STATE OF NEW YORK

TAX APPEALS TRIBUNAL

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| In the Matter of the Petition | : | |
| of | : | |
| **SOUTHERN PACIFIC COMMUNICATIONS COMPANY** | : | DECISION |
| for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period September 1, 1970 through February 28, 1981. | : | |

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on March 22, 1990 with respect to the petition of Southern Pacific Communications Company, One Stamford Forum, Stamford, Connecticut 06904 for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1970 through February 28, 1981 (File No. 800275). The Division of Taxation appeared by William F. Collins, Esq. (James Della Porta, Esq., of counsel). Petitioner appeared by Richard N. Wiley, Esq. and Scott B. Clark, Esq.

The Division of Taxation submitted a memorandum of law in support of its exception. Petitioner submitted a brief in opposition. Oral argument was heard at the request of the Division of Taxation on November 14, 1990.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

## *ISSUE*

Whether long distance telephone services rendered by petitioner are subject to sales taxes.

## *FINDINGS OF FACT*

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Pursuant to 20 NYCRR 3000.7, the Division of Tax Appeals and petitioner entered into a stipulation of facts. At the request of the Administrative Law Judge, this initial stipulation was supplemented with additional facts. The stipulated facts and additional facts are as follows.

During the period in issue, petitioner, Southern Pacific Communications Company, was a specialized common carrier of communications subject to the jurisdiction of the Federal Communications Commission ("FCC"). As aspecialized common carrier, it did not provide the services commonly associated with local telephone companies. It offered a limited microwave system for the transmitting of electrical impulses. This system provided inter-city communications services to the public, offering private line, restricted switched service and data services to both business and residential customers. In short, petitioner was what is commonly called a long-distance telephone company.

On June 20, 1982, the Division of Taxation issued to petitioner, GTE Sprint Communications Corporation, then known as Southern Pacific Communications Company, and hereinafter referred to as "GTE Sprint", two notices of determination and demands for payment of sales and use taxes due, asserting additional sales and use taxes plus interest. Notice number S820611019A, dated June 20, 1982, notified GTE Sprint that sales and use taxes in the amount of $584,737.84 plus interest of $350,510.82, for a total of $935,248.66, had been determined to be due for the period September 1, 1970 through August 31, 1977. Notice number S820611020A, also dated June 20, 1982, notified GTE Sprint that sales and use taxes in the amount of $1,450,733.12 plus interest of $377,751.45, for a total of $1,828,484.57, had been determined to be due for the period September 1, 1977 through February 28, 1981.

The first sales tax return filed by GTE Sprint was for the quarter beginning December 1, 1975. Consents to extend the three-year limitation period were periodically executed only for quarters beginning after March 1, 1976. Therefore, the three-year limitation period for the quarter ending February 29, 1976 expired before the issuance of the statutory notice. The notices, as they relate to all other periods assessed, were timely issued.

The $2,035,470.96 total sales and use taxes assessed consisted of sales tax of $634,819.00 and use tax of $1,399,234.97. On September 17, 1987, the Division of Taxation issued a Statement of Proposed Audit Adjustment, following further review of the use tax portion of the assessment. The statement specifically stated that it reflected the results of the use tax audit only. Revised use tax of $984,999.96 plus interest of $1,169,887.57 was proposed for the period September 1, 1970 through February 28, 1981. On September 17, 1987, GTE Sprint's authorized representative submitted to the Division, a Consent to Fixing of the (Use) Tax as proposed. On October 8, 1987, GTE Sprint remitted the use tax of $984,999.96 plus interest of $1,169,887.57 to the Department of Taxation and Finance. As a result of these actions, the only taxes remaining in contention in the instant proceedings are sales taxes totaling $634,819.00, assessed for the period September 1, 1970 through February 28, 1981.

In the stipulations: the word "State" means the State of New York; the phrase "GTE Sprint's physical network" means the tangible communications facilities owned or leased by GTE Sprint and over which it exercised exclusive rights of management and control - the term specifically excludes services or facilities provided by other carriers pursuant to tariff; and the word "period" refers to September 1, 1970 through February 28, 1981.

The Assessed Transactions

The individual items offered by GTE Sprint to its customers in transactions for which sales tax was assessed are set out below, along with the corresponding amounts of sales tax assessed.[1]

| ITEM | |
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| Private Line Services: | |
| 1. Monthly mileage service charge | $ 55,944.94 |
| 2. Local distribution facilities | 60,445.29 |
| 3. 4 kilohertz termination charges | 43,273.50 |
| 4. Modems | 529.44 |
| 5. Termination at CCSA | 6,229.83 |
| 6. Outside move charges | 794.16 |
| 7. LDF end of foreign exchange | 1,058.87 |

[1]The services listed here as Items 2 through 19 and 23 through 43 are described in Appendix II.

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| 8. Special billing | 1,094.18 |
| 9. Busy lamp | 35.32 |
| 10. C-2 conditioning | 158.82 |
| 11. Multi-point service drops | 653.01 |
| 12. Short-haul termination charges | 1,023.20 |
| 13. Multi-point channel 1,411.85 | |
| 14. Signaling equipment | 847.13 |
| 15. Service charge | 141.18 |
| 16. Loop | 617.67 |
| 17. Voice and data arrangement | 158.82 |
| 18. Traffic analysis - 12 months | 1,835.40 |
| 19. DTMF to Rotary | 229.83 |
| Private Line Services Total | $176,482.44 |
| Switched Services: | |
| 20. Sprint 5 access | $155,780.36 |
| 21. Sprint 5 usage | 210,125.86 |
| 22. Sprint 5 minimum | 33,530.66 |
| 23. Datadial | 6,196.22 |
| 24. Sprint 1 speedline | 2,411.32 |
| 25. Sprint 1 business port | 2,251.87 |
| 26. Sprint 1 speedline minimum | 3,016.29 |
| 27. Sprint 1 security code | 5.33 |
| 28. Sprint 1 WBT line | 405.75 |
| 29. Sprint 1 Greenwich dial | 352.65 |
| 30. Sprint 1 NY site preparation | 85.98 |
| 31. Sprint 1 NY SP/power | 105.16 |
| 32. Sprint 2 & 4 general access port | 1,910.08 |
| 33. Sprint NYC usage | 81.10 |
| Switched Services Total | $416,258.63 |

"Other"

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|---|---|
| 34. Modem | $ 7,615.97 |
| 35. Traffic analysis - 12 months | 1,304.40 |
| 36. Installtion | 1,472.57 |
| 37. Voice and data arrangement | 1,178.26 |
| 38. Multi-point service drop | 2,229.76 |
| 39. C-2 conditioning | 1,220.23 |
| 40. Baud data term | 420.76 |
| 41. DTMF to rotary | 1,051.81 |
| 42. Service charge | 25,498.18 |
| 43. D-1 conditioning | 84.22 |
| "Other" Total | $ 42,076.16 |
| TOTAL | $634,817.23 |
| Effects of rounding | 1.77 |
| ROUNDED TOTAL = Sales tax assessed | $634,819.00 |

Each of the 43 separate items upon which sales tax was assessed was separately identified on GTE Sprint's customers' bills, and each was assigned a separate charge. When totaled the separate charges reflected the amount due from the customer for the month.

GTE Sprint did not charge or collect any sales tax from its customers for any of the above-described transactions.

The parties stipulate that Items 2 through 19 and 24 through 43 above are for services, and not equipment. Further, these services do not, by themselves, comprise telephone services, but are, instead, component parts of the telephone services provided by GTE Sprint to its customers.

As an additional fact, it is found that on audit, items 24 (Sprint 1 Speedline), 25 (Sprint 1 business port), 26 (Speedline minimum) and 32 (Sprint 2 and 4 general access port) were deemed to be the lease of equipment in New York State and as such were held to be taxable charges.

GTE Sprint was authorized by the FCC to provide only long distance interstate service and GTE Sprint offered only such service during the period at issue. GTE Sprint's customers had the capability of making and did in fact make long distance phone calls between points within the State via GTE Sprint's switched services.

Private Line Services

The term "private line service" generally refers to the provision by a carrier of specific circuits, or lines, dedicated to the sole use of a particular customer. Private lines are sometimes referred to as "tie-lines". GTE Sprint offered telephone-to-telephone ("end-to-end") private line services which were regulated by the Federal Communications Commission (FCC) and offered pursuant to FCC-approved tariffs. Those tariffs described the specific services and enhancements offered, and specified the terms and conditions by which they were provided. Specifically, the items listed above for "private line service" (Items 1 through 19) and "other" (Items 34 through 43) were offered for sale in GTE Sprint's private line tariffs filed with the FCC.

The monthly mileage service charge (Item 1) refers to the charge for private line service which varied according to the length of the line, increasing as the length of the line increased. During the period, all GTE Sprint private lines between points in the State passed physically through the State of New Jersey, although the charge was calculated based upon the airline mileage distance between the in-State points. A customer's private line circuits between points in the State could be, and were, connected to other private line circuits ending out-of-State. Thus, a customer's Albany/New York City circuit could connect to the same customer's New York City/Miami, or Albany/Chicago circuits.

GTE Sprint's physical network comprised only an intermediate part of the private line communication pathways. In order to complete the communication pathways, additional physical facilities were needed to link the customer's telephones at either end to GTE Sprint's intermediate physical network. In addition, certain enhancements of that line could only be performed at one or both ends. As an intermediate carrier, GTE Sprint could not, by itself, provide those enhancements.

The facilities that provided the final "links" in, and enhancements of, the communication pathways were purchased by GTE Sprint from the local exchange telephone companies ("LECs"),

and consisted of the items listed above at items 2 through 19 and 34 through 43. GTE Sprint purchased those items from the LECs and then charged its customers for those very same items. The LECs' provision of these items was regulated by the FCC, and was subject to the terms and conditions of the LECs' tariffs filed with that agency. Those tariffs were entitled "Local Distribution Circuits For Patrons of the Other Common Carriers". No customer could make communications solely through the employment of those items. Rather, the addition of the GTE Sprint physical network and LEC-provided facilities at the distant end was necessary to establish the end-to-end communication pathway, and to place into effect the enhancements.

Under the LECs' tariffs, neither GTE Sprint nor its customers could designate, specify, design, own, control, test, repair, maintain, move, change, or in any other way assert dominion or control over the physical facilities (i.e., cable, structures, protective features, poles, plug-in units, etc.) used by the LEC to complete and enhance the communication pathway to and from the GTE Sprint physical network. The design and assignment or routing of specific facilities and equipment items to meet the service requirement as requested by GTE Sprint was performed exclusively by the LEC. Although GTE Sprint was responsible for the end-to-end service, it was required to notify the LEC of problems with the LEC portion of the pathway, and the LEC would perform any necessary repairs at no charge to GTE Sprint.

The private line monthly mileage service charges were calculated on the basis of connecting two points, such that a separate charge would be made for a Buffalo/Albany circuit and for a New York City/Miami circuit. The charges for each circuit would be calculated pursuant to GTE Sprint's FCC tariffs.

GTE Sprint provided private line services on a telephone-to- telephone basis. The charges for those services were determined by the circuit mileage, the access arrangements, or "links", employed, and by the circuit enhancements ordered. All of the access arrangements and circuit enhancements necessary to service a customer's needs were purchased by GTE Sprint from the LECs and were then sold to the end users by GTE Sprint. These access arrangements and

enhancements, provided in connection with private line services, are listed at items 2-19 and 34-43 above.

Switched Services

The term "switched services" generally refers to the provision by a carrier of services over any available line selected by the carrier's switch. If all of the lines are "busy", the call cannot go through. Unlike the dedicated private line networks, all customers "share" the switched networks. Most residential and business customers use the switched networks. GTE Sprint's end-to-end switched services were regulated by the FCC, and were offered pursuant to FCC-approved tariffs. Those tariffs described the basic switched services and features offered, and specified the applicable terms and conditions. Specifically, the items listed above for "switched services" (Items 20 through 33) were offered for sale in those switched service tariffs.

The Sprint 5 usage charge (Item 21) and Datadial charge (Item 23) refer to the charges for switched services which varied according to the distance, duration, and time of day of the telephone communication, increasing as the distance and duration increased. During the period, all GTE Sprint switched service communications that might have been between points in the State passed physically through the State of New Jersey, although the charge was calculated based upon the airline mileage distance between the GTE Sprint physical network entry point and the location where the communication was received.

As was the case for private line services, GTE Sprint's physical network comprised only an intermediate part of the switched communications' pathways. In order to complete the communications pathways, additional physical facilities were needed to link the telephones at either end to GTE Sprint's intermediate physical network. The facilities that provided the final "links" in the communication pathway were purchased by GTE Sprint from the LECs. The LECs provision of these links was regulated by the FCC, and was subject to the terms and conditions of the LECs' tariffs filed with that agency. Those tariffs were entitled "Exchange Network Facilities For Interstate Access" ("ENFIA").

These ENFIA services provided by the LECs did not provide GTE Sprint with information identifying the telephone number, and thus the location (state), from which calls originated. This information, known as automatic number identification ("ANI") was made available by the LECs only to themselves for traffic billed by them. Therefore, while the LECs were able to determine the location of the origin of calls billed by them, no such information was available to GTE Sprint during the period. This information is now available to companies like Sprint as a result of the provision by the LECs of "equal access", which was mandated by the court decree divesting AT&T of its LECs.

The Sprint 5 access charge (Item 20) was $10.00 per customer per month. For this charge, the customer was given "access" to the GTE Sprint network. That is, the customer was given a list of the telephone numbers to dial in order to access the GTE Sprint network, along with a personal identification number which, when dialed, would identify the caller to the GTE Sprint switch as a valid GTE Sprint customer. However, the charge was imposed whether or not telephone calls were made, so long as the personal identification number was maintained in the system. Separate and additional charges were imposed for any telephone calls actually made by the customers, without credit for the $10.00 access charge. The access charge allowed GTE Sprint to charge less for telephone calls than it would have had to charge were no access charge imposed.

The Sprint 5 minimum usage charge (Item 22) was $25.00 per customer per month. If the customer used more than $25.00 in telephone service, no minimum usage charge would apply. However, if the customer used less than $25.00 in telephone service, he or she would be subject to all or part of the minimum usage charge. For example, if the actual usage was $20.00, the customer would be subject to a minimum usage charge in the amount of $5.00, and $5.00 would be treated by the Division of Taxation as subject to the sales tax. Minimum usage charges were imposed to recover administrative expenses associated with maintaining records for

nonperforming customers, and to assure that inactive customers would take steps to cancel their accounts.

Sprint 1 speedline (Item 24) and business port (Item 25) allowed customers who called the same number often the ability to be automatically connected to that number upon accessing the GTE Sprint network. The Sprint 1 speedline minimum usage charge (Item 26) was similar to the Sprint 5 minimum usage charge, above. Other charges (Items 27 through 31 and Item 33) were for special services provided to particular customers. The Sprint 1 & 4 general access port services provided customers with dedicated "links", over facilities provided by the LECs, into the GTE Sprint network access number and personal identification number.

The switched service charges included in items 20 through 26 and item 32 were all imposed for services offered by GTE Sprint pursuant to the terms and conditions specified in its FCC tariffs.

Origination of Calls

Calls could be made from out-of-State locations which would enter GTE Sprint's physical network in New York State. In some cases GTE Sprint charged for the in-State and out-of-State portions of these interstate calls, while in other cases another company might charge for the out-of-State portion.

The cross-border local exchange situation was one case where GTE Sprint would render the entire charge for an out-of-State call entering its network in-State. Thus, when a caller was across the State border, but within an exchange partly located in New York, he or she utilized cross-border exchange access services to enter the GTE Sprint network in New York. In this case, FCC rules placed the responsibility for the entire telephone-to-telephone transmission upon GTE Sprint, and GTE Sprint was required to pay the local telephone company for the cross-border access portion. GTE Sprint priced its telephone-to-telephone service to recover the cross-border access costs (which, overall, comprise roughly 25% to 50% of the company's nationwide

operating expenses), and billed the customer accordingly. In sum, a single charge was applied by GTE Sprint to the whole of a call across state lines.

The split-billing scenario, on the other hand, is illustrated by an example where New York offers the closest Sprint network entry point for an out-of-State Sprint customer (as was often the case during the audit period). Here, an LEC (in partnership with AT&T's Long Lines Department) would impose a separate interstate toll charge for the portion of the call from the out-of-State telephone to the GTE Sprint switching computer in New York, the remainder of the interstate call being billed by GTE Sprint. In this case, then, two separate charges were applied to the whole interstate call, one by the LEC and the other by GTE Sprint.

Audit Method

The Division of Taxation treated the private line monthly service charge (Item 1) as subject to sales tax when made for private line circuits between two points in the State. This was so, regardless of whether the customer was billed to an out-of-State address or whether the the in-State circuit was connected to a circuit ending out-of-State. Tax was not assessed for circuits between a point in the State and a point in another state.

Sprint 5 usage charges (Item 21) and Datadial usage charges (Item 23) were treated by the Division as subject to sales tax when made for switched service communications entering GTE Sprint's physical network in the State and also received in the State. This was so, regardless of whether the customer's billing address was in or out of State. Tax was not assessed on communications entering GTE Sprint's physical network in another state and received in-State. Likewise, tax was not assessed on communications entering GTE Sprint's network in-State, but received in another State.

Sprint 5 access charges (Item 20) and Sprint 5 minimum charges (Item 22) were treated by the Division as taxable if the customer's billing address was located in the State, without regard to whether that customer made any communications, whether the communications made entered GTE Sprint's network in the State or elsewhere, or whether the communications made were

received in-State or elsewhere. These charges were also deemed subject to sales tax even if the customer's address was out of state and the customer was billed to an address located out of State, if the customer's bill indicated that more than 50 percent of its calls entered GTE Sprint's physical network in-State. The Sprint 5 access charges and minimum charges represent fees for the privilege of having the capability of making long distance telephone calls over GTE Sprint's telecommunications systems. The fees were due regardless of whether the customer ever used GTE Sprint's telecommunications systems.

All other charges (Items 2 through 19 and 24 through 43) were treated by the Division as subject to sales tax if the charge was made for activity occurring within the State. This was so, regardless of whether the customer's billing address was located in the State or elsewhere. The Division deemed the providing of these items to be a transaction subject to sales tax.

The Division used two methods to determine the taxability of charges billed by GTE Sprint for items 2 through 19 and 24 through 43. The first was to identify GTE Sprint billing invoices which had a New York billing address. The Division assessed sales tax on all charges on these invoices, excepting those charges made for calls entering GTE Sprint's physical network in states or countries that were different from the calls' destination state or country, and excepting those charges made for calls entering GTE Sprint's physical network in the same state as the calls' destination state if that state was not New York.

The second method focused on GTE Sprint billing invoices which had non-New York billing addresses. The examiners identified the invoices with non-New York billing addresses which contained charges for calls entering GTE Sprint's physical network in New York. Sales tax was assessed on the charges made for all of the calls billed out of State which entered GTE Sprint's physical network in New York when the calls also had New York destinations. In addition, sales tax was assessed on the minimum, access and other charges if more than 50 percent of all of the calls on an invoice entered GTE Sprint's physical network in New York, (calculated without regard to whether those calls had New York or out-of-State destinations).

The parties stipulate to the authenticity of the diagram included as Appendix I, describing the communication pathways for a communication between New York City and San Francisco.

***OPINION***

In the determination below, the Administrative Law Judge determined that petitioner's provision of interstate telephone services was not subject to the imposition of sales tax under Tax Law § 1105(b). The Administrative Law Judge specifically found that the telephone service sold by petitioner was interstate in nature and that the audit's attempt to isolate the purely intrastate components of the service was arbitrary. Accordingly, the Administrative Law Judge cancelled the assessment against petitioner in the amount of $634,819.00 for the period at issue, September 1, 1970 through February 28, 1981.

On exception, the Division of Taxation (hereinafter the "Division") asserts that the Administrative Law Judge erred in excepting petitioner's telephone service from sales tax. First, the Division contends that the Administrative Law Judge erred in concluding that there was a single meaning of interstate commerce. Specifically, the Division contends that the meaning of interstate depends on its context and for purposes of Tax Law § 1105(b), the term "interstate" means a communication with one terminus outside New York. The Division further maintains that petitioner's charges for private line service between points within the State are subject to sales tax, notwithstanding that these charges may have been supplemented by charges for interstate phone services. The Division also asserts that the portion of petitioner's receipts attributable to access charges are subject to sales tax because they represent the consideration for the right to make intrastate long distance phone calls. It is irrelevant, suggests the Division, that the charges may also represent the consideration for the right to make interstate phone calls. Lastly, the Division posits that the fact that petitioner's customers may have made infrequent intrastate calls does not change the taxable status of the components at issue.

In response, petitioner argues in the first instance that the Tax Appeals Tribunal lacks jurisdiction to review the determination of the Administrative Law Judge. In addition, petitioner

asserts that the Division failed to carry its burden to show petitioner's service was subject to sales tax. Petitioner also argues that the proper approach to discern whether the transaction is subject to tax is to look at the overall activity rather then examining the service on a "component by component" approach as advocated by the Division. In that regard, petitioner notes that the relevant case law supports an inquiry based on the overall nature of the service. Petitioner also emphasizes that the stipulation of facts indicate that the charges at issue are components of the overall interstate service and, therefore, are not subject to tax.

We affirm the determination of the Administrative Law Judge for the reasons set forth below.

Preliminarily, petitioner asserts that Tax Law § 2006(7) prohibits the Tribunal from reviewing the determination of the Administrative Law Judge. Tax Law § 2006(7) provides, inter alia, that a determination by an Administrative Law Judge denying a motion for summary determination is not reviewable by the Tax Appeals Tribunal. The determination at issue here does not involve the denial of a motion for summary determination. A review of the procedural posture of this matter establishes that neither party to this proceeding ever made a motion for summary determination pursuant to Tax Law § 2006(6). Accordingly, the provision in Tax Law § 2006(7) limiting the review of the Tax Appeals Tribunal is inapplicable here.

We now turn to the merits of the matter before us. Tax Law § 1105(b) imposes a tax on "[t]he receipts from every sale . . . of telephony and telegraphy and telephone and telegraph service of whatever nature except interstate and international . . . service" (Tax Law § 1105[b] emphasis added). As relevant here, the term "receipt" is further defined as "the charge for any service taxable under [Article 28]" (Tax Law § 1101[b][3]). The term "telephony and telegraphy" includes the "use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals" (20 NYCRR 527.2[d][2]).

It is undisputed that petitioner provides telephone service within the meaning of Tax Law § 1105(b)[2] and 20 NYCRR 527.2(d)(2). Contrary to the Division's assertion, it is also undisputed that the telephone service provided by petitioner in this matter is interstate in nature. The stipulation of facts entered into between the Division and petitioner in this matter specifically provides that petitioner is authorized by the FCC to provide only long distance interstate service and that during the period at issue, petitioner in fact offered only long distance interstate service. Accordingly the issue is not, as the Division argues, whether petitioner's service is interstate in nature. The interstate nature of petitioner's service has been established by the stipulation of facts agreed to by the Division and petitioner (see, 20 NYCRR 3000.7[e]). Rather, the issue presented on exception is whether certain components of petitioner's interstate service which have intrastate attributes may be segregated out and separately taxed under section 1105(b) of the Tax Law. We conclude that such an imposition of tax is not supportable.

Our conclusion rests on the Court of Appeals decision in Matter of Moran Towing and Transp. Co. v. New York State Tax Commn. (72 NY2d 166, 531 NYS2d 885) which interpreted the meaning of interstate commerce for sales tax purposes in the context of another sales tax exemption, section 1115(a)(8) of the Tax Law. This case establishes two important points to guide our analysis. First, that it is appropriate, absent any contrary indication in the statute or legislative history, to give the phrase interstate commerce its "precise and well settled legal meaning in the jurisprudence of the state" (Matter of Moran Towing and Transp. Co. v. New York State Tax Commn., supra, 531 NYS2d 885, 889, citing McKinney's Cons Laws of NY, Book 1, Statutes § 238). Since this was the standard utilized by the Administrative Law Judge, this holding rebuts the Division's challenge to this aspect of the Administrative Law Judge's determination.

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[2]The Administrative Law Judge did not, as argued by the Division (brief on exception, p. 3), find that certain of the charges at issue were for the lease of tangible personal property. Instead, the Administrative Law Judge found that the Division's audit report characterized the charges in this manner.

The second important aspect of Moran Towing is that it establishes that in determining whether a taxpayer's activities are in interstate commerce, it is improper to isolate and individually examine separate components of the overall activity being engaged in by the taxpayer. In Moran Towing, tugboats operating only in New York State waters provided towing services to vessels traveling in interstate commerce. The former State Tax Commission held that the tugboat operations were not within the interstate commerce exemption, stating "while the tugboats are related to the conduct of interstate or foreign commerce, their activities are in general a local event, separate and distinct from interstate commerce" (Matter of Moran Towing and Transp. Co. v. New York State Tax Commn., supra, 531 NYS2d 885, 887). The Court of Appeals rejected this analysis stating "[t]hat the taxpayer's activities were conducted entirely within the waters of the State of New York does not affect the interstate character of those activities. The focus is on what the actor does, not where he does it" (Matter of Moran Towing and Transp. Co. v. New York State Tax Commn., supra, 531 NYS2d 885, 887, citations omitted). The Court concluded that the tugboats were engaged in interstate commerce because the boats they directed were in interstate commerce.

We conclude that the Court's decision in Moran Towing dictates that the Division's attempt to segregate and tax components of petitioner's interstate service must be rejected. If the activities of a taxypayer operating exclusively in New York State cannot be examined for sales tax purposes apart from their interstate context, it follows that the activities of a taxpayer in interstate commerce cannot be segmented into State components and isolated from their interstate commerce context (see, Matter of M & G Convoy v. State Tax Commn., 55 AD2d 204, 389 NYS2d 656, affd 42 NY2d 1017, 398 NYS2d 657 [where the isolation of a New York component of an interstate trip was rejected for franchise tax purposes]).

Our conclusion, that the overall nature of the telephone service determines whether it is in interstate commerce and excepted from tax, is consistent with the Division's opinion that a charge by a local telephone service provider to its customers for the ability to access long distance

services is subject to sales tax as a component of the basic local telephone service (New York Tel. Co., Advisory Opn., Commr. of Taxation & Fin., January 5, 1988 [TSB-A-88(8)S]; Rochester Tel. Corp., Advisory Opn., Commr. of Taxation & Fin., December 9, 1987 [TSB-A-88(1)S]).[3] Clearly, these advisory opinions rest on the rationale that the local telephone service was intrastate in nature and the inclusion of an incidental component that may have had an interstate character did not alter the overall intrastate nature of the service. A similar analysis was also the basis for the Appellate Division's decision in Matter of Callanan Mar. Corp. v. State Tax Commn. (98 AD2d 555, 471 NYS2d 906, lv denied 62 NY2d 606, 479 NYS2d 1026), where the Court concluded that the incidental passage of a boat through interstate waters in what was clearly an intrastate journey did not affect the intrastate nature of the trip[4] (see also, Matter of Western Union Tel. Co., State Tax Commn., March 14, 1983 [where it was concluded that messages passing between points in New York State did not lose their intrastate character simply because they reached their New York destination via New Jersey]). If, as these opinions hold, an intrastate service retains a single intrastate identity in spite of an incidental interstate aspect, we can see no reason for a different rule which would segment an interstate service into components.

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[3]This advisory opinion regarding Rochester Telephone Corporation was cited with approval by the Supreme Court, Albany County in Davidson v. Rochester Tel. Corp. (Sup Ct, Albany County, April 10, 1989, Prior, J) and was said to represent "an accurate interpretation of the law." On appeal to the Third Department, the decision of the Supreme Court was affirmed but on a different legal basis (Davidson v. Rochester Tel. Corp., ___ AD2d ___, 558 NYS2d 1009, lv denied 76 NY2d 714, 564 NYS2d 717). As noted by the Administrative Law Judge, the advisory opinion cited in Davidson does not lend support to the Division's position. In fact, that advisory opinion advocates an approach opposite to the one argued by the Division on exception; that is, that the overall nature of the telephone service is the point of inquiry, not the adjunct components of the service (see, TSB-A-88[1]S, supra).

[4]The Division relies on Matter of Callanan Mar. Corp. v. State Tax Commn. (98 AD2d 555, 471 NYS2d 906) for its position that the New York components of petitioner's service can be taxed. The Court of Appeals in Moran Towing concluded that Callanan did not establish such a rule, but instead merely established the rule that an incidental interstate aspect did not change the nature of "indisputably intrastate voyages" (Matter of Moran Towing & Transp. Co. v. New York State Tax Commn., supra, 531 NYS2d 885, 888). The Moran Towing decision also disposes of another case relied on by the Division, Matter of Niagara Junc. Ry. Co. v. Creagh (2 AD2d 299, 154 NYS2d 229). The Court of Appeals indicated that Niagara Junction Railway has little bearing where, as here, the statutory meaning of interstate commerce is in issue (Matter of Moran Towing & Transp. Co. v. New York State Tax Commn., supra, 531 NYS2d 885, 888).

Applying the Moran Towing analysis to the stipulated facts in this matter results in the conclusion that petitioner has demonstrated its entitlement to the exclusion at issue here. The stipulation of facts specifically provides that the character of the service provided by petitioner is exclusively interstate service. The stipulated facts further state that the charges at issue "do not, by themselves, comprise telephone services, but are, instead, component parts of the telephone services provided by [petitioner] to its customers" (emphasis added). While it is true that portions of the components at issue included long distance service between points within the State, these components are clearly part of the overall interstate service provided by petitioner. Accordingly, the portions of petitioner's interstate service which the Division is seeking to tax must be treated as a component part or adjunct to the overall interstate service provided by petitioner. Therefore, we find that the charges at issue here are excluded from the imposition of sales tax pursuant to section 1105(b) of the Tax Law.

Lastly, the Division argues that if taxable and nontaxable services are covered by a single charge, the entire charge is subject to sales tax. The Division appears to be arguing thereby that the stipulated fact that petitioner's service is interstate in nature is irrelevant (Division's brief, pp. 11-13) and that the entire service should be rendered taxable. That position, however, must be rejected because it would result in imposition of tax on an interstate service in clear violation of the exemption provided in Tax Law § 1105(b) for interstate telephone service.

Nothing in this decision is intended to address the application of the sales tax to an audit that identified and taxed only those services that took place entirely in New York State and which were not an intrastate strand of an interstate service. Examples of such services might include switched services for calls originating in New York State and going to New York State locations and private line circuits between points in New York State which were not connected to a circuit going to another state.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of the Division of Taxation is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petition of Southern Pacific Communications Company is granted to the extent indicated in conclusions of law "E" and "F" of the Administrative Law Judge's determination; and

4. The notices of determination and demand for payment of sales and use taxes due dated June 20, 1982 are cancelled.

DATED: Troy, New York
May 14, 1991

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner

APPENDIX II

Description of Items 2 through 19 and 23 through 43

2. Local distribution facilities - the basic charge made by GTE Sprint to recover the costs of the LEC - provided access "link" portion of the private line circuits, that is, the portion of the circuit that connects the Sprint network entry-exit points to the subscriber's telephones. The charge is partly fixed and partly sensitive to the distance from the customer's premises to the GTE Sprint facility.

3. 4 Kilohertz termination charge - the charge made by GTE Sprint to recover the costs of LEC-provided multiplexing services. Multiplexing is the process of breaking a single radio channel into several circuits so that numerous conversations may simultaneously be carried over that single channel.

4. Modems - charges are for LEC-supplied conversions of signals from analog (wave) form to digital form, such as when a digital computer signal is converted to an analog signal for transmission over GTE Sprint's (then) analog network.

5. Termination at CCSA - charges imposed for GTE Sprint circuits terminating onto LEC-supplied "common control switching arrangement" facilities, which are used by the LECs to provide their very large customers (such as Ford) with virtually private networks, while utilizing the resources of the public switched network.

6. Outside move - charges for LEC's movements of facilities located "outside" their central office facilities, such as when the LEC moves a customer circuit from one location to another.

7. LDF end of foreign exchange - Foreign exchange services permit a company to maintain a local telephone number in a city far away from the company's office. For example, an airline may subscribe to foreign exchange services which permit its reservation agents in Minneapolis to pick up calls to a local New York City telephone number. The Minneapolis LEC's access services

linking GTE Sprint's Minneapolis facilities to the customer's Minneapolis facilities is called the LDF end of the foreign exchange.

9. Busy Lamp - tells a customer whether his/her private line is already in use. As with the other items, the lamp is supplied by the LEC to GTE Sprint under tariff and GTE Sprint supplies it to the end user, also under tariff.

10. C-2 conditioning - a type of circuit conditioning (e.g., frequency response, attenuation, distortion, delay characteristics) necessary in order for a circuit to carry certain types of data transmissions. The LEC provides the conditioned circuits.

11. Multi-point service drops - this is where a subscriber would have, for example, a private line terminating in NYC and also might have offices located in midtown. The subscriber requires that one circuit connect both locations (i.e., a private line between multiple locations). To provide this service GTE Sprint would order facilities or access from the local exchange provider.

12. Short haul termination charges - this describes the rate schedule which exists for short haul service versus long haul service, which has a different rate structure.

13. Multi-point channel - similar to multi-point service drops. Involves a private line service that serves multiple points. A subscriber may have one point of service in NYC, another in Philadelphia and a third and fourth in Baltimore and Washington, DC. All four of these points are connected to the same private line channel.

16. Loop-transmitting loop - like a local distribution facility, but it is used to connect one of GTE Sprint's locations to one of its other locations or one customer location to another customer location in the same area.

17. Voice and data arrangement - type of conditioning. Service leased by GTE Sprint from a local exchange provider for resale to its subscriber.

18. Traffic analysis - 12 months- traffic analysis usage recording and analysis service on GTE Sprint's private line facilities.

19. DTMF to Rotary - refers to a rotary converter used to convert touch tone signaling to rotary signaling.

23. Datadial - similar to GTE Sprint access, usage and minimum charges but for data rather than voice transmittal.

24. Sprint 1 Speedline - an arrangement whereby GTE Sprint provides customers with the ability to be connected to a pre-selected location without dialing any digits after accessing the network.

25. Sprint 1 business port - denotes a switch port designed to enable a subscriber to enter or exit the GTE Sprint network to or from an off network location via a local telephone company provided business line.

26. Sprint 1 speedline minimum - a minimum charge billed to the customer for speedline service whether or not the customer uses the service.

27. Sprint 1 Security code - this is a service requested by a customer to prevent unauthorized usage of a service.

32. Sprint 2 & 4 general access port - denotes entrance or exit device on a switching machine which provides a means of connection between that switching machine and a termination point of the service.

34. Modem - see item #4.

35. Traffic analysis - 12 months- provided where there was a private line.

37. Voice and data arrangement - equipment to provide a voice alternate data service.

38. Multi-point service drop - a piece of equipment (i.e., a bridge) required to provide a multi-point configuration.

39. C-2 conditioning - see item #10.

40. Baud data term - equipment associated with a modem.

41. DTMF to rotary - converts touch tone signaling to rotary dial pulse type signaling required for private line service.

43. D-1 conditioning - type of conditioning similar to C-2 conditioning.