STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
10 ELLICOTT SQUARE COURT CORPORATION	:	DECISION
for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9 of the Tax Law for the Years 1983 and 1984.	:	

Petitioner, 10 Ellicott Square Court Corporation, 210 Ellicott Square, Buffalo, New York 14203, filed an exception to the determination of the Administrative Law Judge issued on September 9, 1988 with respect to its petition for redetermination of a deficiency or for refund of corporation franchise tax under Article 9 of the Tax Law for the years 1983 and 1984 (File No. 803177). Petitioner appeared by Paladino, Quinlivan, Eoannou, Cavan & Reich, Esqs. (Patrick J. Quinlivan, Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Deborah J. Dwyer, Esq., of counsel).

Petitioner filed a brief on exception. The Division filed a letter in lieu of a brief. Oral argument at the request of the petitioner was heard on May 23, 1989.

ISSUE

Whether the Division of Taxation properly determined that petitioner was a "utility" as defined in Tax Law section 186-a and if so, whether its receipts from submetering of electricity to its tenants were "gross operating income" subject to tax under Tax Law section 186-a.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge and such facts are stated below. We find additional facts as indicated below.

On May 30, 1985 petitioner, 10 Ellicott Square Court Corporation, filed with the Division a letter requesting a refund of tax paid under section 186-a of the Tax Law for the months of November and December of 1983 and the entire year 1984, including a prepayment for 1985.

By letter dated December 9, 1985, the Division denied petitioner's refund claim.

Petitioner is a New York corporation which acts as a managing and leasing agent of a 10-story, 300,000 square foot office building in Buffalo, New York, commonly known as the "Ellicott Square Building". Petitioner isthe designated fiduciary of Ellicott Group, a general partnership which owns the Ellicott Square Building. Petitioner operates the property for the partnership and has full authority in all matters involving the operation of the property.

The Ellicott Square Building is a multi-tenant office building with over 125 individual tenancies. Its varied tenants include individuals, law firms, and state and local government agencies.

The Niagara Mohawk Power Corporation supplies electricity to the Ellicott Square Building via one main service line. This main line of service is then broken down by the building's equipment into individual lines for each tenancy. Niagara Mohawk bills petitioner for the total amount of electricity consumed by all of the Ellicott Square Building's tenancies; that is, for the total amount of electricity which is delivered to the building via the main service line.

Petitioner recovers its costs for electricity consumed by the tenants in one of two ways depending upon the size of the tenancy:

> a) Tenancies having less than 1,000 square feet of space pay a flat rental to petitioner which includes an estimated cost of the electricity consumed by that tenant.
>
> b) Tenancies having more than 1,000 square feet of space are submetered by petitioner and then billed by petitioner monthly for their proportionate share of the Niagara Mohawk charge. No additional costs are charged.

A typical lease from the period at issue describes the submetering and sub-billing arrangement as follows:

> "40. Electric current consumed for general lighting, operation of Tenant's office appliances and for the operation of air conditioning equipment shall be submetered and consumption charges paid for by the Tenant to the Landlord in the following manner: It is agreed that said electric charges shall be at Landlord's average cost per kilowatt hour which shall be determined by dividing the total cost of electricity for the building, including

> demand charges and taxes, excluding late charges, if any, by the total building consumption thereby producing Landlord's average cost per kilowatt hour. The Tenant's kilowatt hour consumption, as measured in the submeter, shall then be multiplied by Landlord's average cost per kilowatt hour, as determined aforesaid, thereby producing Tenant's electric charges. Landlord shall provide electric bills from the local utility company, for the building of which the demised premises forms a part, used to determine Tenant's average cost per kilowatt hour. Tenant shall have the right to accompany the Landlord or Landlord's representative during the reading of the submetering device or devices. It is further agreed and understood that no electric current consumption except that which is consumed in the demised premises shall be registered in the submetering device as used by the Tenant."

In addition to payments for usage of electricity, submetered tenants also pay a gross rental which does not include electric.

Approximately 65 percent of petitioner's tenants are submetered.

In addition to the facts found by the Administrative Law Judge, we find that petitioner realized no profit on its system of submetering and sub-billing of electricity with its tenants and that Niagara Mohawk Corporation paid the tax imposed by Tax Law section 186-a on all electricity sold to petitioner. We also find that petitioner attempted to arrange for an adjustment to its bill from Niagara Mohawk by deducting the "Gross Revenue Tax Adjustment" for the portion of the electricity resold by petitioner. Niagara Mohawk refused to make any such adjustment.

OPINION

Section 186-a of the Tax Law imposes a tax upon the gross income of every utility doing business in New York which is subject to the supervision of the State Department of Public Service and a tax upon the gross operating income of "every other utility" doing business in New York.

"Utility" is defined by the statute as every person subject to the supervision of the State Department of Public Service and also:

> "every person (whether or not such person is subject to such supervision) who sells...electricity...delivered through...wires, or furnishes...electric...service, by means of...wires; regardless of

> whether such activities are the main business of such person or are only incidental thereto, or of whether use is made of the public streets..." (Tax Law § 186-a[2][a]).

Tax Law section 186-a(2)(d) defines "gross operating income" in part as follows:

> "[T]he 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 . . . electricity . . . or in or by reason of the furnishing for each consumption or use of . . . electric . . . service in this state, including cash, credits and property of any kind or nature . . ." (emphasis added).

20 NYCRR 500.2(a) and (b) define the two types of utilities described in section 186-a as utilities of the first and second class, respectively.

> "(2) Utilities in the second class are mainly those which, generally speaking, would not be classed as utilities but which are made utilities by statute for the purpose of this tax. Ordinarily, although there are exceptions, such as omnibuses, utilities in this group resell utility services which are purchased from utilities in the first class (20 NYCRR 500.2[b][2]).[1]

The Administrative Law Judge determined that petitioner was a utility within the meaning of Tax Law section 186-a; a "second class utility" as defined by the Division's regulations (20 NYCRR 500.2[b][2][3]) and that the receipts received by petitioner from providing electricity to the tenants of its office building were subject to the tax pursuant to section 186-a.

On exception the petitioner asserts that it is not subject to section 186-a since the history of the section reveals that the term "sale" was not intended to include a system of simple reimbursement between landlord and tenant.

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[1]The questions and answers in 20 NYCRR 500.2(b)(3) provide examples of utilities in this class:

Question 1: Is the owner or lessee of a hotel, apartment house or office building, who purchases gas, electricity, steam, water, refrigeration or telephony and resells any part or all of the same to tenants, subject to tax? Answer: Yes.

Question 2: A tenant in a hotel, apartment house, or office building pays a lump sum as monthly rental, which includes gas, electric, steam, water and telephone services or any one or more of such services. Is the landlord subject to the tax? Answer: No. The landlord becomes taxable only if he sells one or more of such utility services at identifiable, flat or metered rates."

Petitioner contends that its submetering and billing system was intended solely as a mechanism for equitably and fairly allocating the building's costs for electrical service and that since petitioner realized no profit on its system, the transactions between it and its tenants were not sales. Petitioner contends in the alternative that even if petitioner's acts constitute a "sale", the definition of "gross income" and "gross operating income" in section 186-a leads to the conclusion that only "profits" from utility sales are to be included under gross operating income for those entities which are not "ordinary utilities." Petitioner argues that "gross income" includes receipts received in any sale ". . . whether or not such sale is made or such service is rendered for profit." In contrast, the definition of "gross operating income" does not state that receipts are taxable without regard to profit. Petitioner argues that it was the Legislature's expressed intent to tax only those "other utilities" which were in competition with utilities, and therefore, the absence of this provision concerning profit indicates that only sales for a profit are taxable.

Petitioner also contends that the imposition of tax upon it pursuant to Tax Law section 186-a results in an unfair double taxation, for petitioner's payments to Niagara Mohawk included, in addition to the charges for electrical service, a "Gross Revenue Tax Adjustment" pursuant to Niagara Mohawk's obligations under Tax Law section 186-a.

The Division relies on the determination of the Administrative Law Judge.

We agree with the determination of the Administrative Law Judge that petitioner is a "utility" within the meaning of section 186-a(2)(a) of the Tax Law and that the receipts at issue are included in "gross operating income" as defined in section 186-a(2)(d) of the Tax Law. However, we reverse the Administrative Law Judge's conclusion that petitioner is not entitled to a refund for the reasons set forth below.

We deal first with whether petitioner is a utility within the purview of section 186-a of the Tax Law. We conclude it is. As originally enacted, (L 1937, ch 321), section 186-a of the Tax Law provided for a tax ". . . equal to two percentum of its gross income . . . upon every utility

doing business in this state which is subject to the supervision of the state department of public service . . . and a tax equal to two percentum of its gross operating income upon every other utility doing business in this state . . ." (emphasis added).

The term "utility" was defined as including "every person . . . who shall engage in the business of selling . . . electricity, [and] . . . water, . . . delivered through mains, pipes or wires, or of furnishing. . . electric . . . [and] water . . . service by means of mains, pipes, or wire; . . . ." The term "gross operating income" was defined to " . . . mean and include receipts received in or by reason of any sale made to persons for ultimate consumption or use by them of gas, electricity, steam, water, refrigeration, telephony or telegraphy, or in or by reason of the furnishing to persons for such consumption or use of . . . electric . . . water . . . service in this state, . . . " (emphasis added).

The Court of Appeals in Matter of 339 Central Park West Inc. v. Graves (260 App Div 265, 21 NYS2d 93, affirmed 284 NY 691 [1940]) held that section 186-a of the Tax Law was not intended to apply to an apartment house owner who purchased electricity from a public utility, submetered it and resold the same to its tenants since the apartment house was not a utility.

By Chapter 137 of the Laws of 1941, section 186-a was amended to provide among other things, that the term "utility" includes persons who sell or furnish gas, electricity, etc. ". . . regardless of whether such activities are the main business of such person or are only incidental thereto, or of whether use is made of the public streets; . . . ."[2] The stated intent of the amendment was "to include within the purview of the section 186-a tax persons and corporations which were directly in competition with ordinary utilities." (L 1941, ch 137, § 1 [emphasis added].)

In Lacidem Realty Corporation v. Graves, et al (288 NY 354 [1942]) the Court of Appeals sustained the validity of the amended section 186-a as it was applied to taxing a

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[2]The amendment was apparently made to overrule the Court of Appeals' holding in Matter of 339 Central Park West v. Graves, 284 NY 691 (see footnote at page 431 of Matter of Quotron v. Gallman, 39 NY2d 430).

landlord's receipts from his incidental business activity of sub-metering electric current to tenants.[3] Based on this decision, we conclude that petitioner is a utility and the receipts from petitioner's submetering activities are part of gross operating income, under section 186-a of the Tax Law.

We agree with petitioner's assertion, however, that only those amounts received by a reseller of electricity over and above the cost of the electricity to the reseller are taxable under section 186-a. This is consistent with the Division's interpretation of section 186-a, as expressed in its instructions to taxpayers and its regulations. These sources indicate that the Division's policy is to allow utilities in the second class a deduction for the cost of utilities resold on which the 186-a tax was paid by the utility which sold the commodity to the taxpayer.

This policy is set forth in the 1987 and 1988 Form CT-186-A-I, "Instructions for Form CT-186-A Tax Return for Gross Operating Income." The instructions follow the language of the statute by requiring that all receipts from the sale or furnishing of each commodity for ultimate consumption or use within the state be entered on the return. However, a deduction is allowed for the taxpayer's cost of utilities resold on which the tax under section 186-a has been paid by the utility which sold the commodity to the taxpayer. The result, in effect, is to require the taxpayer to pay tax on only the net receipts.

For periods prior to 1987 the Division's policy of allowing a deduction for the cost of utilities resold is articulated in regulations and policy memoranda for specific 186-a second class utilities. Hotels or apartment houses supplementing the telephone service supplied by the telephone company have been required since 1962 to pay tax only on their supplemental charge (20 NYCRR 502.3[d]). Resellers of telephone services have been allowed a deduction for the cost of resold services on which the 186-a tax was paid by the underlying carrier since the tax year 1987. This policy was the result of an agreement between the Division and telephone

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[3] Matter of Lacidem Realty Corp. v Graves (288 NY 354, 43 N.E.2d 440) was decided with 436 West 34th Street Corp. v. McGoldrick (288 NY 346), which contains the full rationale of the Court's decision.

companies in 1987 (Dept. of Taxation, Technical Directives Memo, CC-87-5, DOC-87-6, December 22, 1987)[4].

In this proceeding the Division has not addressed the fact that the 1987 and 1988 instructions allow a deduction for the cost of the utilities resold and certainly has not argued that this deduction was not available to resellers of electricity for prior years. Given the fact that certain second class utilities were allowed such a deduction for prior years, we conclude that such a deduction is also applicable to resellers of electricity. Since petitioner has established that its seller paid tax on the electricity provided, petitioner is entitled to deduct its cost for the electricity in computing its gross operating income.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioner, 10 Ellicott Square Court Corporation, is granted;

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

3. The petition of 10 Ellicott Square Court Corporation is granted; and

4. The Division of Taxation's denial of 10 Ellicott Square Court Corporation's refund claim is reversed.

DATED: Troy, New York
August 24, 1989

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

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

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

[4]The Legislature amended section 186-a in 1989 to, in effect, codify this agreement (L 1989, ch 61, § 313).