

This article discusses a major pro taxpayer change in California sales and use tax treatment of aircraft that are used for business purposes in interstate commerce. For purposes of the use tax exemption, a "plain vanilla" business trip from California to any out of state destination will qualify as interstate commerce.

Aircraft owners that may have trouble qualifying for the Common Carrier exemption because of delays in getting their aircraft on an FAR Part 135 certificate, may want to look at using this exemption.

CALIFORNIA INTERSTATE COMMERCE USE TAX EXEMPTION A PRACTICAL APPROACH

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The purpose of this article is to provide information how I received an exemption from California sales and use taxes on my own aircraft, a 2001 Cessna Turbo 182. My intentions are also to offer a brief explanation of the new business friendly commercial interstate commerce regulation and some practical information concerning the California State Board of Equalization, S.B.E, the authority that regulates and collects sales and use taxes in California.

Background:

On December 17, 2000 the S.B.E. adopted some new pro taxpayer language that was added to California Sales/Use Tax Regulation 1620(b). As of December 17, 2000, California became a very "aircraft friendly" state for those owners who can demonstrate 50% or greater business usage outside of California during the required six month test period.

Briefly, the S.B.E. will grant a sales and use tax exemption if the aircraft buyer:

1. Takes delivery of an aircraft outside of California;
2. Immediately places the aircraft into commercial interstate commerce;
3. Uses the aircraft in interstate commerce for a period of six (6) months after the aircraft enters California; and
4. Achieves a commercial interstate flight time factor of 50% or more during the six months immediately following entry into California.

When I read the new provisions in their entirety, the first question that came to mind was: What is the definition of a commercial interstate flight?

To receive an answer to that question and many others specifically related to my particular set of facts and circumstances, I applied for a sales and use tax ruling on December 26, 2000.

Ruling Request:

1. In the ruling request, I stated that the aircraft delivery would take place at Independence, Kansas.
2. Immediately after delivery at Independence, the first flight would be a business flight to Wichita, Kansas for a business meeting with a Cessna executive and a current client.
3. After entering California a few days later, the aircraft was to be hangared approximately 150 days out of the six month test period.

I also indicated that the anticipated business usage and out-of-state flight time to see current and prospective clients would be well above the 50% requirement.

After I sent the ruling to the S.B.E., I continued to work with several auditors and sales tax legal counsel in Sacramento in an attempt to “lobby” for a broad general definition of a “commercial interstate flight.” Some auditors and attorneys were initially of the opinion that in order to qualify as a commercial interstate flight, the flight should be conducted under FAR Part 135. Still others thought that a trip should qualify as long as it had a business purpose. The answer to the ruling request came several months later.

Answer to Ruling Request:

The following is a quote from the answer to my sales and use tax ruling request.

“Regarding the meaning of commercial flight time, this simply means business travel as opposed to personal travel. If the aircraft is used for a business purpose, the use qualifies as commercial flight time. If the aircraft is used for personal use, it does not qualify as commercial flight time. For example, when your business uses the aircraft to fly to Nevada to meet with a client, then this flight would qualify as commercial flight time. On the other hand, if you were to use the aircraft to go on a golfing vacation with your spouse, then this trip is not a business trip, and the flight would not qualify as commercial flight time.”

At the end of the six-month test period, I accumulated more than enough out-of-state business flight time to qualify for the use tax exemption. The next step was to assemble a documentation package to prove the qualification for the exemption.

The following is a list of items that were submitted as part of the documentation/qualification package:

1. Out-of-state delivery certificate identifying the aircraft, date, place of delivery and Hobbs meter reading. The certificate was not notarized; however, it was signed by a Cessna representative and me.
2. Fuel and tie-down receipts for out-of-state locations.
3. An aircraft logbook reflecting all flights beginning with the first flight from Independence to Wichita and concluding with the first flight after the end of the test period. (Please don't send copies of your personal pilot log book. For this test, the auditors are not interested in your advanced ratings or the like. I personally

recommend that all of my clients keep a separate logbook just for this purpose.)

4. Maintenance records for maintenance performed during the test period.
5. A transmittal letter describing the need for the aircraft in connection with my aviation tax practice.
6. A description of the business purpose for each trip accompanied by the name of the client.
7. A calculation of the commercial interstate usage factor. Please note that the entire flight time for both outbound and inbound legs counts as interstate flight time as long as there are no intermediate California landings.

EXAMPLE: A business flight from Van Nuys, California to Reno, Nevada back to Van Nuys would receive full credit for the trip to Reno and back. However, if you flew from Van Nuys to Sacramento, then Sacramento to Reno, only the portion of the outbound trip from Sacramento to Reno would count. The entire return leg from Reno to Van Nuys, California would also qualify.

In connection with one of my client's aircraft, we were also required to submit the following:

1. Copies of federal income tax returns showing that the aircraft was in fact depreciated for business purposes.
2. Copies of client engagement letters to prove that the individuals and entities named in the aircraft logbook were bona fide clients.

Practical Considerations:

Because of the current state budget crisis, the California State Board of Equalization has found it necessary to eliminate over 140 staff positions. There are only two senior tax auditors that handle the aircraft cases in Sacramento. Because of their tremendous workload they have no time to establish a "pen pal" relationship with taxpayers whose documentation packages are not assembled in a clean, concise and convincing manner that clearly shows that a particular aircraft merits an exemption. Therefore, please be very careful with the type of documentation that you include in your package.

Please remember that if the auditor has any doubt as to whether an exemption is due the taxpayer, the auditor is required by three long-standing court decisions to rule in favor of the S.B.E.

For that reason and because we are still dealing with a relatively new law, I am personally meeting with the auditor on all interstate commerce cases for tax liabilities in excess of \$250,000 because I do not want to risk a misinterpretation of something sent through the mail.

Summary:

This new law places California at the top of the list as being aircraft friendly to all owners who can demonstrate they use their aircraft for bona fide business purposes across state lines during the test period.

Refund possibilities may also exist for sales/use taxes paid on aircraft that could not meet one of the other more restrictive tests in prior years.

Victor Anvick is the managing member of **Aviation Tax Information Services** – ATIS Group LLC., located in Acton, California. He has over 30 years of tax experience and since 1983 has specialized exclusively in researching and developing integrated aircraft business plans to assist aircraft owners in securing and protecting maximum income, sales and estate tax savings as a result of their aviation investment. Extensive cooperation with a client's current tax and legal advisors is encouraged.