

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

TSB-A-89 (31)S
Sales Tax
August 29, 1989

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S890322A

On March 22, 1989 a Petition for Advisory Opinion was received from NASDAQ, Inc., 1735 K. Street, N.W., Washington D.C. 20006.

The issue raised by the Petitioner, NASDAQ, Inc., is whether any of the charges for the use of private telecommunication lines to provide stock quotations and to execute trades in securities are subject to the tax imposed by Section 1105(b) of the Tax Law.

NASDAQ was formed as a wholly-owned subsidiary of the National Association of Securities Dealers, Inc. ("NASD") to be the owner and operator of a computerized data processing and communications system ("NASDAQ System") that collects, stores, and disseminates "up-to-the-second" quotations from a nationwide network of over-the-counter broker/dealers making markets in stocks which have been approved for inclusion in the NASDAQ System. NASDAQ operates two data centers, located in Trumbull, Connecticut and Rockville, Maryland, which are designed to collect, process, store, and disseminate all the information relating to the stocks included in the NASDAQ System. This information is transmitted to the various broker/dealers via private telecommunication lines maintained by AT&T and the local telephone companies. In addition, requests for information about traded securities from the various broker/dealers travel via these lines to the data centers in Trumbull, Connecticut or Rockville, Maryland.

In addition, the NASDAQ System can also be used to access specialized systems for the execution of trades in selected securities. These execution systems are owned and operated by a party related to NASDAQ who reimburses NASDAQ for its use of the NASDAQ system. Such execution systems generally fall into two categories: (1) automatic execution; and (2) execution requiring acceptance by the market maker.

With automatic execution, a subscriber ("the order-entry firm") enters an order to buy or sell an identified number of shares of one of the specified securities. That order travels over the NASDAQ System to the Trumbull, Connecticut data center where the order is automatically executed against a specified market maker at NASDAQ's "inside price" (*i.e.*, the best bid or ask price for that security as set by the various market makers). Both the order-entry firm and the market maker are then notified by the Trumbull, Connecticut data center of the transaction.

As with the requests for information from the Trumbull, Connecticut data center, a buy or sell order executed automatically within the Trumbull, Connecticut data center involves communication between Trumbull, Connecticut and the order-entry firm.

The other format for executing trades using the NASDAQ System consists of orders by an order-entry firm that must be accepted or rejected by a market maker for execution to occur.

When an order-entry firm enters a buy or sell order that must be accepted by a market maker before execution can occur, the order travels via the NASDAQ System to the Trumbull, Connecticut data center. At the data center, the computer application which controls the execution performs the following series of steps:

- (1) the identity of the order-entry firm is determined;
- (2) various validation checks are performed, including the following:
 - (a) determining whether the stock market is open for trading;
 - (b) determining whether the order-entry firm properly entered the offer;
 - (c) determining whether the number of shares subject to the offer is within the appropriate size limits for that transaction;
 - (d) determining whether a valid price was entered;
 - (e) determining whether the market maker selected is an authorized market maker in that security;
 - (f) determining whether the market maker accepts the type of order entered against it;
 - (g) determining whether the market maker is presently active in the security;
and
 - (h) determining whether the market maker has an appropriate arrangement with a clearing agency or NASDAQ member for the clearance and settlement of the transaction;
- (3) if the order is validated in step (2), the computer establishes a file for that order with a system reference number;
- (4) a message is then sent by the Trumbull, Connecticut data center to the market maker which identifies, among other items, the identities of the market maker and the order-entry firm, the date and time of the order entry, whether the order is a buy order or sell order, the number of shares subject to the order, the identity of the security, the price, the system reference number, and a designation whether partial orders are acceptable;

(5) the market maker then has two minutes to accept the order by informing the Trumbull, Connecticut data center of its acceptance by reference to the system reference data center given the order by Trumbull, Connecticut data center;

(6) the acceptance is transmitted back to the Trumbull, Connecticut data center, where the transaction is confirmed by the computer, confirmations are sent to the order-entry firm and market maker, clearing information is delivered to the appropriate clearinghouse.

Section 1105(b) of the Tax Law imposes a tax upon "[T]he receipts from every sale other than sales for resale, of telephony and telegraphy and telephone and telegraph service of whatever nature except interstate and international telephony and telegraphy and telephone and telegraph service."

Section 527.2(d)(4) of the Sales and Use Tax Regulations provides that "a service is not considered telegraphy or telephony if either of these services is merely an incidental element of a different or other service purchased by the customer."

Petitioner as part of its activities collects, processes, stores and disseminates all the information relating to the stocks included in the NASDAQ System. In addition it provides services that executes trades in securities. While the transmission of information is certainly an integral part of its business, its transmissions cannot be likened to that of an ordinary telephone company since the services provided are more than that of a mere conduit that only transmits to third party recipients messages given it by various originators. Therefore in accordance with Section 527.2(d)(4) of the Sales and Use Tax Regulations, Petitioner is not engaged in providing the service of telephony and thus the services provided by it are not subject to the tax imposed by Section 1105(b) of the Tax Law. A similar rationale was adopted by the Court of Appeals in Quotron Systems, Inc. v Gallman 39 NY2d 428 where the court concluded that a company engaged in similar activities to that of Petitioner was not engaged in the furnishing of telegraph services and thus was not a utility subject to the corporation tax imposed by Section 186-a of Article 9 of the Tax Law.

However, the issue is then whether Petitioner's services in providing stock quotations and in executing trades in securities are subject to sales tax under Section 1105(c)(1) of the Tax Law.

Section 527.3(a) of the Sales and Use Tax Regulations provides that:

(1) Section 1105(c)(1) of the Tax Law imposes a tax on the receipts from the service of furnishing information by printed, mimeographed or multigraphed matter or by duplicating written or printed matter in any manner such as by tapes, discs, electronic readouts or displays.

TSB-A-89 (31)S
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(2) The collecting, compiling or analyzing information of any kind or nature and the furnishing reports thereof to other persons is an information service.

(3) Among the services which are information services are credit reports, tax or stock market advisory and analysis reports and product and marketing surveys.

Petitioner states that it operates a "communication system ("NASDAQ System") that collects, stores, and disseminates 'up-to-the-second' quotations from a nationwide network..." Petitioner sells and delivers its information over telecommunication lines. The quotes are displayed on terminals generally located at its customer's premises.

Section 527.3(a)(1) of the regulations imposes a tax on receipts from furnishing information "... in any manner such as by electronic recordants or displays." (Emphasis supplied)

Therefore Petitioner is selling an information service which is not personal or individual in nature and thus is subject to sales tax.

Because the sales tax is a destination tax, the point of delivery controls the rate of tax to be collected. The point of delivery of Petitioner's service would be the location of the computer terminals used by its customers.

However when the NASDAQ system is used to purchase and sell stocks and other securities, Petitioner is not providing an information service. The execution of trades in securities is not one of the services taxed pursuant to Section 1105(c) of the Tax Law and thus this aspect of Petitioner's business is not subject to the imposition of sales tax.

DATED: August 29, 1989

s/FRANK J. PUCCIA
Director
Technical Services Bureau

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