

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-02(5)S
Sales Tax
April 3, 2002

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S001013A

On, October 13, 2000, the Department of Taxation and Finance received a Petition for Advisory Opinion from KPMG LLP, 345 Park Avenue, New York, New York, 10154.

The issue(s) raised by Petitioner, KPMG LLP, are whether the purchase of "bandwidth" by its client, XYZ, a Delaware corporation, constitutes the purchase of interstate or international telephony service and is therefore exempt from the imposition of New York State sales tax.

Petitioner submits the following facts as the basis for this Advisory Opinion.

XYZ, a Delaware corporation with its principal place of business located in New York State, is a worldwide network of properties and services with a core mission to help customers find and communicate with people of similar interests. XYZ operates its business principally through its proprietary Web site, www.XYZ.com. End-users visit XYZ's Web site via the Internet. XYZ's servers and data processing systems are primarily hosted at a third party provider's facilities located in New York State. XYZ's Web site contains content that is not geographic specific. Over 40% of the telecommunications traffic that visits XYZ's Web site originates without the United States. Of the approximately 60% of telecommunications traffic that originates within the United States, about one-half comes from AOL's servers located in Virginia. The remainder of the domestic traffic comes from users located throughout the United States. Therefore, only a very small percentage of telecommunications traffic that visits XYZ's Web site originates in New York State.

To enable end-users to utilize its Web site, XYZ's servers are connected to the Internet through links or circuits provided by telecommunications service providers. To handle the quantity of telecommunications traffic that visits XYZ's Web site, XYZ purchases "bandwidth". "Bandwidth" essentially represents the volume of telecommunications traffic that a circuit can carry at any given time, and is critical to a company that hosts Web sites, because insufficient bandwidth means that users encounter delays or "down times" when attempting to visit the Web site. Generally speaking, bandwidth is directly proportional to the amount of data transmitted or received per unit time. In digital systems, bandwidth is expressed as data speed in bits per second (bps). In a qualitative sense, bandwidth is proportional to the complexity of the data for a given level of system performance. For example, it takes more bandwidth to download a photograph in one second than it takes to download a page of text in one second. Large sound files, computer programs, and animated videos require still more bandwidth for acceptable system performance. Virtual reality and full-length three-dimensional audio/visual presentations require the most bandwidth of all. In digital cable and fiber optic systems, there is an ever-increasing demand for higher data speeds. In

hard-wired systems, available bandwidth can literally be constructed without limit by installing more and more cables.

XYZ is charged a monthly fee based upon the amount of bandwidth purchased. Due to the nature of the service provided, charges are not itemized on XYZ's monthly invoice by the state where XYZ's Web site traffic originates. Rather, the monthly fee covers all "bandwidth" purchases.

Applicable Law and Regulations

Section 1105 of Article 28 of the Tax Law provides, in part:

Imposition of sales tax. On and after June first, nineteen hundred seventy-one, there is hereby imposed and there shall be paid a tax of four percent upon:

(a) The receipts from every retail sale of tangible personal property, except as otherwise provided in this article.

(b)(1) The receipts from every sale, other than sales for resale, of the following:

(A) gas, electricity, refrigeration and steam, and gas, electric, refrigeration and steam service of whatever nature; (B) telephony and telegraphy and telephone and telegraph service of whatever nature except interstate and international telephony and telegraphy and telephone and telegraph service;

Section 527.2 of the Sales and Use Tax Regulations provides, in part:

Sale of utility and similar services. (Tax Law, Section 1105(b)) (a) Imposition.

(1) Section 1105(b) of the Tax Law imposes a tax on the receipts from every sale, except a sale for resale or a sale specifically exempt under section 1115(b) (i) and (ii), (c) or (e) of the Tax Law, of

* * *

(ii) telephony and telegraphy and telephone and telegraph service of whatever nature, except interstate and international telephony and telegraphy and telephone and telegraph service.

(2) Although this tax is generally known as the "consumer's utility tax," the intention of the statute is to tax the enumerated sales and services whether or not rendered by a company subject to regulation as a utility company. The words "of whatever nature" indicate that a broad construction is to be given the terms describing the items taxed. The inclusion of the word "service" indicates an intent to tax, under this provision, items that are furnished as a continuous supply while the vendor-vendee relationship exists.

(3) A charge for installing equipment, such as transmission equipment, which a gas, electric, or telephone or telegraph company makes, according to a tariff, to a real property developer is deemed to be a charge for gas, electric, telephone or telegraph service. The charge may be for reimbursement of the company's cost of doing the work itself, or for the cost the company incurred in having a contractor perform the work.

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(d) Telephony and telegraphy; telephone and telegraph service.

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(2) The term telephony and telegraphy includes use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals.

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Example 3: Message switching services, transmitted to a computer over lines leased from a communication carrier are telegraph services subject to the tax imposed under section 1105(b) of the Tax Law.

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(5) The tax on utility services applies to every charge for any telephone and telegraph service. Among these charges are monthly message rate and intrastate toll charges and charges for special services, such as installation, change of location, conference connections, tie-lines, WATS lines and the furnishing of equipment.

Example 7: A telephone company installs station apparatus, owned by it, on the premises of a customer. The installation is a service taxable under section 1105(b) of the Tax Law.

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Opinion

Petitioner's client, XYZ, purchases "bandwidth" from various providers in order to be able to provide potential users with access to its Web site. In Commonwealth Long Distance, Inc., Adv Op Comm T&F, July 29, 1994, TSB-A-4(33)S, the petitioner paid a local or interexchange carrier for leased lines. The leased lines were considered to be a taxable purchase of an intrastate telephone service from the local or interexchange carrier. The purchases of bandwidth by XYZ from a telecommunications carrier for XYZ's Web site are similar to the purchase or lease of phone lines by persons providing information or services via "1-800" numbers. XYZ's purchases of bandwidth, therefore, are purchases of intrastate telephone service.

The bandwidth service purchased by XYZ is not interstate or international in nature. XYZ's bandwidth purchases are a distinct transaction from the purchases by XYZ's customers or their Internet access providers of telecommunications services linking XYZ's customers to XYZ's servers in New York State. The international, interstate and intrastate telephony and telegraphy services which may be involved in transmitting XYZ's customers' communications to and from XYZ's Web site are not purchased by XYZ. Rather XYZ merely purchases sufficient bandwidth to ensure that the customers' communications may be connected with XYZ's Web site servers. This sale to XYZ of incoming circuit capacity is similar to a leased telephone line service, and is a telephone, telegraph, telephony and telegraphy service which is delivered to and consumed by XYZ at its New York State location. The billing for this service does not distinguish between transmittals that are intrastate, interstate, or international in origin. This service only ensures that the bandwidth capacity of the circuits connected to XYZ's Web site is sufficient to handle the incoming volume. As such, this service is local or intrastate in nature and operation.

In the instant case, XYZ is not selling telephony and telegraphy or telephone and telegraph service to its customers. Its customers are merely accessing information contained on XYZ's Web site. Accordingly, XYZ's purchases of bandwidth are not purchases for resale. XYZ's purchases of bandwidth are, therefore, subject to the state and local sales taxes imposed on intrastate telephone service.

DATED: April 3, 2002

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