DEPARTMENT OF STATE REVENUE

Revenue Ruling #2020-08ST
January 8, 2021

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ISSUES

Sales and Use Tax - Aircraft Maintenance Contracts

Authority: IC 6-2.5-1-11.5; IC 6-2.5-2-1; IC 6-2.5-4-1; IC 6-2.5-4-15; IC 6-2.5-5-46; Sales Tax Information Bulletin #2 (January 2013); Sales Tax Information Bulletin #74 (April 2016); Sales Tax Information Bulletin #94 (June 2020).

A taxpayer ("Company") seeks a ruling regarding whether an optional maintenance contract for an aircraft that will be repaired and maintained in Indiana would be subject to Indiana sales tax.

STATEMENT OF FACTS

Company is an Indiana LLC that owns an aircraft. It is Company's understanding that in the aircraft industry, much of the maintenance work (particularly with respect to aircraft engines) is done pursuant to optional maintenance plans or contracts (or service contracts as they are called in some situations). In these situations, the maintenance contracts are almost never made with the manufacturer selling the aircraft. Rather, the owner of the aircraft will independently purchase a maintenance/service contract with respect to some component of the aircraft for a set price from a third party. For example, one of the most common arrangements is that an aircraft owner will contract with an engine company to provide maintenance/service on the engine. In some cases, the engine maintenance can be fairly significant.

DISCUSSION

Company requests the Department issue a Ruling regarding the taxability of these optional maintenance contracts. Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC 6-2.5-2-1(b). IC 6-2.5-4-1 defines "retail transactions" stating in part as follows:

> (a) A person is a retail merchant making a retail transaction when he engages in selling at retail.
> (b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business he:
> (1) acquires tangible personal property for the purpose of resale; and
> (2) transfers that property to another person for consideration.
> (c) For purposes of determining what constitutes selling at retail, it does not matter whether:
> (1) the property is transferred in the same form as when it was acquired;
> (2) the property is transferred alone or in conjunction with other property or services; or
> (3) the property is transferred conditionally or otherwise.

Further, IC 6-2.5-4-15 provides that "[a] person is a retail merchant making a retail transaction when the person sells tangible personal property as part of a bundled transaction." IC 6-2.5-1-11.5 defines "bundled transaction" as follows:

> (b) "Bundled transaction" means a retail sale of two (2) or more products, except real property and services to real property, that are:
> (1) distinct;
> (2) identifiable; and
> (3) sold for one (1) nonitemized price.
> (c) The term does not include a retail sale in which the sales price of a product varies, or is negotiable, based on other products that the purchaser selects for inclusion in the transaction.

(d) The term does not include a retail sale that:
(1) is comprised of:
(A) a service that is the true object of the transaction; and
(B) tangible personal property that:
(i) is essential to the use of the service; and
(ii) is provided exclusively in connection with the service;
(2) includes both taxable and nontaxable products in which:
(A) the seller's purchase price; or
(B) the sales price;
of the taxable products does not exceed ten percent (10%) of the total purchase price or the total sales price of the bundled products; or
(3) includes both exempt tangible personal property and taxable tangible personal property:
(A) any of which is classified as:
(i) food and food ingredients;
(ii) drugs;
(iii) durable medical equipment;
(iv) mobility enhancing equipment;
(v) over-the-counter drugs;
(vi) prosthetic devices; or
(vii) medical supplies; and
(B) for which:
(i) the seller's purchase price; or
(ii) the sales price;
of the taxable tangible personal property is fifty percent (50%) or less of the total purchase price or the total sales price of the bundled tangible personal property.
The determination under clause (B) must be made on the basis of either individual item purchase prices or individual item sale prices.

The Department's position on the taxability of "optional maintenance contracts" relies on this definition of bundled transactions. This position is explained in Sales Tax Information Bulletin #2 (January 2013), which provides the following:

> **Maintenance contracts generally meet the definition of bundled transactions under IC 6-2.5-1-11.5 and are subject to sales tax on that basis.** The determination as to whether a contract is a maintenance contract is not necessarily based on the particular title of or language used in the contract. Instead, the determination is based on the substantive provisions contained in the contract. An explicit guarantee that tangible personal property will be provided under the contract is not required. What is important is that both the customer and the service provider are aware at the time the contract is executed that consumable items will be provided under the contract. However, the amount of tangible personal property supplied under the contract must be more than a *de minimis* amount. As a rule, the seller's purchase price or the sales price of the taxable items provided under the contracts must exceed 10% of the total purchase price or the total sales price of the bundled products.
>
> (**Emphasis added**)

Thus, an optional maintenance contract is presumed taxable because it is a bundled transaction. One of the exceptions to the definition of a bundled transaction is the ten percent rule discussed in subsection (d), subpart (2), meaning that if the taxable products in a transaction do not exceed ten percent of the total purchase price or the total sales price of the bundled products, then the transaction is not a bundled transaction, and is therefore nontaxable. This is also referred to as the "*de minimis* rule," as discussed in the Sales Tax Information Bulletin #94 (June 2020), which provides the Department's interpretation of IC 6-2.5-1-11.5. The bulletin provides that "nontaxable products" would include "tangible personal property that meets a specific exemption from sales and use tax."

IC 6-2.5-5-46 provides an exemption for tangible personal property used, consumed, or installed in repairing or maintaining an aircraft in Indiana. The statute provides as follows:

> Transactions involving tangible personal property (including materials, parts, equipment, and engines) are exempt from the state gross retail tax, if the property is:
> (1) used;
> (2) consumed; or

(3) installed;

in furtherance of, or in, the repair, maintenance, refurbishment, remodeling, or remanufacturing of an aircraft or an avionics system of an aircraft.

(b) The exemption provided by this section applies to a transaction only if:

(1) the retail merchant, at the time of the transaction, possesses a valid repair station certificate issued by the Federal Aviation Administration under 14 CFR 145 et seq. or other applicable law or regulation; or

(2) the:

(A) retail merchant has leased a facility at a public use airport for the maintenance of aircraft and meets the public use airport owner's minimum standards for an aircraft maintenance facility; and

(B) work is performed by a mechanic who is certified by the Federal Aviation Administration.

(c) The owner of a public use airport shall annually provide to the department the names of retail merchants that have a lease with the public use airport and that perform aircraft maintenance at the public use airport.

Company contends that if the supplies, materials, and equipment utilized in maintenance on an aircraft as part of the maintenance contract qualify for the exemption under IC 6-2.5-5-46, then it would stand to reason that the tangible personal property portion of the optional maintenance agreement would be nontaxable. Therefore, this would satisfy the *de minimis* rule, and as no other portion of the contract would be taxable, the optional maintenance agreement that facilitates such work would not be considered a taxable bundled transaction. Company further contends that if there was no maintenance contract/service agreement, sales tax would still not be paid even if tangible personal property was utilized in the process when work was completed on the aircraft, so long as the underlying maintenance activities performed under the contract meet the exemption requirements detailed in IC 6-2.5-5-46(b) above. Company also claims that this result would also appear to further the legislative purpose of the exemption, which is to encourage aircraft maintenance work to occur in Indiana.

Regarding the necessity for the underlying maintenance activities performed under the contract to meet the exemption requirements detailed in IC 6-2.5-5-46(b), Company points to federal regulations that regulate persons authorized to perform repair or maintenance on aircraft. A repair station that has a certificate issued under 45 CFR 145 may perform maintenance, preventive maintenance, and alterations on an aircraft. *See* 14 CFR 43.3(e). This corresponds with IC 6-2.5-5-46(b)(1). Further, mechanics or repairmen that work on aircraft that have a certificate issued by the FFA under 45 CFR 65 may perform maintenance, preventive maintenance, and alterations on an aircraft; or, if they don't have a certificate, they must work only when supervised by someone who does have a certificate. *See* 14 CFR 43.3(b) - (d). This corresponds with IC 6-2.5-5-46(b)(2). Because federal regulations require that the maintenance be completed by FFA licensed mechanics, repairmen, or repair stations,[1] Company asserts that the requirements of IC 6-2.5-5-46(b) would always be met.

However, IC 6-2.5-5-46(b)(2) would not be satisfied if maintenance was performed by a repairman and not a mechanic, as that term is not mentioned within the statute. Further, IC 6-2.5-5-46(b)(2) would not be satisfied if maintenance was performed by a mechanic at a facility that was not leased at a public use airport, and or if such facility did not meet the public use airport owner's minimum standards for an aircraft maintenance facility. It is not clear if there are other types of facilities (other than a repair station) where a FAA-certified mechanic might perform such repairs or maintenance.

With that being said, if the terms of the optional maintenance agreement comported with the terms of IC 6-2.5-5-46(b), such that maintenance had to be performed either at an FAA-certified repair station or by an FAA-certified mechanic operating at facility leased at a public use airport, then the Department would agree that the optional maintenance agreement would not be considered a taxable bundled transaction because the tangible personal property involved would be exempt. Instead, such contract would be considered a sale of a service, and not subject to Indiana sales tax.

RULING

While generally an optional maintenance contract is presumed to be a taxable bundled transaction, if the terms of Company's optional maintenance contract for aircraft maintenance comports with the qualifications of IC 6-2.5-5-46(b), the optional maintenance contract would meet the exception to a bundled transaction at IC 6-2.5-1-11.5(d)(2) because the tangible personal property involved in the contract would be exempt pursuant to IC 6-2.5-5-46, and therefore the contract would be nontaxable. This presumes that less than ten percent of the tangible personal property transferred might not qualify for the exemption under IC 6-2.5-5-46 or any other provision. If more than ten percent does not qualify the exemption under IC 6-2.5-5-46 or any other provision, then the purchase of the optional maintenance contract would be considered a taxable bundled transaction.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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[1] It appears that the other types of persons authorized to perform repair or maintenance tasks under 14 CFR 43.3 are not applicable to this situation (e.g., an airline may use its own mechanics, which is not applicable to a privately owned aircraft).

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