New York State Department of Taxation and Finance

Office of Counsel
Advisory Opinion Unit

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Corporation Tax
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STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION PETITION NO. C080408B

A petition received April 8, 2008 requests an advisory opinion about how Company A's receipts should be allocated for purposes of calculating the numerator of the receipts factor of the business allocation percentage under Article 9-A. Company A's receipts from advertisers that have a CPC price structure arrangement should be allocated to New York when a New York subscriber clicks on the advertisement. Company A's receipts from advertisers that have fee structures based on CPM arrangements should be allocated to New York based on the ratio of New York subscribers to subscribers everywhere.

Facts

Company A, a Delaware Company, owns and operates a social networking website that connects subscribers with friends, coworkers, and neighbors. The site is open to anyone with a valid email address. Before subscribers join, they must create a "profile" that allows the subscriber to share his or her name, location, interests, and other personal information. Company A then directs the subscriber to networks that share attributes contained in the subscriber's profile.

Company A also provides online advertising services to advertisers. The advertisers seek to target audiences that share specific demographic attributes. Company A generates revenues by delivering online advertisements to target audiences using two pricing structures: cost per clickthrough (CPC) and cost per thousand impressions (CPM). A clickthrough occurs when a subscriber clicks on an advertisement and reaches a site of the advertiser's choosing. An advertiser whose fee structure is based on CPC pays Company A a fee for each time an advertisement is clicked by a user. An advertiser whose fee structure is based on CPM pays a fee for each time an advertisement is displayed on a subscriber's computer screen.

Company A maintains sales and marketing representatives, IT support staff, and account managers in several states. The company's servers and routers facilitate the routing of advertising traffic on its social networking site. The server equipment and IT personnel are located in California and Virginia. The sales representatives are located in California, Virginia, New York and elsewhere. The sales representatives execute advertising arrangements with online marketers. The IT support staff develops software applications that allow Company A to deliver advertisements to subscribers, provide technical support for the company's sales and marketing divisions, and manage the network of servers and routers. The IT support personnel also perform the tasks necessary to load the advertisements on to the servers and deliver them to subscribers. The New York sales representatives only solicit clients to advertise on Company A's website. The company maintains no servers in NY and does not provide any infrastructure or IT support for the site functionality in New York. No New York personnel are involved in uploading or maintaining advertising content.

Company A incurs substantial costs in providing a platform to host and disseminate advertising on the internet, including network maintenance, data center operations, technical support personnel, server and network hosting services, sales and marketing activities, depreciation and amortization expenses with respect to server equipment, and storage, repair and maintenance of server equipment. Except for costs attributable to Company A's New York sales personnel, all costs were incurred outside New York.

Opinion

Tax Law § 210.3(a)(2)(B) requires that taxpayers include in the numerator of their business allocation percentage their income from "services performed within the state," and provides that, for publishers of newspapers and periodicals, "receipts arising from sales of advertising…shall be deemed to arise from services performed within the state to the extent that such newspapers and periodicals are delivered to points within the state." A Tax Department regulation interprets this to mean that publishers' New York receipts from sales of advertising should be "based on the ratio of the New York circulation of the newspaper or periodical containing such advertising to the total circulation of such newspaper or periodical." 20 NYCRR 4-4.3(d)(3). The same regulation treats radio and television advertising similarly, mandating that a lump sum received for the service of broadcasting a commercial message "must be allocated to New York State and another state or states according to the number of listeners and viewers in each state." 20 NYCRR 4-4.3(d)(2). Subsequent departmental guidance, issued in the absence of any statute or regulation governing the allocation to New York of revenue from advertising via cable programming, likewise concluded, by analogy to this regulation, that a cable television corporation "should base the allocation of advertising revenue on the ratio of its New York subscribers to the number of cable programming subscribers everywhere." New York Guidance Memo NYT-G-07(1).

The governing principle is to base the allocation, to the extent possible, on the number of people who view or read the advertisement in New York. Company A's sales of advertising that appears on its website differ in no pertinent way from the sales of advertising by publishers, broadcasters, and cable providers. Although a website operator may not have any way of knowing where a subscriber is when (s)he views or clicks on an advertisement on the website, basing the apportionment on the location of the subscriber should provide a close approximation of this figure. Accordingly, Company A should base the allocation of its internet advertising revenue on the ratio of its New York subscribers to the number of subscribers everywhere. Specifically, receipts from advertisers that have a CPC price structure arrangement, where the advertiser pays Company A each time an advertisement is clicked on by a subscriber, would be allocated to New York when a New York subscriber clicks on the advertisement. For fee structures based on CPM arrangements, where Company A is paid based on where the advertisement is displayed, advertising receipts would be allocated to New York based on a ratio of the number of New York subscribers, to the total number of subscribers everywhere.

Company A suggests incorrectly that its advertising receipts should not be allocated to New York because its employees do not perform any income-generating services in New York. Company A contends that its advertisement fees result from the services performed by Company A's IT personnel, servers, and routers relating to its website functionality, including the management and upkeep of servers that generate and deliver advertising impressions to subscriber groups. Also, even though Company A employs sales representatives in New York who execute the advertising arrangements with online marketers that generate this advertising revenue, it maintains that these sales activities do not warrant any allocation of this revenue to New York. However, the advertising receipts generated by Company A are properly based on the number of times a New York subscriber clicks on or views an advertisement, and not on the activities of IT staff and management that are directly related to its website, wherever these employees may be located.

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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.