STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
PHONE PROGRAMS, INC.	:	DECISION DTA NO. 815759
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Years 1990, 1991 and 1992.	:	

Petitioner Phone Programs, Inc., c/o David Isaacson, Esq., 166 Madison Avenue, New York, New York 10016, filed an exception to the determination of the Administrative Law Judge issued on February 18, 1999. Petitioner appeared by David Isaacson, Esq. The Division of Taxation appeared by Barbara G. Billet, Esq. (Robert Tompkins, Esq. and James Della Porta, Esq., of counsel).

Petitioner filed a brief in support of its exception. The Division of Taxation filed a letter in lieu of a brief in opposition and petitioner filed a reply brief. Oral argument, at petitioner's request, was heard on October 12, 1999 in New York, New York. The Division of Taxation and petitioner filed additional legal arguments by letters dated December 3, 1999 and December 29, 1999, respectively.

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

ISSUES

I. Whether petitioner's applications for refund of sales tax paid by petitioner for telephone services that petitioner used to gather information from sporting and other events was properly denied.

II. Whether any part of petitioner's applications for refund are barred by the statute of limitations set forth in Tax Law § 1139.

FINDINGS OF FACT

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

The business of Phone Programs, Inc. ("petitioner") is to provide entertainment services and information programs to the public by means of electronic distribution by telephone. Since the early 1980s, when information services that are provided within the context of these programs could be owned and operated by independent vendors, Phone Programs established a relationship with New York Telephone Company wherein it bought telephone service from New York Telephone at a wholesale price pursuant to a tariff regulated by the Public Service Commission. In exchange, companies like Phone Programs enhanced the telephone service to make it a saleable commodity to the general public, and it was presented to the public at a retail price (in this case, double the wholesale rate). Such retail price became subject to sales tax in 1990, when New York State began taxing such telephone services (Tax Law § 1105[c][9]).

The company operates through the use of the Mass Announcement Network Service ("MAS") offered by New York Telephone. The MAS consists of a service and facilities whereby telephone users may, by calling a particular central office designation and number, obtain a

subscriber-provided announcement of up to 57 seconds in duration with an automatic disconnect occurring after one complete announcement. A subscriber to the dedicated MAS is referred to by the Public Service Commission as an "information provider" who leases dedicated facilities and is responsible for providing the recorded announcements. The MAS is accessed by petitioner's customers (who are located in the area codes near New York City, i.e., 212, 516, 718 and 914) by dialing a phone number with a prefix of "976" which is assigned to petitioner. If a customer is located outside such area codes, his or her call would have to include one of the four codes.

The "976" channel assigned to petitioner is able to accept an unlimited number of telephone calls simultaneously, and is able to disseminate the information simultaneously to an endless number of people. Phone Programs pays New York Telephone 20 cents each time its channel is reached by the general public, for the privilege of having exclusive use of the particular channel. New York Telephone bills the calling public 40 cents (which is set by tariff), including Federal, State and local taxes, as agent for Phone Programs. New York Telephone remits the difference to petitioner, which becomes its profit.

Petitioner provided the testimony of Jay Levy, an employee of petitioner's representative, David Isaacson, Esq., who bears significant knowledge and expertise in the area of telephone usage, equipment connected with telephones, and the communications field. Mr. Levy spent a substantial amount of time both at petitioner's business location on Third Avenue in New York City, later at petitioner's facilities in Elmont, Long Island, and in the field where information is gathered, Madison Square Garden, Yankee Stadium, Shea Stadium, Belmont Race Track and

Aqueduct Race Track, attempting to understand the nature of petitioner's business and how it operated.

During the years in question, petitioner, through the MAS, provided services known as "Sports Phone," "Sports Extra" and "Coach Kurt." To accomplish the acquisition of the information which is the subject of these programs, Phone Programs employs two categories of individuals, an anchor or narrator, who was generally located at petitioner's office, and reporters or field representatives, who were observed in the "field" where the information is gathered. The field personnel are responsible for the connection of a telephone line that is paid for by petitioner, which is connected to the facility's sound system or to a microphone where an announcer or broadcaster from the event is giving a play-by-play description of what is happening. In a racing event, for example, the information was taped on a continuous running tape where an editor at Phone Programs would extract audio clips to be used in the next 57 second piece. Live information, sounds and audio signals are transmitted by means of the telephone line, and a tape recorder dedicated to each of the incoming lines records the information from the event. A dedicated line at Phone Programs is used to send the final 57 second announcement to the Erickson Switch at New York Telephone Company, where the material is recorded and ready for dissemination to the public. Petitioner's narrator or announcer would simply introduce the information being provided, and the "actuality," the actual voice or sound from an event, would be heard. The phone lines used from such locations as Madison Square Garden or various race tracks are billed to petitioner, and it is the sales tax on such lines that is the subject of petitioner's refund claim herein.

Petitioner filed eight applications for refund, which are identified by six claim numbers assigned by the Division of Taxation ("Division"):

a) Claim Number 1995120136, filed on or about November 28, 1995, covers petitioner's claim for refund for 1991 in the amount of $9,614.59 plus interest.

b) Claim Number 1995120136, filed on or about November 28, 1995, covers petitioner's claim for refund for 1992 in the amount of $20,853.69 plus interest.

c) Claim Number 309047, filed on or about August 31, 1993, covers petitioner's claim for refund for 1990 in the amount of $1,432.21 plus interest.

d) Claim Number 1995090282, filed on or about April 14, 1993, covers petitioner's claim for refund for 1990 in the amount of $4,693.21 plus interest.

e) Claim Number 1995040703, filed on or about April 14, 1995, covers petitioner's claim for refund for 1992 in the amount of $11,574.70 plus interest.

f) Claim Number 311396, filed on or about October 29, 1993, covers petitioner's claim for refund for 1991 in the amount of $11,773.88 plus interest.

g) Claim Number 311396, filed on or about November 1, 1993, covers petitioner's claim for refund for 1992 in the amount of $5,432.52 plus interest.

h) Claim Number 303986, filed on or about March 27, 1993, covers petitioner's claim for refund for 1990 in the amount of $27,131.76 plus interest.

Although the initial applications for refund were based on differing legal theories, such applications were amended to reflect the same basis for refund, i.e., Tax Law § 1101(b)(4) and 20

NYCRR 526.6(c)[1], the resale exclusion. Petitioner's claim for refund in each instance is based on the following, in pertinent part:

> In the course of this taxpayer's business operations, it purchases personal property or services which it intends to sell, either in the form in which purchased, or as a component part of other property or services. Since the property or services which the taxpayer has purchased should be considered as purchased for resale, it is therefore not subject to tax until it has been transferred to the customer.
>
> This taxpayer exclusively utilizes the tariffed billing and collection services of NYNEX (New York Telephone) for the purposes of billing and collecting for its taxable services and remitting the appropriate taxable amounts to the New York State Department of Taxation and Finance.
>
> This taxpayer buys various telephone services to secure audio items and interviews which become component parts of the taxable retail services it sells to the general public.
>
> Copies of the telephone service charges which are the subject of this refund application are attached hereto.

Petitioner executed consents extending the statute of limitations for the assessment of sales and use tax in this matter such that taxes due for the taxable periods June 1, 1991 through February 28, 1994 could be determined at any time on or before March 20, 1996.

Refund denial letters were issued in response to each of the applications filed, in coordination with the six claim numbers. Five of the claims were denied by correspondence dated April 2, 1996 and Claim Number 309047 was denied by correspondence dated December 16, 1996. The denial explanation which responds to the claims (as amended) provides as follows:

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[1] Although petitioner's refund claims and brief indicate reliance upon Regulation § 526.6(4)(c), it is clear from petitioner's argument that the reference was intended to be Regulation § 526.6(c), the resale exclusion.

> Your claim for a refund of sales tax is being denied in full.
>
> Refund is denied as it was determined on audit that vendor makes sales of information services and not telephone service.
>
> This determination denying your claim in full will, according to section 1139(b) of the Sales and Use Tax Law, be final and irrevocable unless you apply for a hearing. If you decide to appeal this determination, complete the enclosed TA-9.1, Request for Conciliation Conference, and mail it within 90 days of the date of this letter.

A Conciliation Conference was conducted in this matter on November 21, 1996, concerning tax years 1990, 1991 and 1992, before the Bureau of Conciliation and Mediation Services. The statutory notices, referred to as the "refund denial dated April 2, 1996 and December 16, 1996," were sustained by Conciliation Order CMS No. 155964/159055 dated March 21, 1997.

A timely petition was filed on April 7, 1997 with the Division of Tax Appeals, seeking review of the six notices denying eight applications for refund of sales tax paid during the period January 1990 to December 1992. The Division of Taxation filed its answer on June 12, 1997.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

After examining Tax Law § 1101(b)(4) and § 1105(b), the Administrative Law Judge held that petitioner was not entitled to a resale exclusion on its purchases of telephone service because petitioner did not resell the telephone service to its customers, only the information it received by means of that medium. The Administrative Law Judge determined that petitioner did not pay tax on its acquisition of the information/entertainment material, only the telephone service (Tax Law § 1105[b]) it used to acquire the information. On the other hand, when petitioner sold the information as entertainment to its customers, which was coincidentally delivered by means of

the same medium, it was subject to sales tax under Tax Law § 1105(c)(9). The Administrative Law Judge drew a distinction between the telephone services used to acquire the information and the telephone services used to deliver the entertainment to its customers. The Administrative Law Judge found that the two telephone services were separate and distinct and one was not purchased and then resold to customers as a part of the service provided, as contemplated by the resale exclusion in Tax Law § 1105(b) and the regulation at 20 NYCRR 526.6(c). Rather, the Administrative Law Judge characterized the telephone services purchased by petitioner as a cost of doing business more accurately categorized as an item of overhead.

Based on this reasoning, the Administrative Law Judge determined that the applications for refund were properly denied by the Division and deemed it unnecessary to address the issue raised by the Division with respect to the statute of limitations.

ARGUMENTS ON EXCEPTION

Petitioner argues that the broad definition of telephone services, coupled with the exceptions found throughout the Tax Law for property acquired for resale, demonstrate that it should not be subject to tax on the telephone services it purchased.

Relying on TSB-M-90(10)S for the definition of "telephone service," petitioner contends that its reception and rebroadcast of data used in its entertainment service qualifies as providing a telephone service. Petitioner cites ***Matter of Burger King v. State Tax Commn.*** (51 NY2d 614, 435 NYS2d 689) and ***Servomation Corp. v. State Tax Commn.*** (51 NY2d 608, 435 NYS2d 686) for the proposition that items of personal property that comprise a critical element of the final product sold to customers meets the definition of property purchased for resale, comparing the containers, cups, lids, wrappings and french fry sleeves purchased by fast food restaurants with

the telephone services petitioner purchases. Although petitioner agrees that the service it provides to its customers is subject to the surcharge in Tax Law § 1105(c)(9)(ii), it argues that the imposition of this tax on its service but not the service which provides it with its raw data demonstrates that the raw data is not an information or entertainment service. Petitioner's theory is that this indicates the telephone service which transmits the data is property which comprises a critical element of the final product and, therefore, must be seen as purchased exclusively for resale and qualifies for the exemption from tax.

The Division of Taxation argues that the telephone service purchased by petitioner was completely different from the service sold by petitioner to its customers, the former taxable under Tax Law § 1105(b) and the latter taxable under Tax Law § 1105(c)(9). In addition, the telephone service purchased by petitioner was not resold as such to its customers. The Division believes that the telephone service in issue was ended when petitioner discontinued the call to the sports facility and the charge petitioner incurred was for transmission service which was not resold.

The Division believes petitioner's reliance on ***Burger King*** is misplaced. The analogy from the containers in ***Burger King*** as a critical element of the product sold to the telephone service purchased by petitioner in this case fails, says the Division, because the telephone was not critical, only an item of overhead expense necessary for the operation of the business.

The Division notes that the Tax Law provides an exemption from sales tax for the resale of telephone service in section 1105(b), but contends that this exclusion is for the resale of telephone services as such (20 NYCRR 527.2[e]) and not the use of telephone service in providing other services.

In post oral argument correspondence, the Division argued that the recent Tennessee case of ***Equifax Check Servs. v. Johnson*** (Tennessee Chancery Court, No. 95-4077-II, Sept. 2, 1999) supported its position that petitioner was merely the consumer of telephone services which it used to produce its taxable information/entertainment services. In ***Equifax***, the issue was whether Equifax was the user or consumer of telecommunications services rather than the provider of such services to its customers for a consideration subject to tax. The Tennessee court held that although the telecommunications services were essential to Equifax's check guarantee business, the services were merely a means for delivering the check services and, therefore, just incidental to the provision of those services. Only when the telecommunication services themselves are being furnished for a consideration are they taxable.

Petitioner responded to the ***Equifax*** case saying that it confirms its belief that the Division continues to misunderstand its position. Petitioner distinguishes itself from ***Equifax*** by noting that it utilizes the telecommunications service as a "resold, value-added telecommunications service."

OPINION

We will first begin with the jurisdictional issue raised by the Division in its answer at hearing and then again in its brief before the Administrative Law Judge. The Division argued that Tax Law § 1139(a) barred part of three applications for refund filed by petitioner herein. Tax Law § 1139(a) provides that applications for refund of tax paid to vendors that sold the telephone service to petitioner must be filed within three years from the date when the tax was payable to the tax commissioner. The Division calculated the dates based upon the following assumptions:

- That the telephone companies selling the services to petitioner were monthly filers;

- That these companies' returns and payments were due within 20 days of the end of the reporting period (month) (Tax Law § 1137);

- That the time for filing an application for refund was due within three years from the date the tax was payable.

There was no evidence of the monthly filing of the telephone service vendors submitted by the Division to substantiate their argument. Without any evidence on the filing status of each of the providers, the Division has failed to establish a date from which the statute of limitations began to run. Therefore, we deem all of petitioner's applications for refund timely filed.

As a general rule, statutes which provide for exemptions from tax must be strictly construed, and the taxpayer must clearly demonstrate that it is entitled to the exemption (***Matter of Lever v. New York State Tax Commn.*** (144 AD2d 751, 535 NYS2d 158). Petitioner has not done so in this case. We find most convincing the argument that petitioner is not a telecommunications company but an entertainment business providing information to its customers. Incidental to the provision of its service, it consumes telephone services upon which it pays sales tax. We do not believe that petitioner resells this telephone service to its customers nor do we believe that is what its customers believe they are purchasing. They call to hear sports news and features, not to purchase telephone services. The resale exclusion for utility services demands that the services be resold as utility services, i.e., telephone services (20 NYCRR 526.6[c]; 527.2[e]). Clearly, this was not the case here.

Petitioner used the telephone service it purchased to gather the information it used to make its product. It was an incidental expense of overhead which enabled it to collect raw materials. Once the materials were acquired, the telephone service ended. It no longer existed as a conduit

through which data passed to petitioner's offices. When it was transmitted for broadcast, the telephone service was no longer part of the product.

In ***Matter of MGK Constructors*** (Tax Appeals Tribunal, March 5, 1992), we held that guard services purchased by petitioner did not qualify for the resale exclusion because they were merely expenses of overhead incidental to the building of a tunnel and were not resold to the City of New York. The instant case presents an indistinguishable set of facts, where overhead expense (telephone service used to acquire the information) was merely incidental to the product sold to consumers. Therefore, we conclude that petitioner has not established a right to the exclusion.

We have carefully examined all of the remaining arguments made by petitioner and find that they were fully and correctly addressed by the Administrative Law Judge.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Phone Programs, Inc. is denied;

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

3. The petition of Phone Programs, Inc. is denied; and

4. The Division of Taxation's denials, dated April 2, 1996 and December 16, 1996, of the eight applications for refund, identified by six claim numbers, are sustained.

DATED: Troy, New York
April 6, 2000

/s/Donald C. DeWitt
Donald C. DeWitt
President

/s/Carroll R. Jenkins
Carroll R. Jenkins
Commissioner

/s/Joseph W. Pinto, Jr.
Joseph W. Pinto, Jr.
Commissioner