

Letter of Findings: 09-0089
Gross Retail Tax
For 2008

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ISSUE

I. Aircraft Public Transportation Exemption – Gross Retail Tax.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-1(a); [IC 6-2.5-3-2](#); IC § 6-2.5-5-8(b); IC § 6-2.5-5-8(e); IC § 6-2.5-5-8(h); IC § 6-2.5-5-27; [IC 6-6-6.5-8](#)(d); Sales Tax Information Bulletin 12 (July 2007).

Taxpayer argues that it is not subject to use tax on the purchase of an aircraft on the ground that the aircraft is being used for public transportation.

STATEMENT OF FACTS

Taxpayer purchased an aircraft in May 2008 and brought it into the state one month later. Subsequent, Taxpayer submitted the Department of Revenue (Department) an "Application for Aircraft Registration or Exemption" (Form 7695) claiming that the purchase of the aircraft was not subject to sales tax because it was purchased for "Public Transportation under FAA Part 135." Along with that application, taxpayer provided documentation purporting to establish that taxpayer had entered into a lease agreement with an Indiana management corporation ("Charter Company").

On the ground that taxpayer – as the aircraft's lessor – was not in the business of providing public transportation, the Department of Revenue (Department) challenged taxpayer's claim that it was entitled to that particular exemption.

Thereafter, taxpayer submitted a substitute "Application for Aircraft Registration or Exemption" abandoning the transportation exemption claim. Instead, taxpayer claimed that it was not required to pay sales tax because the aircraft had actually been purchased for "Rental or Lease to others per [IC 6-2.5-5-8](#)."

Taxpayer acquired a Registered Retail Merchant's Certificate and began to collect lease payments from Charter Company. In addition, taxpayer charged, collected, and forwarded sales tax on the lease payments received from Charter Company.

The Department disagreed with taxpayer's claim that the initial purchase of the aircraft was not subject to sales tax and issued a "Proposed Assessment" of sales tax. In the apparent belief that the aircraft was purchased for ten million dollars, the Department issued a use tax bill for \$700,000. In addition, the Department issued an additional proposed assessment because taxpayer had failed to file sales tax returns for one of the years in which it had been in the business of renting the aircraft.

Taxpayer disagreed with both assessments, submitted a protest to that effect, and an administrative hearing was conducted during which taxpayer's representative explained the basis for the protest. That administrative hearing was conducted in April 2009. This Letter of Findings results.

I. Aircraft Public Transportation Exemption – Gross Retail Tax.

DISCUSSION

Taxpayer argues that it was not subject to sales tax on the purchase of the aircraft because it is renting the aircraft to Charter Company. Taxpayer makes a supplemental argument that it is not required to collect or pay sales tax on the rental income it receives from Charter Company based upon a July 2009 amendment to IC § 6-2.5-5-8 (effective January 1, 2008).

Indiana imposes an excise tax at the time a taxpayer acquires an airplane. [IC 6-2.5-3-2](#) provides as follows: An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

(b) The use tax is also imposed on the storage, use, or consumption of a vehicle, an aircraft, or a watercraft, if the vehicle, aircraft, or watercraft:

(1) is acquired in a transaction that is an isolated or occasional sale; and

(2) is required to be titled, licensed, or registered by this state for use in Indiana.

IC § 6-6-6.5-8 requires the aircraft purchaser to pay sales or use tax shortly after the aircraft is sold or transferred in Indiana. "A person shall pay the gross retail tax or use tax to the department on the earlier of: (1) the time the aircraft is registered; or (2) not later than thirty-one (31) days after the purchase date." IC § 6-6-6.5-8(d).

It is not disputed that taxpayer acquired the aircraft for use in this state. For purposes of this Letter of Findings, it is not disputed that Charter Company is engaged in public transportation and that it supplied taxpayer with an exemption certificate to that effect pursuant to IC § 6-2.5-5-27 which states that:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

Taxpayer's initial claim was that the purchase of the aircraft was not subject to tax because it was acquired for the purpose of leasing or renting to customers such as Charter Company.

That particular exemption is set out at IC § 6-2.5-5-8(b) which states that, "Transactions involving tangible personal property other than a new motor vehicle 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 the person's business without changing the form of the property."

However, Indiana law imposes a rental income threshold above which a person purportedly in the aircraft rental business is entitled to claim the exemption. The threshold is explained at IC § 6-2.5-5-8(e) as follows:

[A] transaction in which a person acquires an aircraft for rental or leasing in the ordinary course of the person's business is not exempt from the state gross retail tax unless the person establishes, under guidelines adopted by the department in the manner provided in [IC 4-22-2-37.1](#) for the adoption of emergency rules, that the annual amount of the gross lease revenue derived from leasing or rental of the aircraft, which may include revenue from related party transactions, is equal to or greater than seven and five-tenths percent (7.5 [percent]) of the (1) book value of the aircraft as published in Vref Aircraft Value Reference guide for the aircraft: or (2) net acquisition price for the aircraft. IC § 6-2.5-5-8(e) (amended June 30, 2009; effective January 1, 2008).

In short, taxpayer acquired an aircraft valued at approximately \$10,000,000 and rented the aircraft to Charter Company. Charter Company paid rent to taxpayer. Assuming for the moment that Charter Company was entitled to the public transportation exemption found at IC § 6-2.5-5-27, Charter Company was not required to pay sales tax on the rental payments.

The issue is whether taxpayer was or was not required to pay sales tax on the initial purchase of the aircraft. In circumstances in which the aircraft purchaser acquires the plane in order to rent it in the "ordinary course of the person's business," the aircraft purchaser must meet the threshold requirement set out in IC § 6-2.5-5-8(h) in order to avoid paying the tax. In taxpayer's case, this means that taxpayer would ordinarily be required to earn \$750,000 in rent each year in order to qualify for the exemption.

However, with the 2009 legislative change set out in IC § 6-2.5-5-8(h), taxpayer believes that the threshold determination is now inapplicable. That amended section of the Indiana Code now reads as follows:

This subsection applies only to aircraft after December 31, 2007. A transaction in which a person acquires an aircraft to rent or lease the aircraft to another person for predominant use in public transportation by the other person or by an affiliate of the other person is exempt from the state gross retail tax. The department may not require a person to meet the revenue threshold in subsection (e) with respect to the person's leasing or rental of the aircraft to receive or maintain the exemption. To maintain the exemption the exemption provided under the subsection, the department may require the person to submit only annual reports showing that the aircraft is predominately used to provide public transportation.

IC § 6-2.5-5-8(h) carves out an exception to the threshold requirement in IC § 6-2.5-5-8(e). If a business acquires an aircraft and rents it to an entity which is engaged in public transportation, the 7.5 percent income threshold does not apply. The business purchaser is entitled to "piggy-back" on the carrier's transportation exemption as long as the carrier is "predominately" engaged in public transportation. In making that determination, the Department has defined "predominately engaged" as follows:

To qualify for the exemption, a taxpayer must be predominately engaged in public transportation. A taxpayer is predominately engaged in public transportation if greater than 50 [percent] of its gross income is derived from transporting people or property for hire. Sales Tax Information Bulletin 12 (July 2007).

Although Charter Company has not submitted "annual reports," the Department is prepared to agree that – for purposes of this Letter of Findings – that Charter Company is predominately engaged in public transportation.

The Department concludes that pursuant to IC § 6-2.5-5-8(h), the purchase of the aircraft is not subject to sales tax because the aircraft was acquired for lease to Charter Company. In this case, taxpayer is entitled to "piggy-back" on the public transportation exemption to which Charter Company is itself entitled. In addition, Charter Company is not required to pay – and taxpayer is not required to collect – sales tax on the stream of income attributable to the rental of the aircraft to Charter Company because "Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property." IC § 6-2.5-5-8.

Taxpayer indicates that for the period at issue, the aircraft was rented to Charter Company for a total of 137.1 hours. Taxpayer indicates that the plane was used for its own purposes a total of 98.9 hours.

Pursuant to IC § 6-2.5-2-1, a sales tax, known as state gross retail tax, is imposed on retail transactions made in Indiana unless a valid exemption is applicable. In addition, a complementary excise tax, known as the "use tax," is imposed 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. The "use" spoken of is defined at IC § 6-2.5-3-1(a) which states that, "'Use' means the exercise of any right or power of ownership over tangible personal property." In this

case, taxpayer exercised its ownership right to use the aircraft for its own purposes for 98.9 hours. Whatever those purposes were, they do not fall under the Charter Company's public transportation exemption umbrella. Therefore, taxpayer owes use tax commensurate with the value of the plane which, in this case, is reasonably measured by the hourly rental price it charges to its customer.

Taxpayer was not required to pay gross retail tax on the purchase price of the aircraft and is not required to collect the gross retail tax on the stream of rental income received from Charter Company. However, on a "going-forward" basis, when taxpayer makes non-exempt use of the aircraft for its own purposes, taxpayer will trigger use tax liability under IC § 6-2.5-3-2.

FINDING

Taxpayer's protest of the assessment of gross retail tax both on the purchase price of the aircraft and on the stream of rental income received from the Charter Company is sustained. Although the Department will apply this ruling prospectively, to the extent that taxpayer makes personal, non-exempt use of its own aircraft, taxpayer will be subject to use tax.

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