstanding any other provision of this chapter, or of any other law, a tax equal to three per centum of its gross income is hereby imposed upon every utility doing business in this state which is subject to the supervision of the state department of public service which has a gross income for the year ending December thirty-first in excess of five hundred dollars, except motor carriers or brokers subject to such supervision under article three-b of the public service law...which taxes shall be in addition to any and all other taxes

and fees imposed by any other provision of law for the same period.

2. As used in section, (a) the word "utility" includes every person subject to the supervision of the state department of public service...

(b) the word "person" means ... co-partnerships ....

Section 186-a of the Tax Law imposes a tax on every utility doing business in New York State that is subject to the supervision of the New York State Department of Public Service. For purposes of section 186-a, a utility includes a person and the definition of a person includes a co-partnership. It is noted that unlike sections 183 and 184, which impose tax only upon corporations, section 186-a imposes tax upon incorporated and unincorporated entities alike.

Since Buffalo Telephone Company, a partnership, is a utility subject to the supervision of the Department of Public Service, Buffalo Telephone Company is subject to tax under section 186-a if its gross income, for the taxable year, is greater than $500.

There is no provision in section 186-a to "pass through" to the partners, the tax imposed on the partnership whereby the partners would individually report and remit their distributive share of the tax. The Department of Taxation and Finance is completely without authority to recognize such a "pass-through" of tax liability. Accordingly, Buffalo Telephone Company, not the partners, must file the section 186-a tax return, form CT-186-P, and must remit any tax due on or before March 15 of each year, for the year ended the previous December 31.

DATED: February 22, 1989

s/FRANK J. PUCCIA
Director
Technical Services

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