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

TSB-A-96 (85) S
Sales Tax
TSB-A-96 (28) C
Corporation Tax
December 26, 1996

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. Z960404C

On April 4, 1996, a Petition for Advisory Opinion was received from Cullen and Dykman, 177 Montague Street, Brooklyn, New York 11201.

The issue raised by Petitioner, Cullen and Dykman, is whether any portion of the revenues derived from the natural gas transactions described in each of the scenarios set forth below is subject to tax under (1) sections 186, 186-a or 189 of Article 9 of the Tax Law, (2) Article 9-A of the Tax Law, and (3) Articles 28 and 29 of the Tax Law.

Petitioner submits the following facts as the basis for this Advisory Opinion. The petition presents various scenarios involving the distribution of natural gas. An advisory opinion addresses the particular set of facts raised by the petitioner (Tax Law, §171, subd Twenty-fourth, 20 NYCRR 2376.1[b]) and it is presumed for purposes of the opinion that the described transactions comply with, and are treated consistently for purposes of, applicable tariffs and contractual agreements among the parties as well as Federal and State (including other States) regulatory and tax requirements.

Scenario 1: An unregulated gas marketing company ("Marketer") is incorporated and headquartered in a state other than New York. Marketer does not maintain an office in New York. However, it solicits business in New York by mail and telephone, and its salesmen periodically visit New York to solicit business. More than 50 percent of Marketer's receipts are derived from sales of natural gas to end-users, including sales to end-users located in New York.

Marketer's transactions with its New York customers are typically structured as follows: Marketer procures and takes title to natural gas from a producer or other supplier outside New York and, in turn, sells the commodity to a New York end-user for ultimate consumption in New York. The gas sales agreement ("Agreement") between Marketer and the end-user provides that the gas will be sold to the end-user at a location outside New York (i) where the quantity of gas sold will be measured, (ii) where the end-user will take title to, and possession of the gas, and (iii) where the end-user will assume the risk of loss respecting the gas; i.e., all indicia of ownership transfer to the end-user outside New York.

Pursuant to other provisions of the Agreement, the New York end-user designates Marketer as the end-user's agent for arranging and administering transportation of the customer-owned gas (i) via interstate pipeline from the out-of-state point of sale to the point of interconnection ("city-gate") with a local distribution company ("LDC") and (ii) via the LDC from the city-gate to the burner-tip. The Agreement will expressly designate Marketer as the end-user's agent for arranging and administering delivery of the gas, and Marketer will hold itself out to the interstate pipeline and the LDC as the end-user's agent. To the extent permitted by the pipeline and LDC tariffs, Marketer will enter into

both interstate and local transportation contracts as agent for the end-user. The end-user will be a principal party to, and have independent rights under, the transportation contracts with both the interstate pipeline and the LDC. Aside from its agency functions, Marketer will have no contractual obligation to the end-user, the interstate pipeline, or the LDC under either of the transportation agreements. Marketer will not own, lease or operate facilities for the transportation of natural gas.

Marketer's Agreement with the New York end-user will impose separate charges for (i) sale of the gas commodity and (ii) the service of acting as the end-user's agent for arranging and administering interstate and local transportation services via interstate pipeline and LDC respectively. The end-user is liable directly to the interstate pipeline and LDC for transportation fees. However, the Marketer, as agent, may collect such fees from the end-user and remit those fees to the transportation companies, acting merely as a conduit.

Scenario 2: Assume the same facts as in Scenario "1", except that, Marketer will charge a single fee for (i) the sale of the gas commodity and (ii) the service of arranging and administering, as the customer's agent, interstate and local transportation of the gas.

Scenario 3: Assume the same facts as in Scenario "1" with the following variations. Marketer is a foreign corporation authorized to do business in New York, as well as other states, and has an office and salespersons in New York. Marketer's customers include both New York and out-of-state end-users. Marketer sells gas to New York end-users in transactions where physical delivery and transfer of title and all incidents of ownership occur in New York. Marketer also sells gas to New York end-users at points outside New York, (as described in Scenario "1"), where title, possession, risk of loss and all other indicia of ownership transfer from Marketer to the end-user. As in Scenario "1", Marketer does not own, lease, or operate facilities for the delivery of gas. When Marketer sells gas to New York end-users at points outside New York, it also arranges and administers, as the end-user's agent, transportation of the customer-owned gas (i) via interstate pipeline to the city-gate and (ii) via LDC from the city-gate to the burner-tip.

Articles 9 and 9-A of the Tax Law

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 for tax under sections 183 through 186 of Article 9 of the Tax Law is not subject to tax under Article 9-A of the Tax Law.

Section 186 of the Tax Law imposes a tax on "[e]very 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 a corporate or organized capacity in New York State and is based, in part, upon gross earnings from all sources within New York State. The term "gross earnings" as used in this section means all receipts from the employment of capital without any deduction.

To determine the classification and proper taxability of a corporation under either Article 9 or Article 9-A of the Tax Law, an examination of the nature of the corporation's activities is necessary, regardless of the purpose for which the corporation was organized. See, Matter of McAllister Bros. v Bates, 272 AD 511, 517. Ordinarily, a corporation is deemed to be principally engaged in the activity from which more than 50 percent 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 this case, Petitioner states that more than 50 percent of Marketer's receipts are derived from sales of natural gas to end-users. Accordingly, when Marketer carries on business in New York State, Marketer would be classified as a corporation subject to the franchise tax imposed under section 186 of Article 9 of the Tax Law and would not be subject to franchise tax under Article 9-A of the Tax Law. Marketer's tax would be based, in part, on its gross earnings from all sources within New York State.

Section 186-a of the Tax Law provides, in part:

> 1. Notwithstanding any other provision of this chapter, or of any other law, a tax equal to three and one-half per centum of its gross income is hereby imposed upon every utility doing business in this state which is subject to the supervision of the state department of public service [utility of the first class] ... and a tax equal to three and one-half per centum of its gross operating income upon every other utility [utility of the second class] doing business in this state ... which taxes shall be in addition to any and all other taxes and fees imposed by any other provision of law for the same period.
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> 2. As used in this section, (a)(i) the word "utility" includes ... every person (whether or not such person is subject to [the department of public service] supervision) who sells gas ... delivered through mains [or] pipes ... or furnishes gas ... by means of mains [or] pipes ... regardless of whether such activities are the main business of such person or are only incidental thereto ... (b) the word "person" means ... corporations ... (d) the words "gross operating income" mean and include receipts received in or by reason of any sale, conditional or otherwise, made for ultimate consumption or use by the purchaser of gas ... or in or by reason of the furnishing for such consumption or use of gas ... service in this state ... without any deduction ....

In this case, Marketer is not subject to the supervision of the Department of Public Service.

Therefore, when Marketer does business in New York State, Marketer would be subject to tax under section 186-a of the Tax Law as a utility of the second class. Marketer's tax would be based on its gross operating income and would include receipts received from the sale in New York State of natural gas to end-users for ultimate consumption or use by the end-user in New York State.

Section 189.2 of the Tax Law imposes, on every gas importer, a monthly privilege tax equal to four and one-quarter percent of the consideration given or contracted to be given by the gas importer for the gas services imported or caused to be imported into New York State by the gas importer for its own use or consumption in New York State.

Section 189.1 of the Tax Law provides as follows:

(a) The term "gas services" means gas delivered through mains or pipes.

(b) The term "gas importer" means every person who imports or causes to be imported into this state services which have been purchased outside the state for its own use or consumption in this state, provided such term does not include a public utility subject to the jurisdiction of the public service commission as to the matter of rates on sales to customers.

(c) The term "person" includes an individual, partnership, society, association, joint stock company, corporation ....

In this case, it appears that Marketer is not importing gas services into New York State for its own use or consumption in New York State. Therefore, Marketer would not be subject to the tax imposed under section 189 of the Tax Law. However, where Marketer sells natural gas to end-users outside of New York state, and the end-user imports gas services or causes gas services to be imported into New York State for its own use or consumption in New York State, the end-user may be subject to the tax imposed under section 189 of the Tax Law.

The Department of Taxation and Finance has issued several advisory opinions regarding the taxability of the receipts from the sale of natural gas by marketers to New York State end-users.

In Mark S, Klein, Adv Op Comm T & F, April 29, 1991, TSB-A-91(11)C, a foreign corporation is principally engaged in the business of supplying natural gas to end-users. The foreign corporation's requirements contracts with its suppliers provide that the delivery point of the natural gas is the point of sale. At the point of sale, both legal possession and title passes to the foreign corporation and that same point of sale is the point the end-user takes possession and title. The Advisory Opinion holds that the foreign corporation is subject to tax under section 186 of the Tax Law on its gross earnings from the sale of natural gas where the point of sale is located within New York State. However, if the foreign corporation sells natural gas to an end-user where the

point of sale is in Louisiana, the gross earnings from such sale are not form a source in New York State. The end-user's subsequent contract with a pipeline company to transport the purchased natural gas to its destination, even if such destination is in New York State, is not relevant in determining the taxability of the foreign corporation selling the natural gas outside New York State.

In Niagara Mohawk Power Corporation, Adv Op Comm T & F, April 20, 1995, TSB-A-95(8)C, one of the issues raised was whether a marketer's receipt from the sale of natural gas to a consumer is taxable under sections 186, 186-a and 189 of the Tax Law under five scenarios. The Advisory Opinion holds that the determination of where the marketer's sale of natural gas occurs in each of the scenarios is a factual matter not susceptible of determination in an advisory opinion. However, the opinion discusses each scenario to aid in making a determination for purposes of sections 186, 186-a and 189 of the Tax Law. The situations in scenarios three, four and five are similar to the facts in this case. In scenario three of the Niagara Mohawk advisory opinion, marketer acquires gas outside New York State. Marketer transfers title to the consumer at a point outside New York State. However, the contract price includes the cost of shipping the gas to the city-gate in New York. Risk of loss transfers from marketer to the consumer at the city-gate. The marketer has a separate transportation contract with an interstate pipeline company to transport the gas to the city-gate. The consumer has no independent control over, or rights to service under, the transportation contract. With respect to scenario three, the opinion provides that the facts are conflicting because title transfers outside New York State but delivery, risk of loss, control, etc. indicate a sale within New York State. Therefore, pending more specific information regarding the proposed transactions and the relationships of the parties and their past dealings, the situs of the sale will be presumptively placed in New York State.

In scenario four of the Niagara Mohawk, supra, advisory opinion, marketer acquires gas outside New York State. Marketer transfers title to the consumer at a point outside New York State, and the contract price includes the cost of shipping the gas to the title transfer point. Risk of loss transfers to consumer at the title transfer point. In a separate transaction, marketer transfers its transportation rights with the interstate pipeline that are sufficient to permit the consumer to transport all the gas purchased from the title transfer point to the city-gate in New York. The consumer pays marketer directly for the gas commodity and pays the interstate pipeline company for the transportation service. The pipeline company then credits marketer's account for the amount paid by the consumer. With respect to scenario four, the opinion provides that absent any other information, it appears that transfer of title and possession occur outside of New York State, and the sale for New York State tax purposes occurs outside New York State.

In scenario five of the Niagara Mohawk, supra, advisory opinion, marketer acquires gas outside New York State. The marketer transfers title to the consumer at a point outside New York, and the contract price includes the cost of shipping the gas to the title transfer point. Risk of loss transfers from the marketer to the consumer at the title transfer point. Interstate transportation of the gas into New York is accomplished under a contract directly between the

interstate pipeline and the consumer. The marketer has no control over, or rights to service under, the transportation contract. With respect to scenario five, the opinion provides that absent any other information, it appears that transfer of title and transfer of possession occurs outside of New York State and that the sale occurs outside New York State for New York State tax purposes.

In Christopher L. Doyle. Esq., Adv Op Comm T & F, May 8, 1996, TSB-A-96(13)C and TSB-A-96(29)S, the issues raised were whether a marketer's receipts from the sales of natural gas to New York end-users pursuant to a specific sales agreement were taxable under sections 186 and 186-a of Article 9 and Articles 28 and 29 of the Tax Law, and whether the end-users were subject to the tax imposed under section 189 of the Tax Law. The advisory opinion, citing Mohawk, supra, holds that the determination of where the sale of natural gas occurs is a factual matter not susceptible of determination in an advisory opinion. However, the opinion provides that it appears that under the terms of the agreement described, title, risk of loss and transportation responsibility for the gas will pass from the marketer to the New York end-user at sales points outside New York State. Under the agreement, the end-user may appoint the marketer as the end-user's agent to arrange for transportation and delivery of the gas from the sales points outside New York State to the downstream transportation nomination point designated by the end-user. Marketer's fee for acting as the end-user's agent is included in the sales price of the natural gas sold to the end-user. The opinion provides that like Mark S Klein, supra, and Niagara Mohawk, supra, it appears that the sale of the natural gas for New York State tax purposes occurs outside New York State. Additionally, when the marketer acts as the end-user's agent to arrange for the delivery and transportation of the natural gas to a transportation nomination point in New York pursuant to the agreement, the sale of the natural gas for New York State tax purposes may occur within New York State. For instance, the sale may occur in New York State if the activities of the marketer while acting as agent for an end-user are not conducted at arms-length or if the cost of the transportation services arranged by the marketer is not at unrelated third-party prices consistent with the industry.

As stated in Niagara Mohawk, supra, and Christopher L. Doyle, supra, the determination of where the sale of natural gas occurs for purposes of sections 186, 186-a and 189 of the Tax Law is a factual matter not susceptible of determination in an advisory opinion. An advisory opinion merely sets forth the applicability of pertinent statutory and regulatory provisions to a "a specified set of facts." Tax Law, §l71.Twenty-fourth; 20 NYCRR 2376.1(a).

Accordingly, it is not within the scope of this advisory opinion to determine whether any portion of the revenues derived from sale of the natural gas in the transactions described in Scenarios "1", "2" and "3" above are (i) includible in Marketer's "gross earnings" from the sale of natural gas within New York State under section 186 of the Tax Law or "gross operating income" from the sale of natural gas delivered into New York State through mains or pipes for ultimate use or consumption by the end-user under section 186-a of the Tax Law, (ii) from importing gas services or causing gas services to be imported into New York State by the end-user for its own use or consumption in New

York State under section 189 of the Tax Law or (iii) are subject to sales tax under Articles 28 and 29 of the Tax Law (see, Articles 28 and 29 of the Tax Law, infra).

However, it appears that in this case, under Scenario "1", title, risk of loss and transportation responsibility for the gas will pass from Marketer to the New York end-user at locations outside New York State. Like Mark S. Klein, supra, Niagara Mohawk, supra and Christopher L. Doyle, supra, it appears that the sale of this natural gas for New York State tax purposes occurs outside New York State. Like Christopher L. Doyle, supra, where Marketer acts as the end-user's agent to arrange for the delivery and transportation of the natural gas to a burner-tip in New York State, the sale of such natural gas for New York State tax purposes may occur within New York State. This would occur if the activities of Marketer while acting as agent for an end-user are not conducted at arms-length or if the cost of such transportation services arranged by Marketer is not at unrelated third-party prices consistent with the industry. Where the sale of the natural gas occurs outside New York State, the Marketer's receipt from the sale of the gas is not included in gross earnings from sources within New York State under section 186 of the Tax Law, or in gross operating income under section 186-a of the Tax Law. Marketer's services of acting as the end-user's agent in making the transportation arrangements are incidental to the sale of the natural gas. Therefore, where the sale of the natural gas occurs outside New York State, Marketer's receipts for acting as agent in arranging the transportation services are not included in gross earnings from sources within New York State under section 186 of the Tax Law or in gross operating income under section 186-a of the Tax Law. Where Marketer, as agent of the end-user, collects the transportation fees from the end-user and remits those fees to the transportation companies, Marketer is acting merely as a conduit and those fees are not receipts of Marketer for purposes of section 186 and 186-a of the Tax Law. (See, Consolidated Edison Company of New York, Adv Op St Tax Comm, December 1, 1986, TSB-A-86(22)C.) Where the sale of the natural gas to the end-user occurs outside New York State, and the end-user imports gas service into New York State for its own use or consumption, the end-user may be subject to the tax imposed under section 189 of the Tax Law.

Scenario "2" is similar to Scenario "1" except that Marketer charges a single fee for both the sale of the gas and the service of acting as agent for the transportation of the gas to the burner-tip. This is similar to L. Doyle, supra, in that the fee for acting as agent for the end-user is included in the sales price of the natural gas to the end-user. Therefore, the taxability of the receipts from the sale of natural gas to the end-user, is the same as described in the previous paragraph relating to Scenario "1".

Under Scenario "3", Marketer sells gas to end-users at points in New York State where all indicia of ownership transfer from Marketer to the end-user, and at points outside New York State where all indicia of ownership transfer from Marketer to the end-user. In all cases, Marketer acts as an agent for the end-user for the transportation of the gas from the sales point to the burner-tip. Where the sale occurs outside of New York State, the taxability of the receipt from the sale of natural gas to the end-user and the receipt for making the transportation arrangements, as the end-user's

agent, are the same as described above relating to Scenario "1". Where the sale of the natural gas occurs in New York State, the receipt from the sale of the natural gas to the end-user and the receipt for making the transportation arrangements, as the end-user's agent, are included in gross earnings from sources within New York State under section 186 of the Tax Law. Where the sale of the natural gas occurs in New York State, the receipt from the sale of the natural gas to the end-user is included in gross operating income under section 186-a of the Tax Law. However, as a utility of the second class, Marketer's receipts for making the transportation arrangements are not includible in gross operating income under section 186-a of the Tax Law. Where Marketer, as agent of the end-user, collects transportation fees from the end-user and remits those fees to the transportation companies Marketer is acting merely as a conduit and those fees are not receipts of Marketer for purposes of section 186 and 186-a of the Tax Law. (See, Consolidated Edison, supra.)

Articles 28 and 29 of the Tax Law

Section 1105(b) of the Tax Law imposes sales tax, in part, on "[t]he receipts from every sale, other than sales for resale, of gas ... and gas ... service of whatever nature ...." Except for purposes of this tax, gas is not defined in the Tax Law as tangible personal property for purposes of the sales and compensating use taxes. Moreover, section 1110 of the Tax Law does not incorporate by reference or contain any language similar to that contained in section 1105(b). (See, Penn York Energy Corporation, Dec Tax App Trib, October 1, 1992, TSB-D-92(71)S and Christopher L. Doyle. Esq., supra.) Accordingly, except for the tax imposed by section l105(b) of the Tax Law, the sale or use of gas in New York State is not subject to the sales tax imposed under section 1105 or the compensating use tax imposed under section 1110 of the Tax Law.

In general, the sales tax is a destination tax. That is, the location at which the sale takes place determines both the incidence of tax and the rate at which the tax is imposed (see, 20 NYCRR 525.5).

As noted, the determination of where the sale of natural gas occurs is a factual matter not susceptible of determination in an advisory opinion. Under Scenarios "1" and "2" (and, in part, Scenario "3"), however, where it appears that the indicia of ownership of the gas transfer from Marketer to the end-user outside of New York State, no sale or use of tangible personal property occurs in the State and neither the receipt from the sale of the natural gas by Marketer nor the use of the gas by the end-user is subject to the State and local sales or compensating use taxes imposed by and pursuant to the authority of Articles 28 and 29 of the Tax Law. (As noted, the sale may occur in New York State if the activities of Marketer while acting as agent for an end-user are not conducted at arms-length or if the cost of the transportation services arranged by Marketer is not at unrelated third-party prices consistent with the industry.) In addition, if the sale occurs outside of New York State, the fee for the service of arranging and administering the transportation of the gas as an agent for the end-user is not includable in any taxable "receipt" or "consideration given," and the service itself is not included among the enumerated services subject to sales or compensating use

taxes. Thus, this fee is not subject to tax regardless of whether Marketer charges separate fees for the sale of the gas and this service or charges a single fee.

However, under Scenario "3" where it appears that the indicia of ownership of the natural gas transfer from Marketer to the end-users in New York State, the entire receipt from the sale of the gas commodity including the fee for the service of arranging and administering the transportation of the gas as an agent for the end-user is subject to the State tax imposed under section 1105(b) of the Tax Law and any State and local taxes imposed within the jurisdiction where the delivery of the commodity takes place. For sales tax purposes, the subject fee is a charge for shipping or delivery of the natural gas and falls within the statutory definition of "receipt."

Section l101(b)(3) of the Tax Law defines "receipt," in part, as follows:

> The amount of the sale price of any property and the charge for any service taxable under this article, valued in money, whether received in money or otherwise, including any amount for which credit is allowed by the vendor to the purchaser, without any deduction for expenses or early payment discounts and also including any charges by the vendor to the purchaser for shipping or delivery regardless of whether such charges are separately stated in the written contract, if any. or on the bill rendered to such purchaser and regardless of whether such shipping or delivery is provided by such vendor or a third party, but excluding any credit for tangible personal property accepted in part payment and intended for resale .... (emphasis supplied)

It is noted that the State and local taxes imposed on receipts from the sale of gas and gas services by Article 28 and pursuant to the authority of Article 29 of the Tax Law are also influenced by the purpose for which the gas is purchased by the end-user. Although beyond the scope of the scenarios presented by Petitioner, gas and gas service may be exempt from sales tax if used for residential purposes, used in research and development, or used in production. (See, sections 1105-A, 1115(b)(ii) and 1115(c) of the Tax Law.)

/s/

DATED: December 26, 1996

John W. Bartlett
Deputy Director
Technical Services Bureau

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