

Letter of Findings: 06-0489
Sales and Use Tax
For the Year 2005

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ISSUE

I. Sales and Use Tax – Imposition on Aircraft Purchase.

Authority: IC § 6-8.1-5-1, IC § 6-2.5-3-2, IC § 6-2.5-3-4, IC § 6-2.5-5-8, IC § 6-2.5-4-10, IC § 6-2.5-2-1, IC § 6-2.5-8-8, [45 IAC 2.2-3-4](#), [45 IAC 2.2-5-15](#), *Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue*, 867 N.E.2d 289 (Ind. Tax. Ct. 2007), *Indiana Dept. of Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

Taxpayer protests denial of rental exemption and subsequent imposition of use tax on the purchase of an aircraft.

STATEMENT OF FACTS

Taxpayer, a single-member LLC, purchased an aircraft but did not pay sales tax on the purchase, claiming an exemption for rental or lease to others. The Indiana Department of Revenue ("Department") reviewed the claim for exemption and determined that taxpayer did not qualify for the exemption. The Department denied the claim for exemption and issued a proposed assessment for use tax on the purchase of the aircraft. Taxpayer protests the assessment. A hearing was held where Taxpayer was represented by its accountant. This Letter of Findings ensues. Additional facts will be provided as needed.

I. Sales and Use Tax – Imposition on Aircraft Purchase.

DISCUSSION

All tax assessments are presumed to be accurate. The taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(b); *Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Indiana imposes a use tax on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction. IC § 6-2.5-3-2; [45 IAC 2.2-3-4](#). IC § 6-2.5-3-4(a)(2) allows for a use tax exemption for property that is acquired in a transaction that is exempt from sales tax under IC § 6-2.5-5, and the property is being stored, used, or consumed for the purpose for which it was exempted. One of those exemptions is found at IC § 6-2.5-5-8(b) which states that,

Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property.

The rental exemption set out in IC § 6-2.5-5-8 is further explained in [45 IAC 2.2-5-15](#), which states:

(a) The state gross retail tax shall not apply to sales of any tangible personal property to a purchaser who purchases the same for the purpose of reselling, renting or leasing, in the regular course of the purchaser's business, such tangible personal property in the form in which it is sold to such purchaser.

(b) General rule. Sales of tangible personal property for resale, renting or leasing are exempt from tax if all of the following conditions are satisfied:

(1) The tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it;

(2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and

(3) The property is resold, rented or leased in the same form in which it was purchased.

When a taxpayer claims it is entitled to a tax exemption, it bears the burden of proving that the terms of the exemption have been met. *Indiana Dep't. of Revenue v. Interstate Warehousing*, 783 N.E.2d 248, 250 (Ind. 2003). The Department will strictly construe the exemption statutes against the taxpayer claiming the exemption. *Id.*

The above exemption, therefore, requires compliance with three elements. One of these requirements is that the Taxpayer must be engaged in the reselling, renting, or leasing of such property in its regular course of business.

When the Department attempted to verify the exempt use of the aircraft from the purchase date, it requested that Taxpayer provide several pieces of documentation that would substantiate whether Taxpayer was leasing its aircraft in the regular course of its business.

The Department asked for "a complete flight schedule/log of all aircraft flights including the date of the use, the entity's name and address leasing the aircraft and the amount charged to lease the aircraft from the date of purchase to present." Taxpayer responded by sending in a document that it called a "complete flight log." The document was not a complete flight log. It did not log each use of the aircraft, including date and time, who rented

the aircraft, for how long, and at what rate. Rather, the document – a simple word-processed document with no unique identifiers – simply summarized total hours purportedly used for each of September, October, November, and December of 2005, along with the total revenue for each of those months. At the hearing, the Department repeated the request for a detailed flight log. Subsequently, Taxpayer presented a similar summary document for 2006; however, this document did not even contain month-by-month totals.

The Department also requested, more than once, copies of lease agreements, including rental rates, that govern the rental transactions between Taxpayer and the lessees of the aircraft. This highly relevant documentation was not provided by Taxpayer.

The Department also requested, more than once, evidence of arms-length rates charged to lessees of the aircraft. Taxpayer offered no documentary evidence of rental rates. Taxpayer stated, in a November 3, 2006, letter to the Department, that "rental rates are \$125 per hour with renter responsible for fuel. Rates are posted in the hanger on the wall as follows: 'RENTAL RATES \$ 125 PER HOUR'." Also, the 2005 summary mentioned above states, "renters pay a minimum of 5 hour[s] no matter how many they actually log, therefore the actual rental revenue charged for 2005 is \$196 pr hr plus fuel." Then, the 2006 summary of total hours states, "net flying time – 150 times \$125 hour." The rate, as stated by Taxpayer, seems to have been reduced significantly from 2005 to 2006, the following year. At the hearing, Taxpayer stated that three qualified pilots rent the aircraft for a minimum of four hours per month at \$155 per hour with renter responsible for fuel if the aircraft is actually flown. Taxpayer has made contradictory statements as to the rental rate(s) of the aircraft and has not provided any documentary evidence as to the rates.

Taxpayer provided, upon the Department's request of a copy of its insurance policy, a copy of the "coverage indemnification page" of the policy along with its various endorsements. The policy was approved on September 15, 2006. The policy's "Use of the Aircraft" (Item #10) condition reads:

The aircraft will be used for your pleasure and business related purposes where no charge is made for such use and also may be used for Other Uses described below: Other Uses: NONE.

At the hearing, Taxpayer suggested that insurance companies do not treat this stipulation as precluding lease arrangements with third parties and offered to provide documentation in support of this proposition. After the hearing, Taxpayer forwarded an email response from an insurer (other than the Taxpayer's insurer); however, this email specifically explained that:

Item #10 in the policy which discusses no charges to others is directed toward 3rd parties. [Taxpayer's insurer], as well as any other aviation insurance company we might speak of, understands there is often internal rental of the plane between the shell corp. and its principals. You [Taxpayer] phrased this as "members" which is fine, as long as they are principals in the corporation and known to the insurance company. These people would not be considered "others." . . . Therefore, any charges made to them [the principals] would not be considered charges to others.

The above explanation confirms that rental to third parties would indeed violate the insurance policy's terms, contrary to Taxpayer's understanding. According to the quoted explanation, only use of the aircraft by Taxpayer's own principal is covered under the insurance policy. This point is further emphasized in the endorsements to the policy. Taxpayer presumably is leasing the aircraft to its single member (per listing of approved pilots in the policy) which is covered by the policy. However, Taxpayer is also presumably leasing the aircraft to third parties – otherwise Taxpayer would not be claiming the use tax exemption. This violates the terms of Taxpayer's insurance policy. Taxpayer is therefore underinsured. This issue of underinsurance may not be determinative on its own of whether or not Taxpayer is leasing the aircraft in the regular course of its business, but, taken with other factors, it calls the argument for exemption into question.

Taxpayer's aircraft was purchased September 1, 2005. The purchase price was \$145,000. Taxpayer reported total sales of \$5,208 in 2005 with sales tax due of \$312.48. For 2006, Taxpayer reported \$18,755 in sales, and \$1,125.30 in sales tax due. Taxpayer has not reported any sales or sales tax for 2007. Taxpayer stated at the hearing that its aircraft was involved in a crash in late 2006. Taxpayer stated it would provide documentary evidence, but did not.

Taxpayer provided, post-hearing, three invoices that appear to reflect monthly billing for use of the aircraft. The invoices show a separately listed sales tax. The invoices, however, state no descriptors that reference aircraft use. The invoices refer to total hourly fees per referenced month.

Again, when a taxpayer claims it is entitled to a tax exemption, it bears the burden of proving that the terms of the exemption have been met. *Indiana Dep't. of Revenue v. Interstate Warehousing*, 783 N.E.2d 248, 250 (Ind. 2003). The Department will strictly construe the exemption statutes against the taxpayer claiming the exemption. *Id.*

It could very well be that Taxpayer is leasing its aircraft in the regular course of its business. Taxpayer, however, has not provided the requisite documentary evidence. Taxpayer has relied mostly on its say-so in presenting information, and on evidence that is not specific or detailed enough for the Department to make proper determinations. Apart from reporting sales and the remittance of sales tax, the documentary evidence that is specific enough calls into question exempt use of the aircraft. Taxpayer has not met its burden to establish that it is actually in the business of leasing an aircraft, therefore, Taxpayer has not substantiated a qualified exempt use.

FINDING

Taxpayer's protest is respectfully denied.

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