New York City Tax Appeals Tribunal

In the Matter of ASSOCIATED BUSINESS TELEPHONE SYSTEMS CORPORATION Petitioner	DECISION TAT (E) 93-1053(UT)

Associated Business Telephone Systems Corporation ("Petitioner") filed an Exception to that portion of the Determination of an Administrative Law Judge ("ALJ") dated July 21, 2005 (the "ALJ Determination") finding Petitioner liable for a modified New York City Utility Tax ("UT") deficiency for the period November 1, 1988 through September 30, 1991 (the "Tax Periods") issued by the New York City Department of Finance (the "Department").[1] The Petitioner appeared by Stuart A. Wilkins, Esq., of the Law Offices of Stuart A. Wilkins, P.C., and the Commissioner of Finance of the City of New York (the "Commissioner" or "Respondent") appeared by Frances J. Henn, Esq., Senior Counsel, New York City Law Department. The Parties filed briefs and oral argument was held before the Tribunal.[2] Commissioner Robert J. Firestone did not participate in this Decision.

[1]Petitioner filed a Petition for Hearing with the Department dated August 21, 1992. Pursuant to the provisions of 1992 N.Y. Sess. Laws, ch. 808, §140 (McKinney), this matter was transferred to the Tribunal for determination.

[2]Petitioner's Exception to a Determination/Order of the ALJ dated May 31, 2005 involving UT deficiencies for the periods April 1, 1993 through December 31, 1995 and January 1,1996 through October 31, 1996 was heard at the same oral argument. However, separate Decisions are being issued by the Tribunal.

Petitioner is a New Jersey corporation headquartered in New Jersey.[3] During the Tax Periods, Petitioner was engaged in the business of providing telephone systems and services.

Petitioner did not file UT returns for the Tax Periods.

After the completion of a field audit, the Department issued a Notice of Determination, dated August 5, 1992, (the "Notice") to Petitioner assessing a UT deficiency for the Tax Periods in the principal amount of $91,439.89 plus interest computed to August 25, 1992 and penalties for a total deficiency of $155,550.33.

Petitioner and Park Centre Associates ("Park Centre"), a New York limited partnership, entered into a Telephone Service Agreement (the "Agreement") dated June 17, 1986. Taxpayer's Exhibit 1. Pursuant to the Agreement, Petitioner agreed to provide the Omni Park Central Hotel (the "Hotel") located at 7th Avenue and 56th Street in New York City (the "City") with telephone service and a telephone system (collectively, the "System"). According to the Agreement, the System included the installation and use of telephone equipment (the "Telephone Equipment") and the maintenance, at no cost, of the Telephone Equipment. The Agreement provided that, "subject to limited exceptions" Petitioner would be the "sole provider of telephone service at the [Hotel] and that no other telephone or telecommunications business or entity shall provide telephone service at the [Hotel]."[4] Agreement, Article 3.

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[3]The ALJ's Findings of Fact although paraphrased and amplified in part, generally are adopted for purposes of this Decision except as noted below. Certain Findings of Fact not necessary to this Decision have not been restated and can be found in the ALJ Determination. Neither Party took exception to any of the ALJ's Findings of Fact.

[4]The Agreement specifically excluded "telephone systems installed and operated" by current or future lessees or concessionaires of the Hotel and coin operated or pay telephone equipment presently installed in the public areas of the Hotel. The Agreement also set up a procedure to be followed for the installation, operation and/or maintenance of other coin operated or pay telephone equipment in the public areas of the Hotel. Agreement, Article 3.

Petitioner agreed to act as the general contractor and facility manager for the System. Agreement, Article 3. Petitioner leased the Telephone Equipment from a third party.[5] According to the Agreement, the Lease for the Telephone Equipment was to provide that Petitioner had the option to purchase the Telephone Equipment from the third party at the expiration of the term of the Agreement. Pursuant to the Agreement, Petitioner assigned its rights under that option to the Hotel.

Michael Dalia[6] was employed by Petitioner from approximately 1979 to 1996 and was, for at least some of that time, Petitioner's Operations Manager. He testified that the telephone system was a "private branch exchange" ("PBX") system which recorded the individual guest's telephone calls. The PBX system "would record the digits that were dialed at the time of the call, the date of the call, duration of the call, [and] all of the ingredients that you needed to bill the call . . . ."[7] The PBX system sent that information to a call accounting system which would determine where the call was placed to, rate the call, and assign a charge to the call.[8] The call accounting system would then send that information to the Hotel's property management system. The Hotel's property management system "was the central system from which the [H]otel billed all transactions that occurred at the [H]otel."[9] Petitioner was responsible for the PBX and call accounting systems and the Hotel was responsible for the property management system.

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[5]We have modified the ALJ's Finding of Fact 8 to the extent that it stated that the Telephone Equipment was leased from an "unrelated" third party. Dominic A. Dalia, Petitioner's President, stated in his Declaration dated June 26, 1992 (the "Declaration of Dominic Dalia") and submitted in a Bankruptcy proceeding involving Park Centre (City's Exhibit B) that he is "President of [Petitioner] and the President of A.B.T.S. Investment Corp. which is the owner of the telephone equipment and provider of telephone services to the [Hotel]." Declaration of Dominic Dalia, ¶1.

[6]Michael Dalia is the son of Dominic A. Dalia.

[7]Tr. at 25.

[8]Tr at 26.

[9]Tr. at 27.

Article 5(a) of the Agreement states, in relevant part, that the "Hotel agrees to charge a billing rate for use of the System in amounts not less than those set forth in Exhibit D . . . and to bill its guests for use of the System in accordance therewith." Article 5(b) of the Agreement further provides, in relevant part, that "Hotel shall pay [Petitioner] the billings and charges set forth on Exhibit D . . . (the "Monthly Charges")." Exhibit D to the Agreement provides that :

> [Petitioner's] representative will present all telephone call charges and bills for each guest room and administration telephones to Hotel. Hotel shall pay to [Petitioner], subject to its right of offset as set forth in the [Agreement], all telephone call charges and billings for both guest rooms and administrative charges.[10]

The Hotel determined the "telephone system and service charges and billings" but, according to Exhibit D of the Agreement, such amounts could not be less than:

> (A) Guest Room Telephone Charges:
> Overseas (access charges) $.90/call
> Collect and Credit Card Calls $.90/call
>
> (B) Surcharges
> All Calls (excluding administrative calls) $.90/call
>
> (C) All guest room telephone calls will be billed at daytime operator assisted rates and prevailing local telephone company D.D.D. rates. In addition, Hotel shall collect from guests and, subject to its right to offset as set forth in the [Agreement], pay [Petitioner] an amount or amounts equal to any and all taxes or other charges, however designated levied or based upon such calls, or on the [Agreement], the System or the Telephone Equipment, including without limitation, all

[10]We disagree with that portion of the ALJ's Finding of Fact 10 stating that "[t]he Monthly Charges were amounts in addition to the costs of calls charged by unrelated carriers." Our review of the Agreement and Exhibit D in particular indicates that the Monthly Charges included "all telephone call charges and billings for both guest room and administrative charges" and was not an amount separate from "the costs of calls charged by unrelated carriers."

> federal, state, municipal and local privilege or excise taxes and/or amounts in lieu thereof paid or payable by [Petitioner] in respect of the foregoing, but not including any personal property taxes assessed on the Telephone Equipment or any taxes based on net income of [Petitioner]. All such taxes shall be included within the meaning of the term "Monthly Charges" . . . .
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> (D) Hotel will be allowed a 25% discount from the prevailing local telephone company direct dial rates for all administrative telephone calls.

Petitioner maintained the records of telephone call charges and bills for each guest room on the System and prepared a daily printout.

The Declaration of Dominic Dalia states that "the Monthly Charges (as defined by the [Agreement]) collected by the Hotel from its guests for telephone service were the sole and exclusive property of [Petitioner] subject to the limitations contained in [Article 6 of the Agreement, Amount Paid to Hotel]." Declaration of Dominic Dalia, ¶3. The Declaration of Dominic Dalia also states that "[i]t has been consistently required by [Petitioner] under each Telephone Service Agreement that the hotel acts as a collection agent of the Monthly Charges as defined in the [Telephone Service Agreement]." Declaration of Dominic Dalia, ¶4.

The Agreement provided that the Hotel would pay Petitioner "Monthly Charges" and Petitioner would pay the Hotel a "Concession Fee."[11]

The Concession Fee was an annual fee of $475,000 that Petitioner agreed to pay to the Hotel for rights granted under the Agreement. The Agreement provided that the Hotel could offset the amount of the Concession Fee against the Monthly Charges due to

[11]Pursuant to Article 6 of the Agreement, Petitioner would also have to make additional payments to the Hotel if either the Hotel increased the surcharges described in Exhibit D to the Agreement or the total Monthly Charges collected by the Hotel, without any offset, exceeded $1,400,000.

Petitioner. A review of the Record indicates that this was the manner by which the parties accounted for the Concession Fee.

Monthly invoices were prepared for the Hotel in the name of A.B.T.S. Investment Corporation with Petitioner shown as Billing Agent. The invoices in the Record reflect charges for (a) guests charges; (b) administrative charges; (c) advertising amounts; (d) collect call amounts; and (e) voice quoted call amounts. These amounts were reduced by (a) the Concession Fee and (b) disputed calls.

Ameritech Credit Corporation ("Ameritech") held a security interest in certain equipment used in the System.

Pursuant to Article 5(b) of the Agreement, the Hotel was required to deposit the amount due shown on a monthly invoice into a "lockbox" account at the Northern Trust Company (the "Bank") to be held and disbursed in accordance with a Deposit and Transfer Agreement for the benefit of Ameritech. Once Ameritech deducted the amount due on its promissory note, the balance was to be remitted to Petitioner from which it paid expenses including local and long distance charges and other related costs for the operation and maintenance of the System.[12]

Using Petitioner's books and records and copies of telephone invoices from unrelated carriers (e.g., New York Telephone, AT&T and MCI Communications) provided by Petitioner, the Department's Auditor calculated "Taxable Revenue" consisting of the Monthly Charges reduced by amounts for disputed calls, amounts charged to Petitioner by the unrelated carriers and an allowance for a 3 percent federal tax.[13]

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[12]Declaration of Dominic Dalia, ¶9.

[13]Tr. 77-78. Respondent offered no explanation as to why the "Taxable Revenue" was reduced by the charges from the carriers for local service. We assume the Department's Auditor excluded those amounts to avoid imposing UT more than once on those charges. "Taxable Revenue" was also reduced by carrier charges for long distance service, which is not subject to the UT.

The ALJ found that Petitioner was liable for UT on the gross operating income it received during the Tax Periods from the provision of telephone services to the Hotel but only to the extent that those services were attributable to local telephone calls. The ALJ found that the deficiency had to be modified to eliminate any amounts attributable to long-distance calls made before 1992 because the Department's change in policy regarding the taxability for UT purposes of surcharges attributable to long-distance calls could not be applied retroactively pursuant to the New York State Supreme Court, Appellate Division's decision in Hilton Hotels Corp. v. Commissioner of Finance of the City of New York, 219 A.D.2d 470 (1st Dept. 1995).[14]

On appeal, Petitioner takes exception to that part of the ALJ Determination that found it liable for the UT as a vendor of utility services. Petitioner asserts that the Hotel was responsible for the payment of the UT in question. Petitioner argues that, based upon Department Letter Ruling, FLR 034815-011 (July 21, 2004) (the "Letter Ruling") even if Petitioner was liable for UT as a vendor of utility services, it should be entitled to exclude from its gross operating income the amount of its sales of utility services for resale. Petitioner contends that it made sales of utility services for resale because it provided its services to an entity (the Hotel) that sold those services to the ultimate consumer (the Hotel guest). Petitioner also asserts that it neither received nor had any control over all of the amounts upon which the deficiency is based. Specifically, Petitioner argues that the amounts that the Hotel charged its guests that were retained by the Hotel and not remitted to Petitioner should be excluded from "Taxable Revenue" for purpose of the UT deficiency.

Respondent contends that the ALJ Determination should be affirmed because Petitioner is subject to the UT as a vendor of utility services. In addition, Respondent argues that the facts in the Letter Ruling relied on by Petitioner are quite different from the

[14]Respondent did not take exception to that portion of the ALJ Determination concluding that the deficiency should be adjusted to eliminate any taxable revenue attributable to long-distance calls made before 1992. Effectively, such adjustment eliminates all taxable revenue attributable to long distance calls from Petitioner's gross operating income for the Tax Periods. Thus, this Decision will not address taxable revenue attributable to long-distance calls for the Tax Periods.

facts in the matter before us. Respondent also contends that the UT was properly computed.

For the Tax Periods, §11-1101.7 of the New York City Administrative Code (the "Code") defined a "[v]endor of utility services" to include a corporation "not subject to the supervision of the department of public service who furnishes or sells . . . telephone . . . service." Section 11-1102 of the Code imposes an excise tax on the gross operating income of vendors of utility service. Gross operating income is defined in §11-1101.5 of the Code to include:

> 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.

In the case of a vendor that resells telephone services, gross operating income includes any mark-up or surcharge imposed by the vendor and collected from its customers (usually called surcharges) even though the Code does not specifically identify such income as gross operating income. The New York State gross receipts tax on providers of utility services rules specifically include surcharge income in gross operating income.[15] Because, the enabling act for City UT, General City Law §20-b, required that the City UT conform to Tax Law §186-a, the surcharge amounts are also includible for purposes of computing City gross operating income.

We find, as did the ALJ, that Petitioner is liable for UT as a vendor of utility services.

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[15] *See,* 20 NYCRR §46.3(d) (formerly NYCRR §502.3(d)) which includes in Tax Law Article 9 gross operating income "the excess above the charge of the telephone company" charged by a hotel providing telephone service to guests.

Pursuant to the Agreement, Petitioner is providing the Hotel with telephone service and a telephone system and serving as the general contractor and facility manager for both. The telephone service is being provided to both the Hotel's guests as well as its administrative offices. The Telephone Equipment was leased from an affiliate of Petitioner. The invoices from most of the third party providers, *i.e.*, MCI Communications and AT&T, were addressed to Petitioner.[16] City's Exhibit A at 27, 28, 29, 30.

The invoices to the Hotel set forth the Monthly Charges payable by the Hotel to Petitioner. The Monthly Charges are, by definition, all telephone call charges and bills for each guest room and administrative telephone calls. While Petitioner contends that the fact that the Hotel directly billed its guests and collected the amounts due should be controlling, the Declaration of Dominic Dalia states that the Monthly Charges "were the sole and exclusive property of [Petitioner]"[17] and that the Hotel acts as a "collection agent of the Monthly Charges."[18] After payments were made under the "lockbox" arrangement to the Bank, which paid Ameritech, the balance of the Monthly Charges were remitted to Petitioner.

Petitioner urges this Tribunal to reduce the amount subject to UT by the amount of the Concession Fee retained by the Hotel from the moneys collected by the Hotel. The auditor included as "Taxable Revenue" the amounts shown on the invoices as the Monthly Charges. All of those amounts (after offsetting the Concession Fee due the Hotel) were remitted to the "lockbox" for disbursement, first to Ameritech for the amount due on its promissary note, and then to Petitioner. The fact that the Monthly Charges remitted to the "lockbox" by the Hotel were reduced by the Concession Fee does not support Petitioner's contention that such amounts should be excluded from gross operating income which is

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[16]The copies of invoices from NY Telephone/NYNEX in the Record do not contain the name or address of the billing customer.

[17]Declaration of Dominic Dalia, ¶3.

[18]Declaration of Dominic Dalia, ¶4.

computed without reduction for any credits or expenses.[19] The fact that Petitioner has agreed to allow the Hotel to offset against the amount it is obligated to pay to Petitioner, an amount that Petitioner owes the Hotel does not change the fact that Petitioner must include the total amount of receipts (without regard to the offset) reflected on the invoices as the Monthly Charges in its gross operating income.

We disagree with Petitioner's contention that it provided services to an entity, the Hotel, that resold those services to the ultimate consumers, the Hotel's guests, and that Petitioner is therefore entitled to exclude from its gross operating income those sales for resale. At the outset, the Letter Ruling, cited by Petitioner was not addressed to Petitioner. Moreover the facts in the Letter Ruling are clearly different from the facts in the matter at bar. The taxpayer in the Letter Ruling sold telephone service to other resellers of that service. The taxpayer often did not know the identity of the ultimate end user of the service. In contrast, Petitioner was not selling telephone service to other resellers of that service. Rather Petitioner was clearly providing telephone service to the Hotel (administrative charges) and the Hotel's guests all of whom are the end users of that service. The fact that the Hotel collected charges from its guests does not change the fact that Petitioner was selling telephone services directly to the Hotel guests, and to the Hotel, in the case of administrative calls, as a concessionaire. Petitioner's President has clearly stated that the income was the property of Petitioner and the Hotel was merely serving as a collection agent. Under the facts of this case there was no sale of utility services to the Hotel for resale and thus Petitioner is not entitled to reduce its gross operating income by receipts for sales of telephone service for resale.[20]

Penalties for "Delinquency" and "Negligence" (including the 50% of interest due to negligence) are included in the deficiency. Exhibit D to the Agreement states that the Hotel was obligated to collect from the guests and remit to Petitioner amounts equal to all taxes

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[19]Section 11-1101.5 of the Code. *See supra* n.13.

[20]We have considered all other arguments raised by the Parties and deem them unpersuasive.

or other charges, including local excise taxes, and that such taxes are included within the definition of Monthly Charges. This explicit language regarding the collection of taxes by the Hotel and the payment of such taxes to Petitioner indicates that the collection and payment of taxes, although the UT was not expressly addressed, was contemplated by the Agreement and that as between Petitioner and the Hotel, Petitioner apparently undertook responsibility for remitting any collected taxes to the appropriate taxing authority. Therefore, Petitioner is unable to show that its failure to file a UT return is due to "reasonable cause and not willful neglect" and that its underpayment of tax is not due to negligence.

Accordingly, the ALJ's Determination is affirmed.

Dated: April 12, 2007
New York, New York

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GLENN NEWMAN
President and Commissioner

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ELLEN E. HOFFMAN
Commissioner