

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

TSB-A-03(37)S
Sales Tax
September 3, 2003

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S030319B

On March 19, 2003, the Department of Taxation and Finance received a Petition for Advisory Opinion from Bway.net, Inc., 459 Broadway, 2nd Floor, New York, New York, 10013. Petitioner, Bway.net, Inc., provided additional information pertaining to the Petition on April 17, 2003, July 14, 2003, and July 30, 2003.

The issue raised by Petitioner is whether its purchases from a telecommunication provider of Digital Subscriber Lines which Petitioner uses to provide Internet service to its customers are subject to sales tax.

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

Petitioner is an Internet Service Provider serving end user customers in New York State, New Jersey, Florida and Massachusetts. Petitioner does not offer telephony or telegraphy services to its customers, and Petitioner is not licensed as a competitive local exchange carrier or interexchange carrier in New York or any other state, or as a telecommunications carrier under federal law.

Petitioner's customers access Petitioner's services and the Internet by virtue of high-speed data Digital Subscriber Line (DSL) connections. The DSL path is separate from the voice grade telephone path. On March 28, 2001, Petitioner contracted with its telecommunication service provider (Provider) to supply to Petitioner high-speed, high-capacity communications services over Provider's existing network. Provider agreed to use DSL technology, in part, for the connection from the end user to equipment located at the local telephone company to achieve high data speeds and capacity. The local telephone company uses this equipment to connect to Provider's national Asynchronous Transfer Mode (ATM) network. All traffic from the end user or customer travels over Provider's national ATM network until it is "handed-off" to Petitioner at Petitioner's network operations center in New York City. At that point, the traffic is translated from ATM to Internet Protocol ("IP") and is routed by Petitioner's router to the appropriate Internet destination.

Petitioner's contract with Provider requires that Petitioner represent and warrant that:

- (i) Provider informed Petitioner "that the Services constitute telecommunications or telecommunications services . . . as defined by federal law, and as a result, [Provider] will assume the obligations of [inter alia] billing, collecting from [Petitioner] and remitting to governmental authorities any applicable taxes . . . ;"
- (ii) Petitioner "shall not in the ordinary course of its business, when using Services, be able to identify, and distinguish between, packet data transmissions that originate and

terminate within the same state (intrastate transmissions), and those packet data transmissions that originate and terminate in different states (interstate transmissions), and states that it is impractical to identify, distinguish and measure its intrastate and interstate transmissions on [Provider's] network;" and

(iii) Petitioner "estimates in good faith that more than ten percent (10%) of all data packets transmitted through Services will consist of interstate transmissions. . . ."

Petitioner represents that it cannot provide voice grade local or toll telephony in New York State because the DSL circuits Provider uses and to which Petitioner's end user customers have access are not connected in any way to the public switched telephone network.

Applicable Law and Regulations

Section 1105 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:

* * *

(b) (1) The receipts from every sale, other than sales for resale, of . . . (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 1115(v) of the Tax Law provides:

Receipts from the sale of Internet access service, including start-up charges, and the use of such service, shall be exempt from the taxes imposed under this article. For purposes of this subdivision, the term "Internet access service" shall mean the service of providing connection to the Internet, but only where such service entails the routing of Internet traffic by means of accepted Internet protocols. The provision of communication or navigation software, an e-mail address, e-mail software, news headlines, space for a website and website services, or other such services, in conjunction with the provision of such connection to the Internet, where such services are merely incidental to the provision of such connection, shall be considered to be part of the provision of Internet access service.

Section 1132(c)(1) of the Tax Law provides, in part:

For the purpose of the proper administration of this article and to prevent evasion of the tax hereby imposed, it shall be presumed that all receipts for property or services of any type mentioned in subdivisions (a), (b), (c) and (d) of section eleven hundred five . . . are subject to tax until the contrary is established, and the burden of proving that any receipt . . . is not taxable hereunder shall be upon the person required to collect tax or the customer.

Section 1139(a) of the Tax Law provides, in part:

In the manner provided in this section the tax commission shall refund or credit any tax, penalty or interest erroneously, illegally or unconstitutionally collected or paid if application therefor shall be filed with the tax commission (i) in the case of tax paid by the applicant to a person required to collect tax, within three years after the date when the tax was payable by such person to the tax commission as provided in section eleven hundred thirty-seven, or (ii) in the case of a tax, penalty or interest paid by the applicant to the tax commission, within three years after the date when such amount was payable under this article

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

Sale of utility and similar services.

(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

(i) gas, electricity, refrigeration and steam, and gas, electric, refrigeration and steam service of whatever nature; and

(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.

* * *

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

(1) The provisions of section 1105(b) of the Tax Law with respect to telephony and telegraphy and telephone and telegraph service impose a tax on receipts from intrastate communication by means of devices employing the principles of telephony and telegraphy.

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

* * *

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.

* * *

(4) A service is not considered telegraphy or telephony if either of these services is merely an incidental element of a different or other service purchased by the customer.

* * *

(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.

(6) Where a customer has telephones at a single location connected to exchanges in different localities, and a tie-line to a locality in which he is not located,

the tax rate applicable for each service is the tax rate in effect in the locality to which the exchange is assigned.

Example 8: A business located in Nassau County has two telephone numbers, one with a Nassau exchange and one with a Queens exchange. This enables his Queens customers to phone him toll free. Service on the Queens exchange is considered to be purchased in Queens County even though the telephone is physically located in Nassau County.

Opinion

Petitioner is an Internet Service Provider (ISP) and does not sell telephone or telegraph services. Petitioner's charges to its customers for access to the Internet are not subject to sales tax. See section 1115(v) of the Tax Law. Petitioner has contracted for and purchases Digital Subscriber Lines (DSL) from Provider. The DSL services purchased by Petitioner from Provider are considered to be telephone or telegraph services which provide a high capacity data transfer between Petitioner's router and its customers to facilitate its customers' access to the Internet. See section 1105(b) of the Tax Law, and Biscotti, Toback and Co., CPA's, PC, Adv Op Comm T & F, March 3, 2003, TSB-A-03(6)S. Petitioner is not purchasing telephone or telegraph services from Provider other than those used to transmit data from Petitioner's customer to Petitioner's Internet router.

Since Petitioner is an ISP and does not sell telephone or telegraph services to its customers, it does not purchase the DSL services from Provider for resale. Rather, Petitioner uses or consumes its purchases of DSL in the provision of high speed Internet access to its customers. Since Petitioner is purchasing the DSL to connect its customers to its Internet router via Provider's network and local telephone lines, such purchases are taxable purchases of telephone or telegraph services where the services are intrastate in nature. Purchases by Petitioner of interstate or international telephone or telegraph services are not subject to the sales tax. See section 1105(b)(1)(B) of the Tax Law and section 527.2 of the Sales and Use Tax Regulations. In Western Union Telegraph Company, Dec St Tx Comm, February 4, 1983, TSB-H-83(57)S, the State Tax Commission determined that a telegraph service where the messages originated and terminated in New York was taxable intrastate telegraphy regardless of the fact that the messages were routed through computers located in New Jersey. Therefore, if Petitioner's Internet router is located in New York State, Petitioner's purchase of DSL connecting Petitioner's customers to its router is taxable when Petitioner's customer is located in New York State since such purchase constitutes a purchase of intrastate telephone or telegraph services. Petitioner's purchase of DSL connecting Petitioner's customers to its router located in New York State is not taxable when Petitioner's customer is located outside New York State, since such purchase constitutes a purchase of interstate or international telephone or telegraph services. This is so regardless of the route that the signal may take between Petitioner's router and its customer. See Western Union Telegraph Company, *supra*. It is also immaterial that Petitioner's customers may be visiting Web sites located outside New York State since Petitioner is only purchasing telephone or telegraph services from Provider between Petitioner's customer and Petitioner's router.

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Provider in this case must maintain records indicating the location of each of Petitioner's customers in order that Provider may properly collect sales tax from Petitioner on those charges pertaining to Petitioner's customers located in New York State, and exclude from tax those charges pertaining to Petitioner's customers located outside New York State. Likewise, Petitioner may apply for a refund of the sales tax it has paid to Provider on purchases of DSL if it can show that those charges pertain to Petitioner's customers located outside New York State. Such claims for refund of sales tax must be submitted within three years after the date that the tax was payable by Provider to the Department of Taxation and Finance. See sections 1132(c)(1) and 1139(a) of the Tax Law.

DATED: September 3, 2003

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