

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition :
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 of :
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 FACILITYSOURCE, LLC :
 : DETERMINATION
 for Revision of Determinations or for Refund of Sales : DTA NOS. 829500 AND
 and Use Taxes under Articles 28 and 29 of the Tax Law : 829501
 for the Period December 1, 2009 through February 28, :
 2017. :

In the Matter of the Petition :
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 of :
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 FACILITYSOURCE NORTHEAST :
 SERVICES, LLC :
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 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, 2013 through February 29, :
 2016. :

Petitioner, FacilitySource, LLC, filed a petition for revision of determinations or for refund of sales and use taxes under articles 28 and 29 of the Tax Law for the period December 1, 2009 through February 28, 2017.

Petitioner, FacilitySource Northeast Services, LLC, filed a petition 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, 2013 through February 29, 2016.

A consolidated formal hearing by videoconference was held before Winifred M. Maloney, Administrative Law Judge, on June 20 through 23, 2023, with all briefs to be

submitted by November 10, 2023, which date began the six-month period for the issuance of this determination. Petitioners appeared by Gordon Rees Scully Mansukhani LLP (Michael S. Marino, Esq., of counsel) and the Division of Taxation appeared by Amanda Hiller, Esq. (Eric R. Gee, Esq., of counsel). After reviewing the entire record in this matter, Winifred M. Maloney, Administrative Law Judge, renders the following determination.

ISSUES

- I. Whether petitioners' motion to strike or for an order of preclusion should be granted.
- II. Whether the notices of determination issued in these consolidated matters had a rational basis.
- III. Whether the Division of Taxation erred in determining that petitioners' facilities management services are taxable as sales of prewritten software.
- IV. Whether, in the alternative, petitioners' facilities management services are subject to tax pursuant to Tax Law § 1105 (c) (1).
- V. Whether, in the alternative, petitioners' facilities management services are subject to tax pursuant to Tax Law § 1105 (c) (5).

FINDINGS OF FACT

The parties entered into stipulations of facts in connection with these consolidated matters. Such stipulations of facts, as modified, have been substantially incorporated into the findings of fact set forth herein.

1. The petitioners in these consolidated matters are FacilitySource, LLC (FacilitySource) and FacilitySource Northeast Services, LLC (FSNE) or together with FacilitySource (petitioners).

2. As a result of its audits of FacilitySource and FSNE, the Division of Taxation (Division) issued four notices of determination (notices) to FacilitySource and one notice of determination (notice) to FSNE based upon its determination that petitioners' management fees for facilities management services are taxable as sales of prewritten software.

3. FacilitySource¹ was founded in 2005 in Ohio and has operated continuously, growing to national prominence in the facility management industry. FacilitySource was not a registered New York State (NYS) sales tax vendor during the period December 1, 2009 through February 28, 2014. FacilitySource registered as a NYS sales tax vendor in March 2014.²

4. FSNE was founded in 2013 in Arizona in order to service The Great Atlantic and Pacific Tea Company, Inc., better known as A&P, a chain of grocery stores primarily in the northeast region, until declaring bankruptcy in 2015. FSNE was not a registered NYS sales tax vendor during the period September 1, 2013 through February 28, 2014. FSNE registered as a New York sales tax vendor in March 2014.³ FSNE used the same employees and operations as FacilitySource.

5. At the hearing, petitioners offered the testimony of three FacilitySource employees, William Hayden, Jordan Wagner and Jeffrey Wirtz, regarding the history and operations of FacilitySource. Mr. Hayden was FacilitySource's chief executive officer (CEO) during the audit period of December 1, 2009 through February 28, 2017. Once CBRE Group, Inc.⁴ wholly acquired FacilitySource in June 2018, Mr. Hayden became president of CBRE. Mr. Hayden was

¹ Prior to 2012, FacilitySource, LLC was Facility Source, Inc.

² Although the parties stipulated that FacilitySource registered as a NYS sales tax vendor in March 2014, its form DTF-17, application to register for a sales tax certificate of authority (form DTF-17) was dated April 9, 2014.

³ Although the parties stipulated that FSNE registered as a NYS sales tax vendor in March 2014, its form DTF-17 was dated April 9, 2014.

⁴ CBRE Group, Inc. (CBRE) is a large commercial real estate services and investment firm.

involved with FacilitySource before, during and after the audit period and offered testimony regarding the history of the company. Mr. Wagner testified that he is managing director of CBRE. Mr. Wagner testified that he began working for FacilitySource in June 2007. He further testified that during the audit period, he was a market director from 2009 to 2012, then he became the director of operations and later vice president of operations at FacilitySource. Beginning in September 2015, Mr. Wirtz was the vice president in charge of FacilitySource's call centers and is currently CBRE's vice president of service delivery for the Americas. Mr. Wirtz offered testimony about the operations of FacilitySource's call centers.

6. FacilitySource was founded in 2005 as a call center to outsource facility management needs. Mr. Hayden testified that he joined FacilitySource in March 2006, with a group of original investors, and became CEO of FacilitySource in September 2007. According to Mr. Hayden, FacilitySource was founded to outsource the facility maintenance accounts of Limited Brands and then expanded the services to other companies. When Mr. Hayden joined FacilitySource, it had approximately 15 employees working at a call center located in Columbus, Ohio, where Limited Brands was headquartered. According to Mr. Hayden, from 2006 to 2012, FacilitySource provided "outsourced coordination of work order management, facilities management services" to its customers. In 2012, to provide additional services to FacilitySource's customers, Mr. Hayden raised capital with the private equity firm Warburg Pincus, with the purpose of building a vendor network. At some point, FacilitySource's Ohio offices were moved into a 35,000 square foot facility, with 10,000 square foot taken up by the call center agents. According to Mr. Hayden, FacilitySource opened a call center in Phoenix, Arizona, in about 2007 to service a customer based in Phoenix. Later, the Phoenix, Arizona, call center became the basis of FacilitySource's "redundant call center."

7. During the audit period, FacilitySource was organized into at least seven separate departments under Mr. Hayden, including client services, controller, information technology (IT) manager, human resources, marketing analyst, business analyst, and business development, the largest of which was client services. In approximately 2015, FacilitySource realigned its employee teams based upon the growth of the business and changed its organizational chart to reflect regional customer service teams.

8. Mr. Hayden testified that facilities management services included answering calls, finding contractors, scheduling appointments, following up on the service to see if the contractors showed up and performed satisfactorily and doing this when scaled up to a thousand stores, or for some customers, fifteen thousand stores.

9. More specifically, FacilitySource provides its customers facilities management services, including 24/7 call-in transaction center access, web-based portal access (portal), work order management, vendor management, electronic invoicing, and data analytics, all under the single moniker – Integrated Facilities Management (IFM).

10. FacilitySource offers its model for IFM nationally to chain stores with greater than 200 locations in the United States, including customers with locations in New York State.

11. Mr. Hayden testified about the difference between IFM and property management stating that facilities management is “tactical” and involves the resolution of work orders, whereas traditional property management has employees managing specific buildings.

12. Work orders would come to FacilitySource through phone calls, email, the portal, and, in the early days, through fax.

13. Mr. Hayden testified and explained each of the components of IFM, specifically the data collection, the movement of the work order through the system, the measures taken to

evaluate their performance, paperless invoicing and the dedicated account teams needed to support FacilitySource's facilities management services.

14. Mr. Hayden testified that IFM was a "people intense model" requiring a very large employee base to process "billions of interactions a year." He further testified that "it's a headcount as . . . we mentioned, a lot of people touching these work orders every day. It's a very headcount intensive business model." According to Mr. Hayden, IFM allows FacilitySource and its customers "to really tap into that pool of resources. They couldn't build internally or be too expensive to build internally."

15. Mr. Hayden acknowledged that fmPilot is a component of the IFM. He explained that FacilitySource is a tech-enabled business that uses technology just like every company does.

16. Mr. Hayden further explained that fmPilot was like "a service desk or IT ticketing system" that serves as a communication platform or communication device. FacilitySource uses fmPilot to interact with its customers and its service providers.

17. Using FacilitySource's IFM, its customers can submit work orders for "need-based" facility management services, such as reporting a broken storefront window. Additionally, during regular maintenance cycles for building or equipment, such as the service or upgrade of a heating, ventilation, air conditioning (HVAC) system, FacilitySource's customers receive maintenance services scheduled through the IFM.

18. FacilitySource's IFM included access to fmPilot, the FSElite network, a call center, analytics and reporting.

Maintenance Management Agreements

19. FacilitySource entered into agreements with its customers to provide its services. The agreements reference management fees that are referred to as subscription fees in the

auditor's report, but no distinction between the two exists. The record includes three representative samples of maintenance management agreements used by FacilitySource during the audit period.

20. The April 2008 Maintenance Management Agreement (Agreement) between FacilitySource and General Nutrition Centers, Inc. (GNC or Customer), is a representative example of a maintenance management agreement with the monthly pay option. As an early version of FacilitySource's offering, the Agreement contracted for Facilities Maintenance Optimization (FMO) that included fmPilot software, a designated toll-free number, fmPilot portal access, call center access, vendor maintenance, reports, and paperless invoicing.

21. Regarding intellectual property, section 12 (b) of the GNC Agreement provides as follows:

“During the term of this Agreement, Customer shall have no right to use FacilitySource's trademarks, service marks, patents, trade names, distinctive words, logos, pictures, colors, formulas, designs, design models or copyrights, or derivations or adaptations thereof or any marks or works similar thereto (all constituting FacilitySource's 'Intellectual Property') in any manner without FacilitySource's prior written approval. After the expiration or termination of this Agreement, Customer shall not use FacilitySource's Intellectual Property in any manner whatsoever. Customer acknowledges that FacilitySource's Intellectual Property is unique and that monetary damages would be insufficient to compensate FacilitySource for any breach of this Section 12 by Customer, its principals, affiliates, employees or agents. Accordingly, Customer agrees that, in addition to any other available remedy, FacilitySource shall be entitled to injunctive and other special and equitable relief in connection with any such breach.”

22. The Agreement, dated October 1, 2012, and Second Amendment to Agreement, dated February 2017,⁵ between FacilitySource and Uniqlo USA, LLC (Uniqlo or Customer) is a representative example of a maintenance management agreement with the percentage pay option. As was the case of the GNC Agreement, the Uniqlo Agreement contracted for FMO.

⁵ The parties signed the Second Amendment to Agreement in April 2017.

23. Review of the Uniqlo Agreement indicates that the language of section 12 (b) is identical to the language set forth in section 12 (b) of the GNC Agreement. However, the Uniqlo Agreement contains a section 12 (c), titled “FacilitySource’s Technical Elements,” which in relevant part states:

“The services provided to Customer hereunder may include data, modules, components, designs, utilities, subsets, objects, program listings, tools, models, methodologies, programs, systems, analysis frameworks, leading practices, and specifications owned or developed by FacilitySource prior to, or independently from, its engagement hereunder, including, without limitation, the fmPilot maintenance and asset management system (web-based portal and software) (collectively, the ‘FacilitySource Technical Elements’), and FacilitySource retains exclusive ownership rights to the FacilitySource Technical Elements. Customer acknowledges and agrees not to modify, reverse engineer or create any derivative works of any FacilitySource Technical Elements, and that any and all modifications or enhancements to the FacilitySource Technical Elements, whether or not suggested or requested by Customer, shall be and remain the sole property of FacilitySource. Only the data relating to Customer’s service requests, input into the fmPilot maintenance and asset management system by Customer, and Customer’s existing proprietary business information, will be considered the intellectual property of Customer. FacilitySource has developed and owns the fmPilot software. *FacilitySource does hereby grant to Customer, a non-exclusive, revocable, limited license to use the fmPilot software to (a) copy, distribute, transmit, display and otherwise use fmPilot (including any documentation, upgrades, modifications, patches or fixes thereto) as part of the services (b) provide access to the hosting services to a limited number of end users.* Nothing herein shall be construed to grant Customer any ownership right in the fmPilot software. After the termination of this Agreement, Customer shall return or certify destruction of all FacilitySource property in Customer’s possession and shall not use FacilitySource’s property, including the FacilitySource Technical Elements in any manner whatsoever. *Customer agrees to abide by any and all license requirements and instructions of FacilitySource related to the fmPilot software.* Notwithstanding anything contained herein . . . FacilitySource alone (and its licensors, where applicable) shall own all right, title and interest in and to FacilitySource Technical Elements and to any commercially available products of FacilitySource developed independently of this Agreement that are provided to Customer, and all related intellectual property rights, in and to any suggestions, ideas, enhancement requests, feedback, recommendations or other information provided by Customer or any other party relating to the services provided under this Agreement. This Agreement is not a sale and does not convey to Customer any rights of ownership in or related to the services, FacilitySource’s intellectual property, including the FacilitySource Technical Elements, or the technology employed by FacilitySource. Customer acknowledges that FacilitySource’s

Technical Elements are unique and that monetary damages would be insufficient to compensate FacilitySource for any breach of this Section 12(c) by Customer, its principals, affiliates, employees or agents. Accordingly, Customer agrees that, in addition to any other available remedy, FacilitySource shall be entitled to injunctive and other special and equitable relief in connection with any such breach” (emphasis added).

24. The Agreement, dated January 29, 2014, between FacilitySource and Vitamin Shoppe, Inc. (Vitamin Shoppe) is a representative example of a maintenance management agreement with the annual pay option. As was the case with both the GNC and the Uniqlo Agreements, the Vitamin Shoppe Agreement contracted for FMO. Section 4 (a) of the Vitamin Shoppe Agreement states that FacilitySource shall provide “the services set forth in the Statement of Work attached hereto as Exhibit A.” The Statement of Work, attached to the Vitamin Shoppe Agreement, lists fmPilot, the support center, reporting, service provider, i.e., contractor, maintenance, and paperless invoicing. With respect to the intellectual property, the language of sections 12 (b) and (c) of the Vitamin Shoppe Agreement are similar to the language set forth in sections 12 (b) and (c) of the Uniqlo Agreement referenced above.⁶

25. Mr. Hayden reviewed the agreements for GNC, Uniqlo and Vitamin Shoppe and testified that the language was “tightened up” over time based on experience. He further testified that the agreements were revised through the years, especially after private equity investment.

26. During his testimony about particular sections of the GNC, Uniqlo and Vitamin Shoppe agreements, Mr. Hayden acknowledged that fmPilot was included within the “Intellectual Property” section 12, i.e., section 12 (b), of the GNC, Uniqlo and Vitamin Shoppe

⁶ The language in section 12 (b) is identical in both agreements. However, one of the last sentences in section 12 (c) of the Vitamin Shoppe Agreement erroneously contains “this Section 18.1,” rather than “this Section 12 (c)” set forth in the language of section 12 (c) of the Uniqlo Agreement. It is noted that there is no section 18.1 in the Vitamin Shoppe Agreement.

agreements and the “Technical Elements” section 12 (c) of the Uniqlo and Vitamin Shoppe agreements.

27. In response to the question of how many individuals could be involved in a hypothetical GNC work order, Mr. Hayden stated that he would put it in two categories:

“[L]ikely there are multiple people in each category touching it because of . . . the twenty-four seven nature of the business, right. . . . The first stop on that work order is our . . .C.S.R. . . .and [then] dispatching that work order . . .there’s multiple people following up to make sure that the vendor accepts the work order . . . the happy path is a very straight line path. Unfortunately, there’s a lot . . . of work orders that don’t go down that happy path.”

Mr. Hayden stated that on average four to eight FacilitySource employees were involved in the processing of a work order.

28. During the audit period, FacilitySource also employed trade experts who weighed in on problems and reviewed quotes for work proposed by the vendors and pushed back on costs.

29. Both Mr. Hayden and Mr. Wagner indicated that FacilitySource’s pricing of a management agreement was very customized and derived from the bundle of services offered and how many people would be dedicated to the customer account. Mr. Wagner testified that fmPilot was never priced or sold separately.

fmPilot Software

30. At FacilitySource’s direction, fmPilot was created in 2007 by a third-party software developer as a FacilitySource owned computerized maintenance management software (CMMS), used to help better manage larger clients. Previously, FacilitySource used a different CMMS, but created the fmPilot software to be more efficient and fill gaps from the prior software.

31. FacilitySource upgraded to fmPilot 2 in 2014 or 2015. The software and data are stored on third party servers, not on FacilitySource’s servers or in customer owned locations.

32. FacilitySource grants its customers a license for use of the fmPilot software in their agreements.

33. FacilitySource's fmPilot is a component part of the IFM product that is consistently touted in its marketing materials. The fmPilot software is the central repository for data for the company's operations. Mr. Hayden acknowledged that the business would not function without fmPilot, or another CMMS, to deliver the overall service.

34. FacilitySource's marketing materials state that fmPilot is a "web-based portal system that enables users to enter facility work requests, dispatch work orders, and create facility reports on all activities." Further, the brochure describes fmPilot as a:

- "[C]entral repository for work order management & asset tracking[,]
- [I]nvoice validation[,]
- [G]ranular visibility to maintenance expenses[,]
- [S]pend thresholds built into system[,]
- [C]ontract & document management[,]
- [S]tatutory compliance management[,]
- [F]ully customizable/business rule driven[.]"

35. The service providers, clients, and FacilitySource all have different access to the same software program. During his testimony, Mr. Hayden reviewed screenshots of fmPilot and testified that the screenshots were what FacilitySource's employees would view.

36. The internal view of fmPilot is the same as what the customer views, except the customer is limited to their own data. Within fmPilot, a customer may log in, see calendars of work, and look at service orders.

37. The fmPilot software has different statuses to track the life cycle of a work order. Different work orders may take different paths. A simple work order may be created, dispatched to a provider, accepted, and completed. Other work orders may need to go through a quoting process and would involve more of FacilitySource's employees including an account team and

possibly a trade specialist. Spend levels and other parameters could lengthen the quoting process.

38. Some customers had limits on the amount spent on jobs, others trusted FacilitySource to set the levels.

39. Ultimately, a repair job is invoiced in fmPilot.

40. According to Mr. Hayden, fmPilot is a communication device, which is the way FacilitySource employees document all the activity. He testified that fmPilot “flags when something needs a follow up, but it doesn’t do the follow up.”

Vendors and the FSElite Network

41. FacilitySource maintains a national list of approved vendors and trade service providers, known as FSElite. The vendors are vetted by FacilitySource and are required to adhere to FacilitySource’s strict service timelines, warranty requirements, cost profiles and billing requirements. FacilitySource’s customers have either pre-loaded their own vendors, or contractors, into fmPilot, or they contract for and utilize the FSElite network.

42. Mr. Hayden discussed the FSElite network and testified that it was a proprietary network consisting of vendors to meet customers’ facility repair needs. FacilitySource’s vendor list was not available to customers on fmPilot.

43. At all times, FacilitySource is the contractual agent of the customer for the purpose of hiring trade services or making vendor purchases.

44. FacilitySource does not perform maintenance or repair work, but does ensure its contractors’ work in amounts greater than its contractors’ individually held insurance. Mr. Hayden testified that this was appealing to smaller contractors because they could take on larger jobs without the requisite individual insurance. FSElite members can do other work.

45. Vendors have access to fmPilot. The contractors do not pay any fee for the access. Vendors utilize fmPilot to receive work orders, report on work order requirements, adhere to the strict schedule requirements and invoice the customer.

46. If a customer does not use FSElite, they may load preferred vendors.

47. If a customer subscribes to FSElite, FacilitySource ranks service providers and loads a matrix into the fmPilot software. A FacilitySource's employee uses the ranking to select the contractor and only invoices the repair job to the client as FSElite.

Call Center Access

48. Pursuant to FacilitySource's management agreements with customers, the transaction center, i.e., call center, operated 24 hours a day, 7 days a week, 365 days per year and consisted of one or more physical locations, personnel, business continuation plan (including generator back-up, automated back-up power supplies, back-up servers and remote hosting facilities), communication systems (integrated voice response systems, IP telephony and hardware), necessary supporting software applications and processes designed to operate an efficient call center.

49. Customer service representatives, internally known as CSRs, staff the call center and maintain client accounts. Mr. Wagner testified that the CSR is the first line of defense and takes the call, email, or portal. CSRs use fmPilot software to maintain client accounts.

50. During the audit period, FacilitySource's Columbus, Ohio, and Phoenix, Arizona, call centers employed approximately 185 employees at its height and 140 employees on average. Mr. Wirtz testified that each of those call centers was organized as a typical call center with pods in an open space for the CSRs.

51. The various employee positions at the call centers included CSRs, team leads, supervisors and workforce management personnel.

52. Call center CSRs answered calls, gathered complete information and triaged the problem all to create a work order and start the work order process.

53. CSRs maintained customer accounts using fmPilot software. Whether a customer placed a phone call or used the web-based portal to request maintenance or repair work at a specific location, the work order sits in a receive status in fmPilot for a CSR to review. Once the job is completed, a billing team becomes involved and closes out the invoice.

54. Mr. Wirtz testified that when a work order comes in through fmPilot, “it’s sitting there in received status at that point in time.” It is the CSR’s responsibility to open each and every one of those work orders then “go in and look for accuracy, completeness of the data that’s been entered in there, correctness of the type and code that it [is] categorized as.” The CSR must ensure that “all the information in there is both accurate and complete,” so that the CSR “can go ahead and manually dispatch out the appropriate [service] provider.”

55. According to Mr. Wagner, 80-90% of the work orders traveled the “happy path” and were resolved, but the balance of the work orders required escalations or pending client invoice approval.

56. Mr. Wagner testified that work orders “predominantly came in via our call center . . . [a]nd some of the technology adoption came later in the last few years . . . most of our clients would call or email in” and that the call centers received thousands of phone calls per day in both Columbus, Ohio, and Phoenix, Arizona.

57. Mr. Wirtz testified that during the audit period, the call centers would get 2,500,000 inbound and outbound calls annually, with 80% being inbound calls and, as a policy, 100% of FacilitySource's customers' emergency inbound calls.

58. For the months of June 2015, July 2015, August 2015, September 2016, October 2016 and November 2016, the percentage of total work orders received through FacilitySource's fmPilot portal were 20.88%, 20%, 18%, 28%, 28% and 27%, respectively, however, some of FacilitySource's customers never used the portal.

59. Both Mr. Wirtz and Mr. Wagner testified that part of FacilitySource's service was to train its employees on each customer's specific and tailored standard operating procedures or their internal procedures, which required material training.

60. Customers received unique 1-800 phone numbers that would connect to the call center or FacilitySource would operate an extension on the customers' phone system's call-tree to make it easy and integrated for its customers' employees to reach the call center.

61. Mr. Wirtz testified that the customers had one phone number to call. However, there were other instances where a company like Limited Brands for their different stores or retail divisions would have a dedicated phone number for each store or retail division to use, regardless of whether the call was emergency or non-emergency, "that would be for us to then triage from that point."

62. Mr. Wagner testified that the fmPilot software was "a work order management software," a CMMS. It is "really a communication tool where we can enter, create, dispatch and track and communicate all of the work order life cycle to help manage our client's facilities."

63. According to Mr. Wagner, some of FacilitySource's customers, even large multi-million dollar customers, do not use fmPilot because they have their own CMMS software or

because they want their employees to use the call center, but importantly, the facilities management service provided by FacilitySource is not affected in anyway.

64. Mr. Wagner testified that fmPilot did not replace the call centers, which remain “a large part of what we [FacilitySource] do[es] today.”

Reports

65. FacilitySource performs quarterly reviews with its customers at which time it reviews all the quarter’s activities, such as work orders, and the performance of the key success criteria set forth in the management agreements.

66. The record includes sample copies of FacilitySource reports that correspond to the GNC, Uniqlo and Vitamin Shoppe agreements referenced herein. The reports were provided in conjunction with presentations to the respective customers. Mr. Hayden testified that the reports were part of the overall product.

67. FacilitySource issues monthly or quarterly reports to its customers to review facility needs and the efficacy of its services. Within the reports, FacilitySource sells other facility management services.

68. FacilitySource uses data from fmPilot, statistical modeling software, and internal workforce management software to produce the reports. Mr. Hayden testified that all that information was placed in a reporting database and had “one data set that we pulled from multiple sources.”

69. FacilitySource used anonymous data to benchmark a customer’s data in the reports. FacilitySource extracted the anonymous customer data from fmPilot and used anonymous benchmarks of other customers’ costs to compare the customer’s performance to similarly situated businesses. Mr. Wagner testified that his team “compiled this information from the data

in fmPilot, rearranges that, and then sends it” to the customer. He further testified that FacilitySource’s customers were interested in how they compared to other similarly situated customers.

Pricing

70. Mr. Hayden testified that there is no average pricing for its product. Instead, it is individually priced based upon the cost of labor and equipment needed to staff the customer’s needs, with a profit margin added.

71. One subscription fee covered all the IFM products and services. FacilitySource charged some customers a “management fee” added to the trade services (trade services) in place of a subscription fee.

72. The fmPilot software was never separately priced or separately invoiced. Additionally, the fmPilot software is not sold separately or as a standalone product.

Operations and Structure of FacilitySource

73. FacilitySource had different divisions, including customer relations, finance, human resources, marketing, business analysts, sales, operations, tech products, and implementation.

74. The fmPilot software is supported by the tech products team, not the IT team. The tech products team has about 20 people and had about 12 to 15 people during the audit period.

75. In 2015, during the audit period, Mr. Hayden testified that FacilitySource employed a total of 350 to 400 employees engaged in facilities management on behalf of its customers. According to Mr. Hayden, those employees helped FacilitySource’s customers save money through the use of FacilitySource’s dedicated shared staffing resources that manage all the work for its customers.

76. Mr. Hayden testified to a “high touch” service with a “sense of urgency” for the customers and that FacilitySource’s “leading position was our people make the difference, right. We hustle, we keep you up and running.” He further testified that “we don’t put boots on the ground. We don’t do any of the work. We don’t turn any wrenches. We do it all remotely. And, you know, leveraging our processes to make sure we get the outcomes that we have in contracts.”

The Audit

77. From December 2015 through November 2017, Jennifer Bramley, Tax Auditor 1, was assigned and conducted a sales tax field audit of FacilitySource for the period December 1, 2009 through February 28, 2017.⁷

78. In December 2015, the auditor spent one hour conducting a preaudit analysis of FacilitySource and leaving a message asking the company to call her back to set up an audit appointment.

79. After receiving no response from FacilitySource, on February 18, 2016, the auditor issued an appointment letter, scheduling the audit of FacilitySource’s sales and use tax books and records at its offices on May 2, 2016, and an information document request (IDR).

80. The IDR was a standard type issued at the commencement of a sales and use tax audit, and requested among other items, all exemption documents supporting non-taxable sales, including documents showing resale, exempt use, exempt organization, and capital improvement certificates. The IDR also requested any other documentation necessary to prove non-taxable sales.

⁷ During the course of FacilitySource’s audit, two consents were executed to extend the period of limitations to determine sales and use taxes for the period December 1, 2009 through November 30, 2014 until December 20, 2017.

81. The auditor issued two additional IDRs to FacilitySource on October 17, 2016 and May 8, 2017. FacilitySource provided responsive documents to the IDRs; however, it did not provide any documents to establish the actual usage of the software at each customer location.

82. On April 14, 2016, the auditor sent an email to FacilitySource to reschedule the audit appointment and to ask some preliminary questions including, among other things, what was the nature of FacilitySource sales/services, and the location of FacilitySource locations in New York State.

83. On April 14, 2016, Tammy Poole, a FacilitySource employee, sent a responding email to the auditor. In that email, Ms. Poole indicated that FacilitySource did not have any New York locations. Ms. Poole also described FacilitySource's business model as "[i]n a nutshell, our customer calls us to let us know they have a problem and then we find a local repair company to go to our customer's location and fix the problem." At that time, the auditor rescheduled the appointment to October 3 and 4, 2016, and asked for additional information to be provided at the field audit appointment.

84. On September 15, 2016, the auditor received an email from Ms. Poole's personal email account, requesting a confidential discussion of the audit of FacilitySource. Because the auditor treated the email and the subsequent conversation with Ms. Poole as in the nature of a "squeal," there is no memorialization of either the contents of Ms. Poole's personal email or any subsequent conversation related to the same in the audit file.

85. In October 2016, the auditor went to FacilitySource's Phoenix, Arizona, offices to conduct the field audit of the company. On October 3, 2016, the auditor met with three of FacilitySource's employees: Ms. Poole, Alan Blackhurst and Hideto Tsujimura, controller.

Those employees were in FacilitySource's accounting department. FacilitySource did not offer for the auditor to speak to anyone else or tour any other division of the company.

86. At the October 3, 2016 meeting, the auditor and Facility Source's employees discussed the different components of FacilitySource's business, including trade services and subscription services. The employees told the auditor that the subscriptions were for the use of the fmPilot software. FacilitySource provided federal income tax returns for the years 2012 through 2015 at the end of the meeting. The auditor began reviewing the federal income tax returns but had questions regarding the information in those returns. She also sent an email to Ms. Poole recapping the meeting and requesting the information needed for review.

87. At the October 4, 2016 field visit, the auditor received FacilitySource's sales tax returns and revenues for the years 2014 and 2015, by state, for both subscriptions and trade services. The auditor also received, via email, subscription figures for 2010 through 2013. Prior to her departure, the auditor received FacilitySource's customer list locations.

88. The auditor received annual figures for FacilitySource's subscription services and federal returns, entered and analyzed the same. Initially, the auditor had difficulty reconciling the federal returns to the sales tax returns because there was no reporting of tax on subscriptions. She concluded that FacilitySource was not collecting tax on the subscriptions.

89. At the October 2016 audit appointments, the auditor worked in a FacilitySource conference room and did not tour the facility or speak with any employees from the operations department. At no time during those audit appointments, did the auditor request a tour of FacilitySource's Phoenix, Arizona, offices.

90. During the October 2016 audit appointments, the auditor learned of the existence of FSNE. Subsequently, the audit of FSNE was assigned to and conducted by Ms. Bramley.

91. On October 25, 2016, the auditor sent FacilitySource an updated appointment letter and associated documents. She also sent an email to Mr. Tsujimura and Mr. Blackhurst for the name of the new contact person since Ms. Poole resigned from the company shortly after the auditor's field visits on October 3 and 4, 2016. Her email also recapped what was needed and advised that the appointment letter and forms were sent to a secure email set up for them, along with the username and password.

92. On October 26, 2016, a separate appointment letter and first IDR were sent for the audit of FSNE. The auditor sent a second IDR for FSNE on May 8, 2017. FSNE provided responsive documents to the IDRs; however, it did not provide any documents to establish the actual usage of the software at each A&P location.

93. Subsequently, the auditor scheduled a second field visit to FacilitySource's Phoenix, Arizona, offices, for May 8 and 9, 2017. On April 4, 2017, the auditor sent an email to FacilitySource employees Kathleen Bobbe and Mr. Tsujimura recapping the information needed for the May 8, 2017 appointment for the audits of FacilitySource and FSNE. The email requested the following information for:

“Facility Source LLC (FS Holdco Inc):

- Responsible Person questionnaire completed
- Sales Tax questionnaire completed
- Backup reports of how you came to your figures on your returns for the audit period (12/1/09- 8/31/16). I reviewed the returns at the last appointment[,] but reports were not provided.
- Tax liability report – tax collected for the audit period (12//1/09-8/31/16) by date.
- Sales Reports for all sales everywhere and then those sales that are for NY for the audit period by quarter (12/1/09-8/31/16). I need Trade & Subscription broken out by quarter.
- Sales details for Trade for the test periods of Sept-Nov 2012, June-Aug 2014 & March-May 2016.
- Sales detail for Subscriptions for the audit period (12/1/09-8/31/16).

Facility Source Northeast Services LLC: (A&P Stores)

- Responsible Person questionnaire completed
- Sales Tax questionnaire completed
- Sales tax returns with backup reports on how you came to the figures on the return for the audit period (9/1/13-8/31/16).
- Tax liability report – tax collected for the audit period (9/1/13-8/31/16) by date.
- Sales report for all sales everywhere and then those sales that are for NY by quarter for the audit period (9/1/13-8/31/16). I need Trade & Subscription broken out by quarter.
- Sales detail for Trade for the test periods of Sept-Nov 2013 & June-Aug 2016.
- Sales detail for Subscriptions for the audit period (9/1/13-8/31/16).”

94. Upon arrival at FacilitySource’s offices on May 8, 2017, the auditor received some information that she had requested for the FacilitySource audit. For subscription services, she received emails with annual figures for all subscription fees with no isolation of New York sales. While on site that day, the auditor requested and received a few different location lists and customer break downs of the subscription sales. The auditor received FacilitySource’s trade service sales detail, and the parties agreed to a test period to examine those sales. The auditor testified that she did not have a formal meeting with FacilitySource employees on May 8, 2017.

95. In addition to reviewing FacilitySource’s records on May 8 and 9, 2017, the auditor reviewed FSNE records provided by FacilitySource employees. During the May 8 and 9, 2017 audit appointments for FacilitySource and FSNE, the audit periods were extended through the period ending February 28, 2017.

96. Review of FacilitySource’s tax field audit record (audit log) indicates that the auditor made field audit visits on October 3, 2016, and October 4, 2016, for 7.5 and 7.5 hours, respectively, and again on May 8, 2017 and May 9, 2017, for 3.5 and 4 hours, respectively. During those field visits, the auditor reviewed FacilitySource’s books and records, including but not limited to federal income tax returns (2013-2016), sales tax returns, subscription access

figures (2013-2017), trade service figures, location lists of clients in New York and monthly invoices pursuant to customer agreements.

97. The auditor deemed FacilitySource's records to be adequate and reviewed its sales in detail for both trade and subscription services.

98. After reviewing FacilitySource's trade service invoices, the auditor found that FacilitySource was taxing all charges, therefore, she decided to accept the sales as reported for their trade service sales.

99. A review of FacilitySource's audit log indicates that the auditor continued to request information regarding its subscription sales in July 2017 and received a response in August 2017.

100. Based upon the information gathered and provided, the auditor determined that subscription fees were taxable because they included access to the fmPilot software. The auditor concluded FacilitySource charged the subscription fees for a bundle of services and tangible personal property, and the entire charge was subject to tax.

101. FacilitySource did not report subscription services on its sales tax returns because it did not consider those sales to be taxable. Since FacilitySource only billed its customers' headquarters, the auditor used percentages based on FacilitySource's customer location list. The auditor received the subscription revenues per year and applied the percentage that should be allocated to New York.

102. An entry in FacilitySource's audit log for August 14, 2017 indicates that the auditor sent audit workpapers assessing tax on FacilitySource's subscriptions to FacilitySource employees via the Division's secure MOVit site, along with an email indicating that any information was due by September 15, 2017. A FacilitySource employee responded by email on August 28, 2017, requesting additional time to gather the 465 invoices previously requested by

the auditor, and asking for the auditor's reasoning for holding the subscription sales taxable. On September 5, 2017, the auditor responded to the FacilitySource employee, by email, informing her that if FacilitySource was unable to provide the information by the deadline of September 15th, the case would be uploaded as disagreed, but work could continue towards an agreement. The audit log entry for September 5, 2017, also indicates that the auditor "explained the reasoning behind holding the subscriptions taxable."

103. On September 7, 2017, the auditor received powers of attorney from petitioners' former representatives, Naftali Dembitzer, Esq., and Ellis Reemer, Esq. Both petitioners' audit log entries for September 13, 2017, indicate that the auditor had a conference call with petitioners' former representatives that, among other things, included a discussion about the open issues and their disagreement that the subscriptions were taxable. The auditor advised the former representatives that, at a meeting with FacilitySource employees, those employees explained that the subscriptions were for the use of the fmPilot software. The audit log entries for September 13, 2017, also indicate that the auditor printed out the fmPilot information from the FacilitySource website "which discusses in detail the software and the use of it," and provided, as requested, a recap email to petitioners' former representatives. Subsequent FacilitySource audit log entries indicate that FacilitySource was given additional time to provide the information still needed regarding the subscription sales and, thereafter, FacilitySource provided additional information that the auditor used to prepare updated workpapers. The auditor sent the updated workpapers through the MOVit site on November 1, 2017. On November 3, 2017, the auditor received a voicemail from petitioners' former representatives advising that they did not have any additional information to provide at that time and to upload both cases and that work

could continue on the same prior to the proceedings at the Division's Bureau of Conciliation and Mediation Services (BCMS).

104. Based upon the information provided, the auditor determined the number of FacilitySource's New York customer locations and multiplied the same by FacilitySource's gross receipts to determine New York sourced gross receipts (New York Taxable Sales). The auditor then multiplied the appropriate state and local sales tax rate to the New York Taxable Sales and determined New York sales tax due. As a result of the audit of FacilitySource, the Division calculated New York Taxable Sales in the amount of \$6,522,921.25,⁸ which resulted in additional tax due in the amount of \$521,833.70.

105. On November 13, 2017, the Division issued a statement of proposed audit change for sales and use tax (statement of proposed audit change) to FacilitySource. The statement of proposed audit change listed additional tax due in the amount of \$521,833.70 and interest, at that time, of \$212,039.15, for the period December 1, 2009 through February 28, 2017. Penalties were not asserted against FacilitySource. Subsequently, FacilitySource orally disagreed with the determination that the subscription services were taxable.

106. On November 22, 2017, the Division issued a closing letter to FacilitySource stating that, as a result of the audit of FacilitySource's tax returns and records, it found additional tax due on "unsubstantiated exempt sales of subscriptions."

107. A review of FSNE's audit log indicates that the auditor conducted the field audit of FSNE at FacilitySource's Phoenix, Arizona, offices on May 8 and 9, 2017, for 2.0 and 3.5 hours, respectively. During those on-site visits, the auditor reviewed FSNE's books and records,

⁸ The FacilitySource audit file's "Additional Audit Information" section stated that the total additional taxable sales amounted to \$6,522,921.25 and additional tax due on the same in the amount of \$521,833.70. However, the audit workpapers show total additional sales of \$6,178,736.12 on SCH-C and additional tax due in the amount of \$521,833.70 on SCH-E. At the hearing, no explanation was provided for this discrepancy.

including but not limited to federal income tax returns (2013-2016), sales tax returns, subscription access figures (2103-2017), trade service figures, location lists of clients in New York and monthly invoices pursuant to customer agreements. The management fee was invoiced monthly to A&P and payment terms were 30 days. During the May 8, 2017 field visit, the FSNE's audit period was extended to the period September 1, 2013 through February 28, 2017.⁹

108. The auditor deemed FSNE's records to be adequate and reviewed its sales in detail for its trade and subscription services.

109. After reviewing FSNE's trade services, the auditor found that FSNE was not charging the tax "consistently correct." The auditor determined additional taxable sales on trade services in the amount of \$393,714.94 and tax due of \$31,497.20. The basis of the tax due was jurisdictional rate errors and sales that were not capital improvement work.

110. The auditor found that FSNE's subscription sales were not reported on its sales tax returns. Since FSNE only billed A&P's headquarters, she used percentages based upon the A&P locations list provided by FSNE that identified 144 New York State locations out of 298 everywhere locations. The auditor calculated that 48.32% of FSNE's A&P locations were in New York State. The auditor received the subscription revenues per year and applied the percentage, i.e., 48.32% that should be allocated to New York. The auditor did not determine the actual usage of the fmPilot software by FSNE's A&P locations in New York.

111. During the audit, FSNE did not provide its management agreement with A&P.

112. Based upon the information provided, the auditor determined the number of FSNE's A&P's New York locations and multiplied the same by FSNE's gross receipts to determine New York Taxable Sales in the amount of \$3,552,640.63. The auditor then multiplied

⁹ On May 10, 2017, FSNE executed a consent to extend the period of limitations to determine sales and use taxes for the period September 1, 2013 through November 30, 2014 until December 20, 2017.

the appropriate state and local sales tax rate to the New York Taxable Sales and determined New York sales tax due in the amount of \$284,211.25.

113. As a result of the audit of FSNE, the Division found additional tax due on subscription sales and trade services in the total amount of \$315,708.45.

114. On November 13, 2017, the Division sent a statement of proposed audit change to FSNE for the period September 1, 2013 through February 28, 2017. The statement of proposed audit change listed additional tax due in the amount of \$315,708.45 and interest, at that time, in the amount of \$77,092.18. Penalties were not assessed against FSNE. Subsequently, FSNE orally disagreed with the determination that the subscription services were taxable.

115. On November 21, 2017, the Division issued a closing letter to FSNE indicating that it had completed its audit of FSNE's tax returns and records and found additional tax due in the areas of subscription sales and service sales, i.e., trade service sales. The closing letter stated that the basis of the tax due on subscription sales was from unsubstantiated exempt sales and the basis of the tax due from service sales was those sales were not capital improvement work.

116. On November 21, 2017, the Division issued four notices of determination to FacilitySource:

(a) Assessment ID# L-047470024, asserting tax due in the amount of \$171,962.62, plus interest, for the period December 1, 2010 through February 29, 2012;

(b) Assessment ID# L-047471272, asserting tax due in the amount of \$169,228.22, plus interest, for the period March 1, 2012 through May 31, 2014;

(c) Assessment ID# L-047471062, asserting tax due in the amount of \$146,711.98, plus interest, for the period June 1, 2014 through August 31, 2016; and

(d) Assessment ID# L-047470180, asserting tax due in the amount of \$33,930.88, plus interest, for the period September 1, 2016 through February 28, 2017.

117. On November 22, 2017, the Division issued to FSNE a notice of determination, assessment ID# L-047474523, assessing tax due in the amount of \$315,708.45, plus interest, for the period September 1, 2013 through February 29, 2016.¹⁰

118. During its audit, FacilitySource did not provide receipts or terms for the subscriptions. However, after the audit, FacilitySource picked three agreements as samples, despite the auditor's request for a larger number of sample agreements. The sample agreements provided by FacilitySource were the GNC, Uniqlo and Vitamin Shoppe agreements referenced above. The auditor reviewed those agreements, but they did not change the Division's opinion on the taxability of the subscription services.

119. At the hearing, the auditor testified that FacilitySource was a "management company who hires third party contractors to perform services to its customer." She further testified that FacilitySource provided "what they call as trade services, which are repairs and maintenance to their customers['] properties and subscription services, which is the use of their fmPilot software."

120. The auditor testified that she did not determine the actual usage of the fmPilot software by FacilitySource's customers in New York because FacilitySource did not have any licensing fees, and she believed "it meant as many stores and staff can use it as possible," and therefore, she assumed 100% store-level use in New York.

¹⁰ Although the audit covered the period September 1, 2013 through February 28, 2017, no tax was determined to be due for the period March 1, 2016 through February 28, 2017 because FSNE's only customer, A&P declared bankruptcy in 2015 and closed its stores.

121. The auditor testified that she never saw fmPilot in operation, but “believed” the vendor list was available to FacilitySource’s customers “within the software and therefore also considered the subscription fees to be the sale of information services.”

122. The record does not include FSNE’s management agreement with A&P. In addition, petitioners did not offer any testimony regarding A&P’s use of the fmPilot software either within or without New York State.

123. FacilitySource requested a conciliation conference with BCMS. After a conciliation conference, the conciliation conferee issued a conciliation order (CMS No. 000302283), dated April 26, 2019, sustaining the four notices of determination.

124. FSNE requested a conciliation conference with BCMS. After a conciliation conference, the conciliation conferee issued a conciliation order (CMS No. 000302284), dated April 26, 2019, sustaining the notice of determination.

125. On July 23, 2019, FacilitySource filed a timely petition challenging the four notices of determination. On October 2, 2019, the Division filed its answer. With permission, the Division filed an amended answer for the FacilitySource matter on October 6, 2021.

126. On July 23, 2019, FSNE filed a timely petition challenging the notice of determination. On October 2 2019, the Division filed its answer. With permission, the Division filed an amended answer for the FSNE matter on October 6, 2021.

127. Petitioners were served copies of their respective audit files on June 9, 2020.

128. On November 1, 2019, FacilitySource made a demand for verified bill of particulars. On November 29, 2019, the Division filed its responding bill of particulars. On October 28, 2021, FacilitySource made another demand for verified bill of particulars. On

November 17, 2021, the Division filed its responding bill of particulars related to the amended answer filed on October 6, 2021.

129. On November 1, 2019, FSNE made a demand for verified bill of particulars. On November 29, 2019, the Division filed its responding bill of particulars. On October 28, 2021, FSNE made another demand for verified bill of particulars. On November 17, 2021, the Division filed its responding bill of particulars related to the amended answer filed on October 6, 2021.

130. Along with their initial brief, petitioners filed a motion to strike or for order of preclusion under 20 NYCRR 3000.6 (a). In support of their motion, petitioners submitted a document titled “Motion to Strike or for Order for Preclusion (with attached Memorandum),” dated and signed by petitioners’ representative, Michael S. Marino, Esq., on September 8, 2023. No notice of motion was included in petitioners’ supporting papers.

131. By letter dated September 13, 2023, the undersigned Administrative Law Judge informed the parties’ representatives that the Division’s response to petitioners’ motion to strike or for an order of preclusion would be due on October 13, 2023, and that petitioners’ motion would be addressed in the determination issued in these consolidated matters.

132. On October 13, 2023, the Division filed the affirmation of Eric R. Gee, Esq., in opposition to petitioners’ motion to strike or for order of preclusion.

133. Pursuant to 20 NYCRR 3000.15 (d) (6), petitioners submitted 143 proposed findings of fact. In accordance with State Administrative Procedure Act (SAPA) § 307 (1), proposed findings of fact 1, 2, 4, 5, 7-9, 11-17, 19-24, 26-28, 32, 37, 39-43, 45, 46, 48-50, 56, 58-64, 70, 75-80, 84-92, 96, 97, 100, 103, 107, 108, 110, 111, 113, 115, 122, 129, 131, 133, 134 and 137-143 are supported by the record, and have been combined, renumbered and substantially

incorporated herein. Proposed findings of fact 6, 65, 81, 82, 98, 99, 101, 102, 106, 127, 130 and 135 have been modified to more accurately reflect the record and, as modified, have been combined, renumbered, and substantially incorporated herein. Proposed findings of fact 3, 83, 117, 120 and 126 are argumentative. Proposed finding of fact 109 is conclusory. Proposed findings of fact 18, 29, 30, 33-36, 93, 94, 116, 118, 119, 121 and 136 have been rejected. If any part of a proposed finding of fact is not supported by the record, it has been rejected in its entirety. Proposed findings of fact 10, 25, 31, 38, 44, 47, 51-55, 57, 66-69, 71-74, 95, 104, 105, 112, 114, 123-125, 128 and 132 are irrelevant.

134. Pursuant to 20 NYCRR 3000.15 (d) (6), the Division submitted 88 proposed findings of fact. In accordance with SAPA § 307 (1), proposed findings of fact 1-25, 27-34, 36-41, 44, 45, 47-52, 54-56, 60, 61, 63-66, 68-73, 75, 77-80, 82 and 86-88 are supported by the record and have been combined, renumbered and substantially incorporated herein. Proposed findings of fact 42, 43, 57, 62, 67, 81, 84 and 85 have been modified to more accurately reflect the record and, as modified, have been combined, renumbered, and substantially incorporated herein. Proposed findings of fact 26, 35, 46, 53, 58, 59, 74 and 76 have been rejected. If any part of a proposed finding of fact is not supported by the record, it has been rejected in its entirety. Proposed finding of fact 83 is irrelevant.

CONCLUSIONS OF LAW

A. Petitioners' motion to strike or for an order of preclusion must be denied. Petitioners did not include a notice of motion with their motion papers. The Tax Appeals Tribunal (Tribunal) in *Matter of Silvestri* (Tax Appeals Tribunal, March 17, 2022), held that "[a] notice of motion is required under our Rules of Practice and Procedure (20 NYCRR 3000.5) and is necessary to 'ensure that the elements of due process are present' in our procedures" (citing Tax

Law § 2000; *Burstin v Public Serv. Mut. Ins. Co.*, 98 AD2d 928, 929 [3d Dept 1983]).”

Petitioners’ failure to include a notice of motion renders the motion invalid (*see id.*). As such, petitioners’ motion must be denied.

B. It is well established that a presumption of correctness attaches to a properly issued statutory notice issued by the Division and the taxpayer bears the burden to prove that the assessment is incorrect (*see Matter of Hotel Depot, Inc.*, Tax Appeals Tribunal, January 24, 2020, citing *Matter of Darman Bldg. Supply Corp. v Mattox*, 106 AD3d 1150, 1151 [3d Dept 2013]; *Matter of Blodnick v New York State Tax Commn.*, 124 AD2d 437, 438 [3d Dept 1986], *appeal dismissed* 69 NY2d 822 [1987]). Although a determination of tax must have a rational basis in order to be sustained, the presumption of correctness raised by the issuance of the assessment, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment (*see Matter of Leogrande v Tax Appeals Trib.*, 187 AD2d 768, 769 [3d Dept 1992], *lv denied* 81 NY2d 704 [1993]). However, a determination of tax must have a rational basis to be sustained upon review (*see Matter of Grecian Sq. v New York State Tax Commn.*, 119 AD2d 948, 950 [3d Dept 1986]). If it has no rational basis, it must be set aside (*see Matter of Snyder v State Tax Commn.*, 114 AD2d 567, 568 [3d Dept 1985]; *Matter of Ristorante Puglia v Chu*, 102 AD2d 348, 350 [3d Dept 1984]). In *Matter of Atlantic & Hudson Ltd. Partnership* (Tax Appeals Tribunal, January 30, 1992), the Tribunal established how the presumption of correctness of an assessment may be overcome:

“Although a determination of tax must have a rational basis in order to be sustained upon review, the presumption of correctness raised by the issuance of the assessment, in itself, provides the rational basis, so long as no evidence is introduced challenging the assessment. Evidence that both rebuts the presumption of correctness and indicates the irrationality of the audit may appear: on the face of the audit as described by the Division through testimony or documentation; from factors underlying the audit which are developed by the petitioner at hearing; or in the inability of the Division to identify the bases of the

audit methodology in response to questions posed at the hearing” (citations omitted).

The record must provide sufficient evidence to allow the trier of fact to determine whether the audit had a rational basis (*see Matter of Hammerman*, Tax Appeals Tribunal, August 17, 1995).

C. Based upon its conclusion that FacilitySource’s subscription services were taxable sales of prewritten software, the Division issued four notices to FacilitySource asserting additional tax due for the period December 1, 2009 through February 28, 2017. After an audit of FSNE, the Division concluded that its sales of subscription services to A&P were taxable sales of prewritten software and additional tax was also due on its trade services for the period September 1, 2013 through February 29, 2016. Petitioners argue that the notices lack a rational basis because the Division did not have the information necessary to determine the primary function of their facilities management services because the Division never requested it. Petitioners assert that the Division’s auditor did not understand IFM and, therefore, could not determine the primary function of the integrated service. This argument is unpersuasive.

Upon commencing the audit of FacilitySource, the auditor issued an IDR requesting, among other things, all exemption documents supporting non-taxable sales, including a catchall phrase stating, “[a]ny other documentation necessary to prove non-taxable sales.” On April 14, 2016, the auditor sent an email to FacilitySource requesting, among other things, preliminary information regarding the nature of FacilitySource’s sales/services. A responding email dated April 14, 2016, from Ms. Poole, a FacilitySource employee, described FacilitySource’s business model. On October 3 and 4, 2016, the auditor went to petitioners’ Phoenix, Arizona, offices to conduct a field audit of FacilitySource. On October 3, 2016, the auditor met with three FacilitySource employees, Ms. Poole, Mr. Blackhurst and Mr. Tsujimura. During that meeting, the auditor and those employees discussed different components of FacilitySource’s business

including trade services and subscription services. At that time, the employees told the auditor that the subscriptions were for the use of the fmPilot software. During the October 2016 audit visit, the auditor reviewed the federal income tax returns for the years 2012 through 2015, and requested additional information needed for review. In response to her request, she received FacilitySource's sales tax returns, revenues for the years 2014 and 2015, by state, for both subscriptions and trade services, subscription figures for 2010 through 2013, and FacilitySource's customer lists. Subsequently, the auditor issued two additional IDRs regarding the FacilitySource audit. After learning of the existence of FSNE during her October 2016 visits, the auditor was assigned to and conducted an audit of FSNE as well. During the course of her audit of FSNE, the auditor issued two IDRs. Prior to returning to FacilitySource's Phoenix, Arizona, offices for a second field audit appointment and the commencement of the field audit of FSNE on May 8 and 9, 2017, the auditor sent an email to Ms. Bobbe and Mr. Tsujimara recapping the additional information needed for the audits of both companies. The additional information requested for both companies included sales details for subscriptions and sales reports for all everywhere sales as well as New York sales broken down by quarter for the audit period, which at that time was December 1, 2009 through August 31, 2016 for FacilitySource, and September 1, 2013 through August 31, 2016 for FSNE. During the May 8 and 9, 2017 audit appointments of both companies, their respective audit periods were extended through the period ending February 28, 2017.

Upon review and reconciliation of the documents provided, the auditor found that neither FacilitySource nor FSNE were collecting tax on their subscription sales and had a duty to determine whether tax was due on those subscriptions. During the course of the audits of petitioners, the auditor requested information, including revenue and location lists, that provided

more than enough notice to petitioners that an evaluation of the taxability of subscriptions was taking place. Petitioners had ample opportunity to provide the Division with evidence that would dissuade it from assessing tax on both companies' subscription sales. During both companies' audits, petitioners only provided accounting information, including sales tax returns, sales reports, and customers' location lists. Despite two separate audit visits to FacilitySource's Phoenix, Arizona, offices, none of the FacilitySource employees with which the auditor interacted offered her a tour of the FacilitySource facilities including the call center. Indeed, petitioners did not provide the Division with any evidence of the nature of the companies' services exclusive of the descriptions provided by FacilitySource employees. Even after petitioners were aware that the auditor intended to assess tax on the companies' subscription services, they failed to provide any information about their products. The auditor kept the audits open for an additional two months until petitioners advised that they had no further documents and would continue to work on the cases prior to the BCMS proceedings. Contrary to petitioners' assertions that the auditor did not understand their businesses, petitioners failed to provide any documentation that supported their position.

Based upon the information she reviewed during the audits, the auditor's conduct and conclusions in both audits were rational. Both petitioners presented the auditor with an untaxed revenue stream, i.e., subscriptions, that represented a bundled package with a software component. While petitioners may disagree with the auditor's conclusions as to what the companies' sell, that does not render either the Division's audits or the notices irrational.

D. Tax Law § 1105 (a) imposes sales tax on the retail sale of tangible personal property, which includes "prewritten software" (*see* Tax Law § § 1101 [b] [6]; 1105 [a]). "Sale" is defined as:

“[a]ny transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume (including, with respect to computer software, merely the right to reproduce), conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor” (Tax Law § 1101 [b] [5]).

20 NYCRR 526.7 (e) (4) provides that a transfer of possession has occurred if there is actual or constructive possession, or if there has been a transfer of “the right to use, or control or direct the use of, tangible personal property.”

In these consolidated matters, the Division concluded that petitioners’ subscription sales of facilities management services included sales of prewritten software and were subject to tax. In their brief, the Division acknowledged that, in addition to prewritten software, petitioners also sold services as part of a mixed bundle of property and services.

Petitioners point out that the parties stipulated to the components of the facilities management services. Specifically, that

“[p]etitioner provided its customers facilities management services that include 24/7 call-in transaction access, web-based portal access, work order management, vendor management, electronic invoicing and data analytics, under the single moniker – IFM.”

Petitioners argue that the testimony and evidence presented at the hearing clearly established that the facilities management service that each company provides is an integrated service made up of different components. Although petitioners acknowledge utilizing technology, specifically computer software in the form of the fmPilot software, petitioners assert that they neither sell the same nor is it the primary function of their businesses. Rather, petitioners assert that the primary function of their business is to provide facilities management services to their customers.

Petitioners claim that they are “merely tech enabled.” Petitioners maintain that the fmPilot software operates either via the portal or app. Petitioners further maintain that fmPilot is used by petitioners’ customers to communicate work orders and is used by petitioners and vendors to

communicate regarding actions taken to resolve work orders and invoice the customers.

Petitioners argue that fmPilot is a software ticketing system that does not conduct any function on its own. Rather, it is merely a communication tool between customers and petitioners and petitioners and their vendors. Petitioners further argue that it is not a technical replacement for their hundreds of operations employees or call center employees. Petitioners assert that from entering a work order through invoicing, humans are performing the facilities management service, not fmPilot.

E. Where the sale of bundled taxable and nontaxable services is considered, the taxation of such is determined according to the primary function of the bundle (*see Matter of Strata Skin Sciences, Inc.*, Tax Appeals Tribunal, May 5, 2022). However, the Tribunal has reserved judgment on whether “all mixed bundled sales of tangible personal property and services should be analyzed using the primary function test” (*id.*). In these consolidated matters, petitioners’ witnesses testified that the fmPilot software is a CMMS. FacilitySource’s website and advertising never fail to state that fmPilot is an integral part of the IFM product. Further, Mr. Hayden acknowledged that the fmPilot software is part of the overall package to deliver the service. Mr. Hayden also agreed that petitioners’ business would not function the way it does without the fmPilot software or another CMMS.

The technical elements of the fmPilot software are integral to petitioners’ business. Mr. Hayden testified that FacilitySource had the fmPilot software created because it was not satisfied with the CMMS it had been using. During the audit period, the fmPilot software was upgraded. Petitioners had a staff of 15 to 20 people to maintain the functionality of the software. The fmPilot software is not merely an application that petitioners sell to interface with their customers; petitioners’ call center employees and operations employees also use the software

itself to provide streamlined facilities management services. Petitioners license the fmPilot software to their customers. Section 12 (c) of both the Uniqlo and Vitamin Shoppe agreements state that “FacilitySource does hereby grant to Customer a non-exclusive, revocable, limited license to use the fmPilot software to (a) copy, distribute, transmit, display and *otherwise use* fmPilot” (emphasis added). As such, FacilitySource contracted with its customers to permit them to enjoy the functionality of the software and not access to a communication portal. As opposed to a mere communication portal, petitioners’ witnesses acknowledged that the customer may see calendars of work, review service orders, submit work orders, and program in price limits for anticipated facility maintenance.

Clearly, FacilitySource sold subscriptions comprised of access to a bundle of prewritten computer software and services for one charge (*see Matter of Strata Skin Services.*; *see also* 20 NYCRR 527.1 [b]). When a bundle of taxable and non-taxable property is sold together for one charge, the entire charge is taxable (*see Matter of Strata Skin Services*). The Division’s determination that FacilitySource’s subscriptions were taxable prewritten software was proper.

F. Petitioners claim that FSNE’s customer A&P did not use the fmPilot software at the store level. The record does not include a copy of FSNE’s maintenance management agreement with A&P. In addition, petitioner did not offer any testimony regarding A&P’s use of the fmPilot software either within or without New York State. As such, FSNE has failed to prove that its maintenance management agreement with A&P did not allow for the use of the fmPilot software at its New York State locations.

G. Based upon conclusions of law E and F, petitioners sold prewritten software along with other components for one single subscription charge and the Division’s determination that the petitioners’ subscriptions were taxable sales was proper.

H. In addition to its determination that FSNE's subscription sales were taxable, the Division also determined that additional tax was due on trade services due to jurisdictional errors and sales that were not capital improvement work. Petitioners have provided no arguments regarding the Division's determination of additional tax due on FSNE's trade services. As such, the Division's determination that additional tax was due on trade services was proper.

I. The Division raises two alternative arguments regarding the taxability of petitioners' subscriptions. The Division's first alternative argument is that petitioners sold a taxable information service and failed to collect the tax. The second alternative argument is the primary function of petitioners' facilities management services is to maintain real property, and such maintenance of real property is subject to tax. Although it was determined in conclusions of law E, F and G that petitioners' subscriptions are subject tax, for completeness of the record, I will address the Division's alternative arguments.

J. Tax Law § 1105 subjects certain enumerated services to tax. Among the services subject to tax is the furnishing of information by printed, mimeographed or multigraphed matter or by duplicating written or printed matter in any other manner, including the services of collecting, compiling or analyzing information of any kind or nature and furnishing reports thereof to other persons (*see* Tax Law § 1105 [c] [1]; *see also* Tax Law § 1105 [c] [9] [furnishing information services provided by means of telephony or telegraphy or telephone or telegraph service of whatever nature subject to sales tax so long as such would be subject to sales tax pursuant to Tax Law § 1105 [c] [1] if it were furnished by one or more means enumerated therein]). There is a distinction between a taxable information service and the furnishing of a nontaxable service where the information is merely a component of that service. In *Matter of*

SSOV '81 Ltd. (Tax Appeals Tribunal, January 19, 1995), the Tribunal explained that an information service has been interpreted to mean:

“the sale of the service of furnishing information by a business whose function it is to collect and disseminate information which is taxable under Tax Law § 1105 (c) (1) and not the mere sale of information’ In order to determine a service’s taxability, the analysis employed by the New York courts and the Tax Appeals Tribunal focuses on the service in its entirety, as opposed to reviewing the service by components or by the means in which the service is effectuated” (emphasis and citations omitted).

In *Matter of SSOV '81 Ltd.*, the Tribunal focused on the “primary function” of the service, which was to enable members of a dating referral service to meet others. In concluding that such primary function was not one of the enumerated taxable services set forth in Tax Law § 1105 (c), the Tribunal recognized that the proper focus should be on the primary function itself and not upon whether the service might, as an incident thereof, involve the provision of information (*id.*). In so holding, the Tribunal stated that “[t]o neglect the primary function of petitioners’ business in order to dissect the service it provides into what appears to be taxable events stretches the application of Article 28 far beyond that contemplated by the Legislature” (*id.* [footnote omitted]).

K. Under the foregoing conclusion of law J, to be an information service, the taxpayer’s primary function must be the business of furnishing information, including the services of collecting, compiling, or analyzing information and furnishing reports thereof. Petitioners provided their customers facilities management services that included 24/7 call-in transaction center access, web-based portal access, work order management, vendor management, electronic invoicing, and data analytics. Petitioners used the data analytics to provide their customers with reports about their services and the status of their facility management. FacilitySource offered five such reports into evidence. Petitioners’ reporting is an information service because they

compiled information gleaned from a client's facilities maintenance services data, organized the information and presented the information to the customer (*see Westwood Pharms. v Chu*, 164 AD2d 462, 464-465 [4th Dept 1990], *lv denied* 77 NY2d 807 [1991]). Information services like written reports, generated from client information are generally considered personal and individual to the respective client and excluded from tax (*id.*). However, if such information may be incorporated into reports for others, the reports are no longer considered personal and individual (*see Matter of Towne-Oller & Assoc. v State Tax Commn.*, 120 AD2d 873, 874 [3d Dept 1986]; *Matter of Dynamic Logic, Inc.*, Tax Appeals Tribunal, January 20, 2022). Two of FacilitySource's witnesses testified that they used benchmarks to compare the facility management services data of the customer with that of other customers. Although both witnesses testified that the benchmark information was anonymized, the lack of identifying information is irrelevant when it comes from the same common database (*see Matter of Dynamic Logic*). Furthermore, this information is important to the customer because it permits the customer to see how it compares to other businesses. Since the benchmark data is culled from the same database, the information is incorporated into various customers' reports and cannot be excluded from tax as personal and confidential (*id.*). Based on the foregoing, petitioners' subscription product would be taxable as an information service that does not qualify for the exclusion from tax.

L. Lastly, the Division, in the alternative, asserts that the primary function of petitioners' facilities management services is to maintain property, and such maintenance of real property is also subject to tax (*see* Tax Law § 1105 [c] [5]). The Division asserts that petitioners' customers are provided with facilities maintenance, actual work to real property, and petitioners' advice about how to keep that real property in "a condition of fitness, efficiency, readiness or safety or

restoring it to such condition” (*see* 20 NYCRR 527.7 [a] [1]). The Division argues that petitioners provide reports detailing their customers’ facility management data. The customer then seeks a facilities management solution. The Division points out that Mr. Hayden defined facilities management as “tactical,” with a goal “to resolve that work order efficiently, timely, make sure clients are paying the right price.” The Division contends that although petitioners invoiced the charges for trade services and subscriptions separately, they are integral to each other. The Division argues that the trade services and subscriptions are comparable to the facts in *Matter of Penfold v State Tax Comm* (114 AD2d 696, 697 [3d Dept 1985]). The Division’s reliance on *Matter of Penfold* is misplaced. In that matter, the petitioner unsuccessfully argued that the disposal of refuse and its pickup and delivery were two distinct transactions (*id.*). The State Tax Commission and the Third Department both concluded that the customer purchased one service, removal of refuse, and that the two services could not be divided into two separate services arising out of the same transaction (*id.*). Here, petitioners are not performing both the facilities management services and the ultimate repairs to the property, as was being done by Penfold.

Based on the foregoing, the Division’s argument that the primary function of petitioners’ facilities management services is to provide the taxable service of maintaining, serving, and repairing property, which includes charges for trade services and the means, via the IFM bundle, to effectuate the same fails. Petitioners’ facilities management services would not be taxable under Tax Law § 1105 (c) (5).

M. Petitioners’ motion to strike or for order for preclusion is denied.

N. The petition of FacilitySource, LLC is denied, and the notices of determination, dated November 21, 2017, are hereby sustained. The petition of FacilitySource Northeast Services, LLC, is denied, and the notice of determination, dated November 22, 2017, is hereby sustained.

DATED: Albany, New York
May 09, 2024

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE