STATE OF NEW YORK

STATE TAX COMMISSION

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| In the Matter of the Petitions of MANHATTAN CABLE TELEVISION, INC. 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 January 1, 1974 through February 28, 1979. | DECISION |

Petitioner, Manhattan Cable Television, Inc., 120 East 23rd Street, New York, New York 10010, filed petitions 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 January 1, 1974 through February 28, 1979 (File Nos. 21691 and 39474).

A formal hearing was held before Frank A. Landers, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on August 21, 1984 at 9:15 A.M., with all briefs to be submitted by December 24, 1984. Petitioner appeared by Ronald W. Meister, Esq. The Audit Division appeared by John P. Dugan, Esq. (Irwin A. Levy, Esq., of counsel).

ISSUES

I. Whether the Audit Division properly imposed sales and use tax on petitioner's purchases of equipment, or whether such purchases were exempt from tax by virtue of Tax Law section 1115(a)(12).

II. Whether petitioner is liable for sales or use tax on purchases of cable and equipment to be installed in the public way.

III. Whether petitioner is liable for sales or use tax on payments to subcontractors who installed cable and equipment in the public way.

IV. Whether petitioner is liable for sales or use tax on payments to subcontractors for installing cable and equipment inside the subscribers' buildings.

V. Whether the Audit Division erroneously disallowed as exempt from tax certain payments to subcontractors for performing "hook-ups" inside the subscribers' apartments.

VI. Whether the purchase by petitioner of a private telephone interconnect system is exempt from the sales and use tax as the purchase of a capital improvement to real property.

FINDINGS OF FACT

1. Pursuant to a contract with the City of New York dated August 18, 1970, petitioner, Manhattan Cable Television, Inc. ("MCTV"), formerly Sterling Information Services, Ltd., was granted the franchise and right to install, operate and maintain a community antenna television system (cable television system) in the southern half of Manhattan. At all times during the period at issue, MCTV operated as a cable television company, pursuant to said franchise, providing entertainment programs and information services to its subscribers. In consideration for the franchise, which was to continue for a period of twenty (20) years, MCTV pays the City of New York 5 percent to 10 percent of gross revenues on a quarterly basis.

2. On May 5, 1977, MCTV filed an Application for Credit or Refund of State and Local Sales or Use Tax covering the period January 1, 1974 through January 1, 1977 and claiming a refund of $107,552.13 in sales tax paid, pursuant to section 1105 of the New York Tax Law, on equipment purchased for use in providing cable television service to customers. It was then the position of MCTV that the provisions of section 1115(a)(12) of the Tax Law would be applicable

to certain purchases of equipment which it utilizes and that it would be entitled to a refund of all sales taxes paid thereon if the New York courts decided that (i) MCTV furnishes a telegraph or telephone service subject to the sales tax; or (ii) MCTV owns or operates telegraph or telephone lines; or (iii) MCTV is engaged in providing telegraphic or telephonic communication and is subject to Public Service Commission jurisdiction.

3. On September 23, 1977, the Audit Division denied petitioner's refund claim with the following explanation:

> "It has been determined through court proceedings, that you are not engaged in the activities of telephony and telegraphy within the meaning and intent of Section 1105(b) of the Tax Law.
>
> Because of this determination, you do not qualify for the exemption from the tax on your purchases as requested by you under Section 1115(a)(12) of the Tax Law."

4. On March 19, 1979, MCTV filed two applications for credit or refund of state and local sales or use tax. The first application requested a refund of $105,623.98 and covered the period January 1, 1977 through December 31, 1978. The second application amended MCTV's May 5, 1977 application for the period January 1, 1974 through January 1, 1977 by increasing the amount of refund claimed to $125,829.02. Both applications covered the purchase of certain equipment and contained the notation that "(d)ocumentation in support of this application has been submitted to the Tax Appeals Bureau." Therefore, the total amount of refund claimed by MCTV is $231,453.00 for the period January 1, 1974 through December 31, 1978.

5. On July 5, 1979, MCTV filed a perfected petition wherein it contended that:

> "The determination of this matter should await the end of litigation in Manhattan Cable Television, Inc. v. Freyberg. At issue in that action is whether the cable television equipment of the very petitioner here is telephone and telegraph equipment and therefore

subject to real property tax under Section 102(12)(d) (sic) of the Real Property Tax Law. The Supreme Court, New York County, held that the equipment was so subject to the tax and its decision has been affirmed by the Appellate Division, First Department. Manhattan Cable has obtained leave from the Appellate Division to appeal to the Court of Appeals and is preparing its appeal. This case concerns the nature of Manhattan Cable's equipment and, as such, is of particular relevance to the question at issue in this petition."

6.(a) On April 6, 1976, an opinion of counsel was issued by the Deputy Commissioner and Counsel of the Department of Taxation and Finance stating that the provision of cable television services was "telephony or telegraphy" within the meaning of section 1105(b) of the Tax Law.

(b) In accordance therewith, the Audit Division issued Sales Tax Information Letter No. 46 which provided as follows:

"An Opinion of Counsel, effective June 1, 1976, subjects receipts from the sale of cable television services to New York State and local sales and use taxes (including Schedule B Taxes). This reversed a prior opinion of Counsel dated March 29, 1973.

"Counsel's Opinion is based on the premise that cable television companies, which furnish their services by transmission of pictures and sound, are engaged in the activities of telephony and telegraphy within the meaning and intent of Section 1105(b) of the Tax Law. Accordingly, receipts from the sale of such services, including charges for installation of wires and other devices used in furnishing such services, are subject to tax pursuant to Section 1105(b) of the Tax Law. As installation charges have been held subject to tax under prior opinions, there is no change in the sales tax status of such charges."

(c) Regulation section 20 NYCRR 527.2(d)(2), which took effect on September 1, 1976, provided the term "telephony and telegraphy" includes use or operation of any apparatus for transmission of sound, sound reproduction or coded or other signals. Example 6 of said section provided as follows:

"A company transmits signals for television programs, over wires to a customer's premises. It both relays signals for programs from other sources and generates signals for programs it originates. The transmission of such signals constitutes telephony or telegraphy."

(d) Regulation section 20 NYCRR 528.13(f)(2), which explains the exemption in section 1115(a)(12) of the Tax Law in regard to telephone and telegraph equipment and which took effect on June 1, 1977, provided at example 3:

> "A cable television company purchases equipment that is used for receiving incoming signals, duplicating them and transmitting new signals to subscribers. Such equipment is exempt."

(e) On November 10, 1976, the Supreme Court, Special Term, Albany County, in N.Y.S. Television Assn. v. Tax Comm., found that a determination of the State Tax Commission that cable television services fell within the definition of telephony and telegraphy within the meaning of section 1105(b) of the Tax Law, is without statutory basis and hence arbitrary and capricious. The court further declared regulation sections 20 NYCRR 527.2(d)(2) and 528.13(f)(2) null and void. On August 4, 1977, the Appellate Division affirmed the holding of the Supreme Court.

(f) On May 23, 1979, the Audit Division's Technical Directives Section issued audit guidelines for cable television and other transmission service companies. The preface to the section of said guidelines on purchases provided:

> "The following purchases made by Cable Television and other Transmission service companies (master antenna, community antenna and Muzak) are subject to applicable New York State and Local Tax. The exemptions provided in Section 1115(A)(12) (sic) and 1210(A)(1) (sic) of the Tax Law do not apply, even during the period June 1, 1976 to August 4, 1977 when these services were deemed to be subject to tax pursuant to Section 1105(b) of the Tax Law." (Emphasis added.)

(g) Regulation sections 527.2(d)(2) and (3) and 528.13(f)(2) and (5) were subsequently amended, effective September 15, 1980, to conform to the aforementioned court decisions.

(h) On March 25, 1980, the Court of Appeals, in the Matter of Manhattan Cable TV Services v. Freyberg, held that equipment which was owned by Community

Antenna Television Corporations, which was situated on its own leased premises and premises of subscribers and which consisted of cables and appurtenances thereto, was not subject to taxation under section 102 [subd. 12, par. (d)] of the Real Property Tax Law.

7. On May 20, 1981, as the result of a field audit, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due under Articles 28 and 29 of the Tax Law against petitioner for taxes due of $521,452.78, plus interest of $155,297.86, for a total amount due of $676,750.64 for the period December 1, 1975 through February 28, 1979.

8. Petitioner, by signature of its secretary, Carolyn K. McCandless, executed a consent extending the statute of limitations for assessment of sales and use taxes for the period December 1, 1975 through February 28, 1979 to June 20, 1981.

9. The auditor determined that petitioner failed to pay sales or use tax on material and equipment purchases of $2,980,757.44 and on fixed asset purchases of $929,668.76. The auditor also found that petitioner failed to pay sales or use tax on payments to three (3) subcontractors as follows:

| Subcontractor | Payments |
|---|---|
| Petrocelli Electric Co., Inc. | $ 738,863.02 |
| Antenna & Communications Corp. | 691,553.12 |
| Rae Mar Installation, Inc. | 1,177,317.41 |
| Total Payments | $2,607,733.55 |

Therefore, the auditor determined additional purchases subject to use tax of $6,518,159.75 and additional taxes due of $521,452.78.

10. In providing cable television services, MCTV connects its subscribers' television sets to a coaxial cable which runs from "headend" or main distribution point of the service located at Columbus Circle through a distribution system of cables, amplifiers and filters located in conduits under the public

streets to the subscribers' premises. Petitioner purchased the cables, amplifiers and filters and furnished them to the aforementioned subcontractors for installation.

11.(a) Petrocelli Electric Co., Inc. installed the distribution system, also known as the trunk system, in the conduits under the city streets. At times, the installation of the trunk system required trenching the streets in order to lay the cable. MCTV intended that the cable become a permanent installation to real property. At all times during the period at issue and at the present time, MCTV paid real property taxes to the City of New York based on the number of miles of cable which it installed. At the present time, the real property taxes are imposed pursuant to section 102.12(h) of the Real Property Tax Law which includes within the definition of real property, "(s)pecial franchises as defined in subdivision seventeen of this section." Subdivision seventeen provides, in pertinent part, that:

> "17. 'Special franchise' means the franchise, right, authority or permission to construct, maintain or operate in, under, above, upon or through any public street, highway, water or other public place mains, pipes, tanks, conduits, wires or transformers, with their appurtenances, for conducting water, steam, light, power, electricity, gas or other substance. For purposes of assessment and taxation a special franchise shall include the value of the tangible property situated in, under, above, upon or through any public street, highway, water or other public place in connection therewith...".

(b) Section 19 of the franchise contract provides the following in the event of cancellation or expiration of the contract:

> "(d) If all or any part of the streets within the District are closed or discontinued as provided by statute, then this franchise, and all rights and privileges hereunder with respect to said streets or any part thereof so closed or discontinued, shall cease and determine upon the date of the adoption of the map closing and discontinuing such streets, and the Company shall not be entitled to damages from the City due to the closing or discontinuance of such streets or for injury to any part of the System in the streets or for the removal or relocation of the same.

* * *

"(f) Upon cancellation or expiration of this franchise, the City shall have the right to purchase the System in accordance with subdivision (g) of this Section, and the Board may direct the Company to cease operation of the System. If the City elects to purchase the System, the Company shall promptly execute all appropriate documents to transfer title to the City, and shall assign all other contracts, leases, licenses, permits and any other rights necessary to maintain continuity of service to the public...

"(g) If this franchise:

(i) is cancelled by the Board by reason of the Company's default, that part of the System located in the streets shall, at the election of the City, become the property of the City without any charge therefor; that part of the System not located in the streets shall, at the election of the City become the property of the City at a cost not to exceed its then book value (i.e. cost less accumulated depreciation) according to generally accepted accounting principles, with a reduction for any damages incurred by the City in connection with such cancellation...

(ii) terminates by expiration of its term, the purchase price to the City for the System shall be its then fair value as determined by arbitration held pursuant to Section 20 of this contract... If the City does not purchase the System, the Company shall remove that part of the System located in the streets and restore the streets to a condition satisfactory to the Commissioner of Highways."

12. With regard to the notice of determination, petitioner is protesting tax of $69,582.42 imposed on payments to subcontractors of $710,435.31 and purchases of equipment of $159,345.00 which it considers improvements to its franchise or capital improvements. Of the refund claim, $68,587.94 represents tax which petitioner claims was paid on improvements to its franchise or capital improvements.

13.(a) After the trunk system is installed in the city streets, the next step in providing cable television service is the installation of cable, building amplifiers, fittings and transformers between the trunk system and the subscribers' buildings and apartments. Although the trunk system may be in the city streets, installation is not made in a building until requested of petitioner.

(b) When requested by the owner of the building or landlord, petitioner is required to install the system in the building and apartments. Lastly, when requested by the tenant or subscriber, petitioner is required to "hook-up" the system which is already in the apartment to the subscriber's television set. On the first bill to the subscriber, petitioner bills the subscriber an installation charge, as a separate item, and collects tax on said installation charge. Also, the amount which MCTV charges a subscriber for the installation of cable television service is fixed by the Board of Estimate of the City of New York, notwithstanding that the actual cost to MCTV may be greater. Antenna & Communications Corp. and Rae Mar Installation, Inc. performed these installations on behalf of petitioner.

(c) The auditor considered payments to the subcontractors for performing the above services as subject to tax with the exception of payments for "hook-up" services. The auditor determined that the installation charge which MCTV added to the subscriber's bill to be the charge for the "hook-up" service only and therefore purchased for resale by MCTV. The auditor determined the other payments for installation services were not purchased for resale and, therefore, subject to tax.

14. Petitioner is protesting tax of $143,381.82, included in the notice of determination, on purchases of $1,792,272.75 of the installation services described above.

15. At the hearing held herein, petitioner presented evidence that the auditor erroneously included as taxable purchases services to perform "hook-ups" inside the subscribers' apartments in the amount of $95,025.16. The tax included in the notice of determination on said amount is $7,602.01.

16. In or about 1979, MCTV purchased from United Telecommunications Corporation a private telephone interconnect system for $177,943.00, less allowable credits, for a total of $97,868.00. The auditor determined a tax due on said purchase of $7,829.44. The telephone system substantially added to the value of the real property and was intended as a permanent installation. There was no evidence presented as to why the auditor considered the purchase of the system subject to tax.

17. In addition to the arguments described above, petitioner is protesting the entire amount of the notice of determination ($521,452.78) and a portion of the denial of the refund claim ($130,612.68) on the basis that since the Department of Taxation and Finance did not seek to impose tax on purchases by cable television companies for the period between April 6, 1976 and September 15, 1980, the Department cannot now impose a tax through a retroactive change in its regulations.

## CONCLUSIONS OF LAW

A. That Tax Law section 1105(b) imposes sales tax upon:

> "The receipts from every sale, other than sales for resale, of gas, electricity, refrigeration and steam, and gas, electric, refrigeration and steam service of whatever nature, and from every sale, other than sales for resale, of 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(a)(12) exempts from sales and use tax receipts from the following:

> "Machinery or equipment for use or consumption directly and predominantly in the production of tangible personal property, gas, electricity, refrigeration or steam for sale, by manufacturing, processing, generating, assembling, refining, mining or extracting, or telephone central office equipment or station apparatus or comparable telegraph equipment for use directly and predominantly in receiving at destination or initiating and switching telephone or telegraph communication, but not including parts with a useful life of one year or less or supplies used in connection with such machinery, equipment or apparatus...".

B. That as above-stated, it was judicially determined that cable television service is not telephony or telegraphy within the purview of section 1105(b). N.Y.S. Cable Television Assn. v. State Tax Comm., 59 A.D.2d 81 (3rd Dept. 1977), affg. 88 Misc.2d 601 (Sup. Ct. Albany Co. 1976). It then follows that equipment used to provide cable television service is not used in the receipt, initiation or switching of telephone or telegraph communication for purposes of the exemption of section 1115(a)(12). Petra Cablevision Corp., State Tax Comm., Jan. 29, 1982. Insofar as the Tax Commission's regulations attempting to impose tax on cable television service were declared null and void, N.Y.S. Cable Television Assn., supra, then any exemption which flowed from the reasoning for the attempted imposition, i.e., that cable television service is telephony or telegraphy, is similarly without effect. The imposition of tax on cable television service and the equipment exemption were inextricably linked. If cable television service does not involve telephone or telegraph communication as the Appellate Division so decided, then the equipment in issue does not involve telephony or telegraphy.

C. That petitioner's position that the Audit Division may not apply the sales and use tax regulations (20 NYCRR 527.2[d][2] and [3] and 528.13[f][2] and [5]) retroactively is without merit. Regulations serve as interpretations of statutes, and the cited regulations merely reflected what the Commission believed the statute permitted.

D. That petitioner's purchases of cable and equipment which were installed in the public way and its payments to subcontractors for installing the distribution system were taxable receipts under sections 1105(a) and 1105(c)(3), respectively. Petitioner is subject to real property tax upon the franchise granted to it by the City of New York, which franchise includes "the value of

the tangible property situated in, under, above, upon or through any public street [or] highway..." (Real Property Tax Law section 102.12[h][17]). Further, the franchise contract provides that if the City chooses not to purchase the system at the expiration of the contract, petitioner must remove the portion of the system located in the streets. Thus, given that the cable system is not considered real property and that it is subject to removal by petitioner, it does not constitute a capital improvement. (See the definition of "capital improvement", section 1101[b][9], added by Laws of 1981, Ch. 471.)

E. That section 1105(c)(3) of the Tax Law imposes a tax upon the receipts from every sale, except for resale, of the services of installing tangible personal property with certain exceptions which are not applicable in this case. Petitioner's payments to subcontractors for installation of the cable television system inside the subscribers' buildings, as well as the subscribers' apartments, were purchases for resale to the subscribers and therefore not subject to tax.

F. That in view of Conclusion of Law "E", Issue V is rendered moot.

G. That the purchase by petitioner of the private telephone interconnect system constitutes a capital improvement and is therefore not subject to tax.

H. That the petitions of Manhattan Cable Television, Inc. are granted to the extent indicated in Conclusions of Law "E", "F" and "G"; and except as so granted, the petitions are denied.

DATED: Albany, New York

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STATE TAX COMMISSION

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