October 11, 2005

RE: Ruling Request

Utility Tax
FLR: 054835-011

Dear :

This letter responds to your request, dated April 25, 2005, on behalf of the Condominium (the "Taxpayer") for a ruling regarding the application of the New York City Utility Tax (the "UTX") to the situation described below. This office received additional information concerning this request on April 31, and June 11, 2005.

FACTS

The facts presented are as follows:

The (the "Property") is a complex located at in . It includes . The Taxpayer is the condominium established with respect to the Property.

The Taxpayer is composed of units (the "Units") and is managed by a condominium board (the "Board") on behalf of the owners of those units (the "Unit Owners"). Appurtenant to each Unit Owner's interest is an interest in the Taxpayer's common elements, which are used by or for the benefit of all the Unit Owners. Those common elements include its common areas (the "Common Areas"), such as the lobby, and a plant to provide heat, ventilation, and air conditioning ("HVAC") service for the Units (the "Central Plant"). The Units, have, in turn, their own organizational structure; some have a condominium organization within the Unit ("Subunits") with a condominium board (a "Subboard").

Utility Use at the Property.

With a few exceptions noted below, the Taxpayer is generally responsible for acquiring utility services for use at the Property, pursuant to which it acquires water from the City and steam and electricity from or another utility provider (together, the "Utility Provider"). The Taxpayer uses those utilities to operate the Central Plant, to provide services to the Common Areas, and to provide utility services to the Unit Owners for consumption by those Owners.

The Central Plant. The Central Plant produces chilled water and HVAC services for the Common Area and is used to supply chilled water and HVAC services to the Unit Owners. The Taxpayer allocates charges for the utility services consumed in operating the Central Plant to the Unit Owners based on the owner's "AC Factor." Each Unit Owner's AC Factor charge is based upon a combination of the actual design capacity for its Unit (for fixed costs) and actual usage as measured by BTU meters for its Unit (for variable costs).

The Common Areas. The Taxpayer is responsible for the Common Areas and uses utility services it acquires for use in those areas (the "Common Utilities"). The Taxpayer allocates charges with respect to the Common Utilities to the Unit Owners based on the owners' agreed upon "Common Area Percentages."

Operation of the Units. The Taxpayer provides utility services to the Unit Owners for consumption in the operation of their Units (the "Unit Operation Utilities") and charges the Unit Owners generally based on submeters specific to each Unit.[1]

Utilities Used by the Units.

The Unit Owners are responsible for the Unit's share of the AC Factor charge, Common Utilities, and Unit Operation Utilities. Many of the units have common areas (the "Unit Common Areas"), such as the lobby, which are used by all the Unit Owners, and the Unit must pay utility charges associated with use of the Unit Common Areas (the "Unit Common Utilities"). As the needs and structure of the Units vary, their use of utilities and accounting for that use, vary.

The Corporation's Units. The "Corporation's Units" are two Units owned by (the "Corporation"). One such Unit (the "Corporate Office Unit") includes corporate offices and space for the Corporation and its affiliates. The other such Unit (the "North Office Unit") is composed of 100,000 feet of office space. Currently, the Corporation intends to occupy both the Corporate Office Unit and the North Office Unit. However, in the future it is possible that some part or all of the North Office Unit could be leased to third-party tenants.

The Corporation's Units do not use or pay Unit Operation Utilities and AC Factor because they have separate submetered electricity acquired directly from the Utility Provider and their own

[1] Currently, because not all of the submeters are fully operational, some charges are estimated. This ruling is requested based upon the ultimate factual situation. Even after the submeters are fully operational, the Board may charge each Unit Owners for certain utilities based on allocations rather than submeters.

HVAC plant. However, the Corporation must pay the Taxpayer for the Corporation's Units' share of the Common Utilities. The Corporation does not anticipate billing future third-party tenants in the North Office Unit for submetered electric, steam, water, or AC Factor, although that may change.

The ___. The " Unit" is owned and operated by one entity, a . That pays for the AC Factor charge, Common Utilities, and Unit Operation Utilities charges allocated to the Unit.

Residences. Two Units, the "North Residential Unit" and the "South Residential Unit," are composed of residential Subunits. A board (the "Subboard") manages each Unit, which includes Unit Common Areas, on behalf of the Subunit Owners. The North and South Residential Units bill Subunit Owners for submetered electric for use in the Subunit Owners' premises and bill common charges that include the Units' share of the AC Factor, steam, water, the Common Utilities, and the Unit Common Utilities.

Offices. The "Office Unit" rents out office space to tenants. The Office Unit Owner bills office tenants for submetered electric and AC Factor charge for the tenants' use in their premises and bills rent and escalations that cover the Office Unit's share of steam, water, Common Utilities, and Unit Common Utilities.

Retail establishments. The "Retail Unit" rents out space for retail establishments. The Retail Unit Owner bills retail tenants for submetered electric, steam, AC Factor charge, and hot water charges, and, in some cases, water, for use in their premises. It bills rent and escalations that cover the Office Unit's share of the, Common Utilities, and the Unit Common Utilities.

_____. The " Unit" consists of an and related facilities and is used by Inc. (the " Company"), a not-for-profit organization affiliated with . The Unit acquires electricity directly from the Utility Provider. The Taxpayer bills the Company for its share of AC Factor charge and Common Utilities.

Parking. The "Parking Unit" rents out space for a garage. The Parking Unit Owner bills its tenant for submetered electric, for AC Factor on a straight pass-through basis, and for rent and escalations that cover the Parking Unit's share of the Common Utilities.

Summary.

The Taxpayer has contracted with the Utility Provider to procure electricity and steam and with the City to acquire water for use at the Property. Those utility services will ultimately be consumed by the persons occupying the Property. Between the delivery of utilities to the Property and the ultimate consumer, however, there are a variety of layers of legal entities and owners. In some cases, such as the Unit, the Unit Owner is the ultimate consumer; in others, such as the Residential Units, the Unit Owners distribute the services to other entities for ultimate consumption.

The UTX consequences of utility services used at the Property but not acquired by the Taxpayer, such as electricity acquired directly by the Corporation's Units and the Unit, and utilities

used in the operation of the Corporation Unit's HVAC plant, are not addressed by this ruling.

ISSUES

You have requested that we rule as follows:

1. The Taxpayer will be treated as a landlord providing utility services to its tenants for purposes of the exception to the sale-for-resale exclusion, and, as a result:

   a. the sale-for-resale exclusion will not apply to the sales of utility services by the Utility Provider to the Taxpayer, and

   b. with respect to electricity and steam and electric and steam service acquired by the Taxpayer as to which UTX is properly paid, UTX will not apply to any subsequent redistribution of those services to the Unit Owners, by the Unit Owners, or by distributees of the Unit Owners for use in the Property; and.

2. The UTX will not apply to water acquired by the Taxpayer from the City for use in the Property.

CONCLUSIONS

Based upon the facts presented and the representations submitted, and exercising the discretion afforded to the Commissioner of Finance under Section 11-1112 of the New York City Administrative Code (the "Code"), we conclude as follows:

1. The Taxpayer will be treated as a landlord providing utility services to its tenants for purposes of the exception to the sale-for-resale exclusion, and, as a result:

   a. the sale-for-resale exclusion will not apply to the sales of utility services by the Utility Provider to the Taxpayer, and

   b. with respect to electricity and steam and electric and steam service acquired by the Taxpayer as to which UTX is properly paid, UTX will not apply to any subsequent redistribution of those services to the Unit Owners, by the Unit Owners, or by distributees of the Unit Owners for use in the Property; and.

2. The UTX will not apply to water acquired by the Taxpayer from the City for use in the Property.

DISCUSSION

The UTX is imposed on entities providing utility services, which include electricity, steam, and water. A "utility," a provider of utility services subject to the supervision of the New York State Public Service Commission (the "PSC"), is subject to tax at the rate of 2.35 percent of its "gross income, which includes "all receipts received in or by reason of any sale." Code §§ 11-1101.4

and 1102. A "vendor of utility services," a provider of utility services not subject to the supervision of the PSC, is subject to tax at the rate of 2.35 percent of its "gross operating income," which includes income derived from providing utility services. Code §§ 11-1101.5 and 1102.

Resales under the UTX. 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 this chapter, as is derived from sales for resale to vendors of utility services." Sales for resales are similarly excluded from the gross operating income of vendors of utility services.[2] As a result, when utility services are sold by a utility or a vendor of utility services to a vendor of utility services that, in turn, resells the services to the ultimate consumer, the tax is imposed when those services are provided to the ultimate consumer, rather than upon the initial sale.

The Code was amended in 1998 (New York Laws of 1998, chapter 536) to address multiple resales of utility services by a landlord providing utility services to its tenants (the "1998 Amendments"). Before the 1998 Amendments, a landlord, as a vendor of utility services, would be subject to the UTX on income derived from providing utility services to its tenants, and, under Code section 11-1102(b), the utility would exclude the income as income derived from sales to the landlord for resale. The 1998 Amendments amended Code section 11-1102(e) to provide that where a landlord provides utility services "as incident to [its] activity of renting premises to tenants," the income derived from providing those services will be excluded from the landlord's gross operating income. However, in the case of electricity, gas, or steam, but not water, the exclusion is available to the landlord only to the extent that the UTX has been validly paid on the prior sale, *e.g.*, the sale by a utility to the landlord. The landlord must pay the tax to the extent it has not been paid on the prior sale. The 1998 Amendments also amended Code section 11-1102(b) to provide that the sale-for-resale exclusion does not apply to sales to "to a vendor of utility services for resale to its tenants as an incident to such vendor's activity of renting premises to tenants."

The effect of the 1998 Amendments was to change the point in the process of selling utility services at which the UTX is imposed. Rather than being imposed on the sale to the ultimate consumer, *i.e.* the tenant, the tax is imposed on the purchase of the utilities by the vendor, the landlord. The purpose of this change was to reduce the burden of compliance with the UTX, as described in the Memorandum in Support of the 1998 Amendments:

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[2] The City's authority to impose the City UTX is limited by the interaction of four statutes: Tax Law sections 1201, 1221, and 186-a, and General City Law section 20-b. 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). General City Law Section 20-b provides that the UTX must include the limitations provided by section 186-a of the New York State Tax law, as in effect on January 1, 1959.

Tax Law 186-a(2)(d), as in effect on January 1, 1959, 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 was included "gross operating income;" income from sales of utility services to another entity that resold those services was excluded. Under General City Law 20-b, that exclusion applies to the UTX.

> Under existing law, the determination of the amount of electricity resold by landlords to tenants and the charges attributable to such resales often requires complex calculations …. Utilities, on the other hand, currently pay the Utility tax on sales directly to consumers and pass the cost of the tax liability along to consumers as a separate charge on the utility's bill. Utilities are therefore, positioned to assume responsibility for paying the utility tax on sales to landlords for resale with only a minimal additional compliance burden.

Code section 11-1101 defines "tenant" broadly to mean a "person paying, or required to pay, rent for premises as lessee, sublessee, licensee or concessionaire."

The Commissioner's discretion. The Code grants the Commissioner of Finance latitude, in addition to its rule-making and other powers, to determine methods for determining income subject to the UTX. Code section 11-1112 provides that:

> In addition to the powers granted to the commissioner of finance in this chapter, he or she is hereby authorized and empowered: …
>
> 2. To prescribe methods for determining the amount of "gross income" and "gross operating income" received by a person subject to tax hereunder; ….

Utilities provided by The Utility Provider.

In this case, the Utility Provider provides utility services, electricity and steam, to the Taxpayer for use in the Property. The Utility Provider may be either a utility or a vendor of utility services for UTX purposes. This discussion is based on the assumption that, absent any sale-for-resale exclusion, the Utility Provider would pay UTX on sales to the Taxpayer.

Resale exclusions. The Taxpayer uses the utility services acquired from the Utility Provider in a number of ways, including furnishing them for use by other entities in the Property, such as the Unit Owners. Applying the sale-for-resale exclusion in this case, with the numerous layers of legal entities and owners, results in a complex maze of tax liability presenting the potential for administrative and compliance problems.

If the 1998 Amendments were to apply to the utility services acquired by the Taxpayer for use at the Property, the UTX would be imposed upon the sale of the utility services by the Utility Provider to the Taxpayer, and neither the Taxpayer nor any other entity would have any further filing or payment obligations with respect to utilities used at the Property. Those amendments, however, apply to utility services provided to tenants. Code section 11-1101 defines "tenant" broadly to mean a "person paying, or required to pay, rent for premises as lessee, sublessee, licensee or concessionaire." Like tenants, the Unit Owners pay the Taxpayer a monthly maintenance charge, which may include charges for utility services, and they share many attributes with tenants. However, the Unit Owners are not directly covered by the provisions relating to "tenants" because they are property owners and do not pay rent for the right to use or occupy premises.

Applying the Commissioner's discretionary powers**.** Code section 1112 grants the Commissioner latitude, in addition its rule-making and other powers, to prescribe methods for determining income subject to the UTX.

The 1998 Amendments did not address property subject to a condominium regime. The relationship of a landlord to its tenants and of a condominium to unit owners bear many resemblances, and, in some legal contexts, the differences have been found not to matter. *See, e.g.*, 200 East 74 Corporation v Dallas, 164 Misc. 2d 417 (N.Y. Civ. Ct. 1995). (the three-day demand for rent due before commencing proceedings that applied to rental tenants held to apply to shareholders in cooperative building and, in dictum, to a condominium arrangement). In terms of the provision of utility services there is little difference between a rental tenant and the Unit Owners. As in the case of a landlord of rental property, the Taxpayer contracts with a utility to provide services for the Units and passes those charges to the Unit Owners. The Taxpayer, like a landlord, is charged with the responsibility of providing the service and must account to the Unit Owners for that service.

The 1998 Amendments were intended to provide more efficient UTX administration and collection in the context of utility services sold by landlords to tenants. If the 1998 Amendments were applied, the Utility Provider would pay the tax, and it would be responsible for information concerning the UTX applicable to the utility services acquired by the Taxpayer, including returns, audits, and collection of the tax. Given the complexity of the ownership and operational structure of the Taxpayer, applying the 1998 Amendments to the Taxpayer as if it were a landlord would provide for more efficient administration and collection of the tax and help achieve the purpose of those amendments, as stated in the Memorandum of Support.

Based on the above, we conclude that, applying the 1998 Amendments to utility services acquired by the Taxpayer for use at the Property is consistent with the purpose of those amendments, and would reduce the administrative burden on the Commissioner. As a result, exercising the discretion afforded the Commissioner by Code section 1112, we conclude the UTX with respect to the utility services acquired by the Taxpayer for use at the Property should be imposed on the Utility Provider.

Water provided by the City.

The City's authority to impose the City UTX is limited by the interaction of four statutes: Tax Law sections 1201, 1221, and 186-a, and General City Law section 20-b. 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). General City Law Section 20-b provides that the UTX must include the limitations provided by section 186-a of the New York State Tax law, as in effect on January 1, 1959. Tax Law section 186-a(2)(b) as in effect on January 1, 1959 exempted "the state, municipalities, political and civil subdivisions of the state." Under General City Law 20-b, that exclusion applies to the UTX. The City, a municipality of the state, will provide water to the Taxpayer for use in the Property. Because the UTX does not apply to utilities services provide by "the state, municipalities, political and civil subdivisions of the state," water the City provides to the Taxpayer is not subject to the UTX.

Conclusions.

Based upon the facts presented and the representations submitted, and exercising the Commissioner's discretion under Section 11-1112 of the New York City Administrative Code (the "Code"), we conclude as follows:

1. The Taxpayer will be treated as a landlord providing utility services to its tenants for purposes of the exception to the sale-for-resale exclusion, and, as a result:

   a. the sale-for-resale exclusion will not apply to the sales of utility services by the Utility Provider to the Taxpayer, and

   b. with respect to electricity and steam and electricity and steam service acquired by the Taxpayer as to which UTX is properly paid, UTX will not apply to any subsequent redistribution of those services to the Unit Owners, by the Unit Owners, or by distributees of the Unit Owners for use in the Property; and.

2. The UTX will not apply to water acquired by the Taxpayer from the City for use in the Property.

Those conclusions apply only to the facts presented and should not be interpreted as applying to the UTX treatment of other condominiums or any other taxpayers.

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The Department reserves the right to verify the information submitted.

Sincerely,

Ellen E. Hoffman
Assistant Commissioner for Tax Law and Conciliations

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