

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

TSB-A-97(19)C
Corporation Tax

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C960807A

On August 7, 1996, a Petition for Advisory Opinion was received from Ernst & Young LLP, 787 Seventh Avenue, New York, New York 10019.

The issue raised by Petitioner, Ernst & Young LLP, is the treatment of fax services for purposes of Article 9-A, and sections 183, 184, 186-a and 186-e of Article 9 of the Tax Law.

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

Company X and Company Y, a subsidiary of Company X, are in the business of providing enhanced fax services. Customers send information to Company X and Company Y to be faxed or sent to various recipients either by fax machine, personal computer, telex or electronic mail address. The enhancement feature of the fax service means that a report is formatted by means of merging the customer supplied data on the customer's document format for transmission. Once the documents are prepared, they are transmitted to multiple destinations and recipients simultaneously, thereby allowing numerous recipients to receive the document at the same moment. The destinations are determined by the recipient list provided by the customer. Company X and Company Y also provide computer access and storage services, equipment rental and supply sales. The computer access and storage are in the form of an electronic mailbox. The mailbox may be used by a customer to access a file, to obtain a message or document or report on delivery status.

Customers can access the services of Company X and Company Y by FAX, Personal Computer (PC), mainframe or minicomputer, or Local Area Network (LAN). Company X and Company Y furnish customers with specialized software for access through PCS and LANs.

Company X and Company Y personalize the documents for customers by inserting a recipient's name, address or other unique information by means of a file merge onto any document, such as the customer's letterhead, forms, such as purchase orders or invoices, or other reports. Also, Company X and Company Y can automate the collection and receipt of responses to fax documents sent to a customer's recipients, such as the receipt of large volumes of survey responses, completed questionnaires and inquiries. A key component of all services is the generation of reports showing how and when documents are delivered.

Company X and Company Y provide both "broadcast" and "point-to-point" services. "Broadcast" service involves the sending of the initial document from the customer's computer or fax machine to Company X or Company Y's computer and

switching facilities, which initial document Company X or Company Y then forwards to various recipients at multiple fax, telex, or electronic mail address locations simultaneously. "Point-to-point" service essentially involves the same handling of the document as "broadcast" except that the document is sent to a single destination.

All transmissions made by Company X originate in New Jersey. Company X currently owns multiple switches within various states, however, these switches are used to route calls and are not used to originate any transmissions. All of Company Y's transmissions originate in New York State. These transmissions are both intrastate and interstate, and may be intra-LATA or inter-LATA with respect to those terminating within New York State.

Company X and Company Y bill their customers for "Usage" charges and "non-usage" charges. "Usage" includes charges for the delivery of a document to the ultimate recipient and are billed at various rates, depending on the enhanced feature purchased by the customer, such as report customization or the collection of fax responses. The increase in the rate for the enhancement features provided to the customers are not separately identified on the invoice so that Company X and Company Y may remain competitive with other unrelated companies providing the same service. The "usage" charge rate is then multiplied by a factor such as time, pages, or number of characters per document to obtain the amount billed to the customer. The type of factor used in calculating the total amount billed varies among customers.

Certain service charge items, which are classified as "non-usage" charges, are separately identified on the customer's invoices. These "non-usage" charges include "form or logo" registration, mailbox rental, PC connect charges, and recipient list update charge.

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 corporations liable for tax under section 183 of Article 9 of the Tax Law are not subject to tax under Article 9-A.

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 telegraph or 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 purpose for which the corporation was organized. In Matter of Stat Equipment Corp and Matter of Bi-County Ambulance and Ambulette Transport Corp, Dec Tax App Trib, January 25, 1996, TSB-D-96(3)C, the Tax Tribunal stated the test for proper classification of business activities as follows:

We stated the test in Matter of Capitol Cablevision Sys. (Tax Appeals Tribunal, June 9, 1988):

"[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, affd 288 NY 635; Matter of McAllister Bros. v Bates, 272 AD 511)" (Matter of Capitol Cablevision Sys., supra).

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.

In CCC Telex Service, Inc, Adv Op Comm T & F, July 18, 1989, TSB-A-89 (9)C, it was held that where the petitioner was principally engaged in a telex-fax service business, it would be classified as a transmission corporation and would be subject to tax under sections 183 and 184 (as in effect prior to January 1, 1995) of the Tax Law.

Section 186-e.2(a) of Article 9 of the Tax Law imposes an excise tax "on the sale of telecommunication services by a provider of telecommunication services" from any intrastate telecommunication services and 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 the services are billed or ultimately paid.

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."

In the case of People ex rel Public Service Commn. v NY Telephone Co, 262 App Div 440 (1941), the hotels claimed that a separately stated charge for providing telephone service was not a telephone charge but a charge for additional hotel services, such as bookkeeping or secretarial services. The opinion stated in part, "We think the distinction sought to be made as to the type of charge is somewhat nebulous, but granting that some distinction exists and that extra service is provided in many cases the main purpose is to furnish the public telephone service." In Merchants Refrigerating Co v Taylor, 275 NY 113 (1937), New York City subjected Merchants total receipts which included charges for refrigeration along with other charges to the tax on the furnishing of utility services under a City provision substantially the same as section 186-a of the Tax Law. The opinion stated in part, "The City has subjected the appellant's entire refrigeration business -- storage and all -- to this utility tax. If the construction of the statute urged by the City is adopted, the statute is unconstitutional as arbitrary and discriminatory -- unreasonable."

However, the court did sustain the imposition of the tax on the company's separately stated receipts from the sale of refrigeration by transmission through pipes to its customers. (See also, Empire State Bldg v Dept of Taxation and Fin., 219 AD2d 459 (1995).)

Petitioner's specific questions are as follows.

Question 1. If Company X and Company Y are primarily engaged in providing enhanced fax services, are they considered transmission companies and thereby subject to tax under Article 9 rather than Article 9-A of the Tax Law?

When determining the classification and proper taxability of Company X and Company Y, the business activities of each company "must be viewed in its entirety and from the perspective of its customers - what they buy and pay for" as stated in Stat Equipment Corp, supra. The determination of whether Company X and Company Y are subject to tax under Article 9-A or section 183 of Article 9, depends on what activity Company X and Company Y are principally engaged in.

Company X and Company Y provide enhanced fax services. The enhancement feature of the fax service means that a report sent to Company X or Company Y is formatted by means of merging the customer supplied data on the customer's document format (i.e. letterhead, shipping invoice) for transmission and sent to multiple destinations and recipients simultaneously by fax machine, personal computer, telex or electronic mail address, thereby allowing numerous recipients to receive the document at the same moment. Company X and Company Y also automate the collection and receipt of responses to fax documents sent to a customer's recipients, such as the receipt of large volumes of survey responses, completed questionnaires and inquiries. A key component of all services is the generation of reports showing how and when documents are delivered.

The enhanced fax services provided by Company X and Company Y encompass several activities, one of which is the transmission of a document. However, Company X's and Company Y's overall activities in providing the enhanced fax services to their customers is not a fax service as contemplated in CCC Telex, supra. Rather, the enhanced fax service activities of Company X and Company Y constitute an office service which includes the transmission of a document in their efforts to provide the services that the customer has requested. The customer is paying Company X and Company Y to provide office functions; that is, 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 Company X and Company Y do transmit documents, the transmission is an incidental activity to the overall service Company X and Company Y provide for their customers. Therefore, the enhanced fax services provided by Company X and Company Y do not constitute a business that is taxable under section 183 of the Tax Law.

Further, the activities of Company X and Company Y in providing computer access and storage services, equipment rental and supply sales, would not constitute businesses that are taxable under section 183 of the Tax Law.

Accordingly, it appears that Company X and Company Y are not principally engaged in a business that is taxable under section 183 of the Tax Law and they would not be subject to tax under section 183 of Article 9 of the Tax Law. Company X and Company Y would be subject to tax under Article 9-A of the Tax Law.

Question 2. Assuming that Company X is taxable under section 183 of Article 9 of the Tax Law, is Company X, whose transmissions originate in New Jersey and terminate in New York, in the form of transmission of image (i.e. logos, photographs, etc.) as well as alpha and numeric information and data, providing telecommunication services as a "local telephone business" subject to tax under section 184 of the Tax Law?

Since it appears that Company X is not taxable under section 183 of the Tax Law, this question is moot.

Question 3. Assuming that Company Y is taxable under section 183 of the Tax Law, is Company Y, whose transmissions originate in New York, which are both intrastate and interstate as well as intra-LATA or inter-LATA, providing telecommunication service as a "local telephone business" subject to tax under section 184 of the Tax Law?

Since it appears that Company Y is not taxable under section 183 of the Tax Law, this question is moot.

Question 4. Are the enhanced fax services provided by Company X, which originate in New Jersey, subject to the excise tax under section 186-e of the Tax Law?

As established in the Answer to Question 1, the enhanced fax services which Company X is providing its customers constitutes an office service. Company X's activities in providing the enhanced fax services may include the use of telecommunication services in its efforts to perform the services requested by its customers, but Company X is not a provider of telecommunication services because it is not furnishing or selling telecommunication services to its customers. Therefore, the enhanced fax services provided by Company X would not be subject to the excise tax under section 186-e of the Tax Law, because there is no separately stated charge for the transmission of documents.

Question 5. Are the enhanced fax services provided by Company Y, which originate in New York, subject to the excise tax under the provisions of section 186-e of the Tax Law?

As established in the Answer to Question 1, the enhanced fax services which Company Y is providing its customers constitutes an office service. Company Y's activities in providing the enhanced fax services may include the use of telecommunication services in its efforts to perform the services requested by its customers, but Company Y is not a provider of telecommunication services because it is not furnishing or selling telecommunication services to its customers. Therefore, the enhanced fax services provided by Company Y would not be subject to the excise tax under section 186-e of the Tax Law, because there is no separately stated charge for the transmission of documents.

Question 6. Are Company X and Company Y, which are not regulated by the Public Service Commission, subject to tax on their "gross income", other than telecommunication service income, under section 186-a of the Tax Law?

No. Since Company X and Company Y are not subject to the supervision of the Department of Public Service, they are not utilities subject to tax on their "gross income" under section 186-a of the Tax Law.

DATED: August 6, 1997

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

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