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

TSB-A-95 (12) C
Corporation Tax
July 28, 1995

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. C950316A

On March 16, 1995, a Petition for Advisory Opinion was received from Nixon, Hargrave, Devans & Doyle, Clinton Square, P.O. Box 1051, Rochester, New York 14603.

The issue raised by Petitioner, Nixon, Hargrave, Devans & Doyle, is whether a New York corporation which is a natural gas broker that never owns the natural gas is subject to tax under Article 9-A or under section 186 of Article 9 of the Tax Law and under section 186-a of Article 9 of the Tax Law.

The New York corporation (the "Corporation") is engaged in the business of natural gas brokering. The Corporation facilitates the transfer of natural gas from in-state and out-of-state producers of natural gas to end-users of the natural gas.

Approximately 30% of the Corporation's business is with in-state producers. The Corporation facilitates the transfer and sale of gas from an in-state producer to an end-user without ever taking title to the gas, without having possession or control of the gas, and without bearing any risk of loss with respect to the gas. The gas is transported from the producer to the end-user on a pipeline system owned by a large New York utility (the "Utility"). Petitioner states that the utility does not allow the Corporation to own gas on its system. Title to the gas is transferred directly from the producer to the end-user, and the Corporation serves merely as a broker.

In a typical transaction, the Corporation locates an end-user and determines its need for gas. The Corporation then matches this need with a producer's ability to provide the gas. The gas is then transferred from the producer to the end-user via the Utility's system. The Corporation never owns any of the gas.

Approximately 70% of the Corporation's business is with out-of-state producers. As with the in-state producers, the gas is transferred from the producer to the end-user, and the Corporation never takes title to the gas, has possession or control of the gas, or bears any risk of loss with respect to the gas. In addition, title transfers from the out-of-state producer to the end-user outside New York. Petitioner states that the end-users are liable for the gas importer tax under section 189 of the Tax Law which the end-users pay to the Utility which then remits the tax to New York State.

With both in-state and out-of-state gas, the Corporation receives a commission from the end-user as compensation for its services, which amount is set by the producer. On behalf of the producers, and for the convenience of both producers and end-users, the Corporation bills end-users for the amount of gas purchased by the end-users from the producers. The end-users remit payments

to the Corporation which then deposits such payments in a separate noninterest-bearing bank account set up solely for the deposit of amounts received from end-users. The Corporation forwards the sale proceeds to the producer and then withdraws its commission from the account for its own use.

The Corporation uses two separate brokerage agreements in doing business with its customers: one is entitled "Gas Brokerage Agreement with Seller" and is used to enter into agreements with the producers of gas; and the other is entitled "Gas Brokerage Agreement with Buyer" and is used to enter into agreements with end-users of the gas. Each of these agreements states that the Corporation is acting as a broker, and that the Corporation itself is not involved in buying or selling natural gas. Both of the agreements also clearly state that the Corporation never takes title to the gas, is never in possession or control of the gas, and never bears any risk of loss with respect to the gas. In both the in-state and out-of-state situations described above, a new end-user located by the Corporation must, in writing, indicate to the Utility that the Corporation is acting as its agent. For Federal income tax purposes, the Corporation reports only its commissions as income. It does not report the remaining gross receipts received from end-users.

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 a corporation liable to tax under section 186 of Article 9 of the Tax Law is not subject to tax under Article 9-A of the Law.

Section 186 of the Tax Law imposes a franchise tax on a corporation, joint stock company or association "formed for or principally engaged in the business of supplying ... gas, when delivered through mains or pipes" The tax is imposed for the privilege of exercising its corporate franchise or carrying on its business in such corporate or organized capacity in New York State and is based, in part, upon gross earnings from all sources within New York State.

Section 186-a of the Tax Law imposes a tax on the furnishing of utility services. The tax is imposed on a utility which is not subject to the supervision of the New York State Department of Public Service, if it "sells gas ... delivered through mains [or] pipes ... regardless of whether such activities are the main business of such person or are only incidental thereto " The tax imposed under section 186-a of the Tax Law is imposed in addition to the franchise tax imposed under Article 9-A or under section 186 of Article 9 of the Tax Law.

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 purposes for which the corporation was organized. See, McAllister Bros., Inc., v Bates, 272 App Div 511, 517.

The determination of whether the Corporation is subject to tax under Article 9-A or section 186 of Article 9, depends on what activity the Corporation is principally engaged in. Ordinarily, a corporation is deemed to be principally engaged in the activity from which more

than 50% of its receipts are derived. See, e.g. Re Joseph Bucciero Contracting Inc., Adv Op St Tax Comm, July 23, 1981, TSB-A-81(5)C.

In Boundary Gas, Inc., Adv Op St Tax Comm, April 9, 1981, TSB-H-81(24)C, the Tax Commission determined that boundary was not engaged in.the business of supplying gas (and, thus, was not subject to tax under section 186 of the Tax Law) because (1) Boundary had no connection with the gas being sold other than holding bare legal title thereto for an instant of time; (2) Boundary did not take physical possession or have any control or supervision of the gas; (3) Boundary did not own or operate any facilities of any nature whatsoever and was prohibited by its certificate of incorporation from either owning or constructing any facility; (4) Boundary was prohibited by its certificate of incorporation from selling gas to any entity which was not a shareholder of Boundary; and (5) all expenses of Boundary were reimbursed dollar for dollar by shareholders.

Herein, the Corporation (1) never takes title to the gas; (2) never has possession or control of the gas; (3) never bears any risk of loss with respect to the gas; (4) indicates in its brokerage agreements that it is acting as a broker and it does not engage in the business of selling or buying gas; (5) only includes its commission in its gross income on its Federal income tax returns; and (6) has a separate account into which it deposits payments it receives from end-users, and only retains its commissions.

Accordingly, the Corporation would not be engaged in the business of supplying gas through mains or pipes. Therefore, the Corporation would not be subject to tax under section 186 or section 186-a of Article 9 of the Tax Law. The Corporation would be taxable under Article 9-A of the Tax Law.

DATED: July 28, 1995

s/PAUL B. COBURN
Deputy Director
Taxpayer Services Division

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