Business Aircraft Sales Tax Planning:

Sales and use tax considerations.

Chris Younger is a partner at GKG Law, P.C. practicing in the firm's Business Aircraft Group. He focuses his legal practice on business aircraft transactions as well as issues relating to federal and state taxation and regulation of business aircraft ownership and operations. Mr. Younger can be contacted at cyounger@gkglaw.com

With careful planning, a business aircraft purchaser can substantially reduce or completely eliminate sales and use tax liability on a business aircraft purchase, advises attorney Chris Younger.

A primary consideration for the Board of Directors in connection with the acquisition of a business aircraft is understanding and addressing potential sales and use tax liability and, if possible, avoiding or mitigating that expense.

Most deliveries of new and used aircraft occur in states with either no sales tax or an applicable "fly away" exemption, resulting in no sales tax being owed on the aircraft purchase at closing. However, many buyers fail to recognize that a concomitant liability, known as a use tax, may arise with respect to the subsequent storage or other use of a business aircraft in one or more particular states. The use tax is equal to the sales tax as if the transaction had actually closed in the state that imposes it. Since the sales and use tax rate in most states is in excess of 5% of the purchase price, this liability may exceed $1,000,000 without proper planning.

Companies often do not engage in any sales and use tax planning prior to their acquisition of a business aircraft and unwittingly end up with a large liability for sales or use tax that they cannot ›

continued on page 56

subsequently unwind. This article will identify some important sales and use tax planning issues that a Board should consider.

States thoroughly and carefully scrutinize opportunities to apply their sales and use tax to aircraft based - or even temporarily stored - within their borders. For example, California and Texas send out notification to all aircraft owners requiring proof of payment of sales or use tax or, if any exemption from the tax is claimed, requesting documentation that adequately supports the application of the claimed exemption. The Board must ensure that a company is prepared for such an inquiry before the company acquires a business aircraft.

Additionally, the Board must understand that strategies for sales and use tax mitigation or avoidance are difficult to administer, overly time-consuming and sometimes confusing. States often insist that qualifying for a particular exemption from aviation sales or use tax requires the taxpayer to follow exactly each intricate step involved in such compliance precisely, and in a particular order. For example, in Florida and New York, the process may involve having certain items, such as dry leases or retail sales registrations, in place prior to the acquisition of the property in question.

In many instances, it is impossible to know what a state requires without having previously encountered and engaged in the process designed by that state.

ATTENTION TO DETAIL

Setting up an internal dry lease between related parties (i.e. a sale for resale transaction) is a common planning technique. However, there are numerous "gotchas" that arise in connection with the use of a leasing structure.

For example, the Texas Comptroller carefully scrutinizes aircraft dry leases between related parties and, absent adequate recordkeeping and supporting documentation, will treat those leases as "sham" transactions, to which the sale-for-resale exemption from Texas sales and use tax is almost automatically denied. Texas, like all states, looks for evidence of an "arm's-length" transaction between the lessor and the lessee, such as the actual payment of fair market value rent by the lessee to the lessor.

In New York and New Jersey, as in many other states, sales tax on lease rent may be calculated on an "accelerated" basis, meaning that the tax is due at the time of lease signing and is owed up front on all the rent that will accrue during the term of the aircraft lease. Therefore, it is imperative that the Board understand and follow all requirements imposed by a specific state in connection with the use of such a structure.

The Board should avoid cavalier planning, planning that is not based on a specific statutory exemption or procedural structure, or planning that is based on something relied on in a prior aircraft purchase. Laws and their interpretation by state taxing authorities often change.

Most importantly, avoid planning based on "cocktail party" talk where you hear that "everyone is doing it" this way, or that way. Naturally, all such informal conversation or "common wisdom" reinforces the need for thorough tax planning prior to the purchase of a business aircraft.

Note: This article should not be construed as legal advice or legal opinion on any specific facts or circumstances. The reader is urged to consult legal counsel or other advisors concerning his/her own situation and specific legal questions.

Do you have any questions or opinions on the above topic? Get them answered/published in World Aircraft Sales Magazine. Email feedback to: Jack@avbuyer.com

Business Aviation and the Boardroom continues on Page 58

"Laws and their interpretation by state taxing authorities often change."