



**FINANCE**  
**NEW • YORK**  
THE CITY OF NEW YORK  
DEPARTMENT OF FINANCE

July 21, 2004

RE: Ruling Request

Utility Tax  
FLR: 034815-011

Dear \_\_\_\_\_ :

This letter responds to your request, received October 31, 2003, on behalf of (the "Taxpayer"), for a ruling regarding the application of the New York City Utility Tax (the "City UT") to the Taxpayer's businesses. This office received additional information concerning this request on February 24, March 17, April 30, and June 25, 2004. This letter supercedes our letter to you dated May 26, 2004.

**FACTS**

The facts presented are as follows:

The Taxpayer, a wholly owned subsidiary of \_\_\_\_\_ (the "Parent"), is incorporated under the laws of \_\_\_\_\_. The Parent, organized under the laws of \_\_\_\_\_ ("Country X"), is the principal provider of telecommunications services in that country. Through various subsidiaries, the Parent also provides telecommunications services in other countries. The Parent formed the Taxpayer in \_\_\_\_\_ to be its contact with emerging commercial and technological trends in the United States.

In 2001, the Federal Communications Commission granted the Taxpayer a license to operate as an international facilities-based carrier and resale carrier between the United States and other countries. To conduct this business, the Taxpayer owns and operates a switch in \_\_\_\_\_ and other technical equipment in New York City. It also leases office space in the City.

The Taxpayer sells international, long-distance telecommunications services to other international long-distance carriers on a variable, per minute basis. Those carriers then resell the services to other carriers or resell them to their ultimate, end-user customers. The Taxpayer often will not know the identity of the ultimate end users. The following example illustrates a typical transaction involving the Taxpayer. A telephone call originates in the City. The call is

carried on the lines of an interexchange carrier (an “IXC”) to the Taxpayer’s switch, where it is transferred to the Parent’s undersea cable. The call then terminates in County X. The service address is in the City. The IXC pays the Taxpayer \$1.00 for its services and bills the customer in the City \$10.00 for the call.

You have represented that the Taxpayer is subject to tax under section 186-e of the New York State Tax Law (the “Tax Law”). You have also made the following representation:

Based on the facts presented with respect to the plaintiff Cable & Wireless in Cable & Wireless, Inc. v. The City of New York Department of Finance, 190 Misc. 2d 410, 735 N.Y.S. 2d 717. (Supreme Court, New York County, 2001), we represent that the Taxpayer operates in a competitive environment where market forces shape its rates, capital structure and corporate decisions to the same extent as the plaintiff in that case.

## **ISSUES**

You have requested the following rulings:

1. The Taxpayer is not subject to the City UT as a “utility.”
2. In computing its City UT liability as a vendor of utility services, the Taxpayer is entitled to exclude from its gross operating income the amount of its sales of utility services for resale.

## **CONCLUSIONS**

Based upon the facts presented and the representations submitted, we conclude that

1. The Taxpayer is not subject to the City UT as a “utility.”
2. In computing its City UT liability as a vendor of utility services, the Taxpayer is entitled to exclude from its gross operating income the amount of its sales of utility services for resale.

## **DISCUSSION**

The City UT is imposed on entities providing utility services in the City. “Utilities,” providers of utility services that are subject to the supervisions of the New York State Public Service Commission (the “PSC”), are subject to tax on their “gross income;” “vendors of utility services,” providers of those services that are not subject to the PSC’s supervision, are subject to tax on their “gross operating income.” New York City Administrative Code (the “Code”) § 11-1102.a.

The New York City General Corporation Tax (the “GCT”) is imposed on domestic and foreign corporations for the privilege of doing business, employing capital, owning or leasing property or maintaining an office in the City. Code § 11-603.1. Under Code section 11-603.4, utilities are exempt from the GCT. There is no comparable exemption for vendors of utility services. A

vendor of utility services is subject to both the City UT and the GCT, but is permitted to reduce its business income, for purposes of the GCT, by the ratio that its gross operating income subject to City UT bears to its total gross operating income.

#### Taxpayer as a Utility.

Because it is providing telecommunications services in New York City, the Taxpayer is subject to the City UT, either as a utility or a vendor of utility services. Code §§ 11-1101.7 and 1101.9. Code section 11-1101.6 defines a utility as “[e]very person subject to the supervision of the department of public service.” The PSC supervises utilities in the state. Section 5.1(d) of the New York State Public Service Law (the “PSL”) provides that the PSC’s “jurisdiction, supervision, powers and duties” apply to entities “owning, leasing or operating” any telephone lines in the State.

In Cable & Wireless, Inc. v. The City of New York Department of Finance, 190 Misc. 2d 410, 735 N.Y.S. 2d 717 (Supreme Court, New York County, 2001), the issue presented was whether a reseller of telephone services was “subject to the supervision of the department of public service.” for purposes of Code section 11-1101.6 by reason of PSL section 5.1(d). The court examined the history of the City UT in detail, distinguishing traditional utilities subject to the supervision of the PSC from resellers of telephone services. Noting that traditional utilities were monopolies that “provided services or commodities viewed as necessities,” the court concluded that: “it is evident that the City Council did not intend the Utility Tax on gross income to apply to an entity such as Cable which operates in a competitive environment where market forces shape its rates, capital structure and corporate decisions.” Id., at 723. As a result, it found that the reseller was not subject to the supervision of the department of public service for purposes of Code section 11-1101.6 and thus not a utility under the City UT.

In that regard, you have represented that:

Based on the facts presented with respect to the plaintiff Cable & Wireless in Cable & Wireless, Inc. v. The City of New York Department of Finance, 190 Misc. 2d 410, 735 N.Y.S. 2d 717. (Supreme Court, New York County, 2001), we represent that the Taxpayer operates in a competitive environment where market forces shape its rates, capital structure and corporate decisions to the same extent as the plaintiff in that case.

Based on your representation, we conclude that the Taxpayer is not a utility under the City UT. Because it is providing telecommunications and is not a utility, the Taxpayer could be subject to the City UT only as a vendor of utility services.

#### The Taxpayer as a Vendor of Utility Services.

Code section 11-1101.7 defines a vendor of utility services as:

Every person not subject to the supervision of the department of public service, and not otherwise a utility as defined in subdivision six of this section, who

furnishes or sells gas, electricity, steam, water or refrigeration, or furnishes or sells gas, electric, steam, water, refrigeration or telecommunications services, or who operates omnibuses, (whether or not such operation is on the public streets); regardless of whether such furnishing, selling or operation constitutes the main activity of such person or is merely incidental thereto.

A vendor of utility services is subject to tax on its gross operating income. Code § 11-1102.a. Code section 11-1101.5 defines gross operating income, in part, as including:

receipts received in or by reason of any sale made or service rendered, of the property and services specified in subdivision seven of this section in the city, including cash, credits and property of any kind or nature (whether or not such sale is made or such service is rendered for profit), without any deduction therefrom on account of the cost of the property sold, the cost of materials used, labor or other services, delivery costs or any other costs whatsoever, interest or discount paid, or any other expenses whatsoever....

You have presented two reasons to support the conclusion that the Taxpayer does not earn gross operating income for City UT purposes: first, that the Taxpayer's telecommunication services do not involve transactions that originated and terminate in the City; and, second, that because the Taxpayer provides its services to other entities that then resell those services to the ultimate consumer or another vendor, it is entitled to exclude from its gross operating income the amount of its sales of utility services for resale.

Concerning the first reason, the only geographic restriction in the Code is that the services must be rendered "in the City," it does not require that the calls originate or terminate in the city. Concerning resales of utility services, Code section 11-1102(b) provides that "so much of the gross income of a utility shall be excluded from the measure of the tax imposed by [the City UT], as is derived from sales for resale to vendors of utility services validly subject to the tax imposed by [the City UT]." The Code does not provide comparable relief for vendors of utility services engaging in sales for resale. Thus, the Code does not address either of the two issues presented.

The City's authority to impose the City UT is limited by the interaction of four statutes: Tax Law sections 1201, 1221, and 186-a, and General City Law section 20-b (the "1221 Statutory Scheme"). Brooklyn Union Gas Co. v. McGoldrick, 270 A.D. 186 (1st Dept., 1945), aff'd without opinion, 298 N.Y. 536 (1948). Matter of Hilton Hotels Corp. v. Comm. of Finance of the City of NY, 219 A.D.2d 470, 475-6 (1st Dept., 1995).

The 1221 Statutory Scheme starts with Tax Law section 1201(a), which authorizes the City to impose the City UT. Brooklyn Union Gas, 67 N.Y.2d at 1038. Tax Law section 1201 also provides that any tax imposed under its authority is "subject to the applicable limitations and exemptions in Part II of" Article 29 of the Tax Law.

Tax Law section 1221(a)(3), part of Part II of Article 29, provides, in part, that

(a) This article shall not be construed as authorizing the imposition of: ...

(3) except in accordance with the provisions of section [20-b] of the general city law, a tax upon gross incomes, gross operating incomes or gross receipts of persons subject to taxation under the provisions of section [186-a] or [186-e] of this chapter....

You have represented that the Taxpayer's gross operating income is subject to tax under Tax Law section 186-e. As a result, the City UT must be applied to the Taxpayer in accordance with General City Law section 20-b.

General City Law section 20-b provides, in part, that:

Notwithstanding any other provisions of law to the contrary, any city of this state, acting through its local legislative body, is hereby authorized and empowered to adopt and amend local laws imposing in any such city a tax such as was imposed by section [186-a] of the tax law, in effect on January first, nineteen hundred fifty-nine, except that the rate thereof shall not exceed one per centum of gross income or of gross operating income....

A tax imposed pursuant to this section shall have application only within the territorial limits of any such city, and shall be in addition to any and all other taxes. This section shall not authorize the imposition of a tax on any transaction originating or consummated outside of the territorial limits of any such city, notwithstanding that some act be necessarily performed with respect to such transaction within such limits.

General City Law section 20-b limits the City UT in several respects. Of particular relevance to this ruling are the requirements that: (i) the tax can only be imposed on transactions that both originate and terminate in the City; and (ii) the City can only impose a utility tax "such as was imposed by [Tax Law section 186-a] in effect on January 1, 1959."

Concerning the first requirement, you have represented that: (i) The Taxpayer sells international, long-distance telecommunications services to other international long-distance carriers on a variable, per minute basis; (ii) those carriers then resell the services to other carriers or resell them to their ultimate, end-user customers; and (iii) that the Taxpayer often will not know the identity of the ultimate end users. Because the Taxpayer sells its services to long distance carriers, it would seem highly unlikely that its services are used on a telephone call that both originates and terminates in the City. However, we cannot conclude that none of the Taxpayer's services involves a transaction that originates and terminates in the City because such a conclusion would require a factual determination that is properly an audit function. Title 19 of the Rules of the City of New York § 16-01(c)(5).

The second limitation provided by General City Law section 20-b is that the City can only impose a utility tax "such as was imposed by [Tax Law section 186-a] in effect on January 1, 1959." As in effect on January 1, 1959, Tax Law 186-a imposed a tax on income of utilities. A provider of "gas, electricity, steam, water, refrigerator, telephone, or telegraphic" service, not subject to the supervision of the PSC, paid at the rate of three percent of its "gross operating income." Thus

while the State UT did not use the term “vendor of utility services” it taxed unregulated providers of utility services much the same as the City UT does.

Tax Law 186-a(2)(d) defined “gross operating income” as “receipts received in or by reason of any sale ... made for ultimate consumption or use by the purchaser of gas, electricity, steam, water, refrigerator, telephone, or telegraphic service in this state.” Thus, under the law in effect on January 1, 1959, only income received from sales to ultimate users were included “gross operating income;” sales of utility services to another entity that resold those services were excluded.

As discussed above, General City Law section 20-b requires that the City UT “must be a tax such as was imposed by [Tax Law section 186-a] in effect on January 1, 1959.” The phrase “such as” is not the same as “identical to,” permitting some differences on minor matters. The definition of gross operating income was an integral component of the State UT as in effect on January 1, 1959. As a result, we conclude that, when it amended General City Law 20-b in 1959, the legislature intended that sales for resales would be excluded from gross operating income of vendors of utility services under the City UT.

As a result, we conclude that the Taxpayer can exclude from its gross operating subject to the City UT income received from sales of utility services for resale.

#### GCT Consequences.

The Taxpayer has an office and does business in the City, and, as a result, it is subject to the GCT. Because it is not a utility under the City UT, it remains subject to the GCT. Under Code section 11-603.4, it is permitted to reduce its business income, for purposes of the GCT, by the ratio that its gross operating income subject to City UT bears to its total gross operating income. For purposes of Code section 11-603.4, income received from sales of utility services for resale that is excluded from the City UT and income that is not subject to tax because it is from transactions that do not originate and terminate within the City, is not considered gross operating income subject to the City UT, and the Taxpayer cannot use that income to reduce its business income subject to the GCT.

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The Department of Finance reserves the right to verify the information submitted.

Sincerely,

Ellen E. Hoffman  
Assistant Commissioner for Tax Law and Conciliations

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