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The Taxman Cometh: How to Stem the Rising Ride of Aircraft Sales and Use Tax Enforcement

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THE TAXMAN COMETH: HOW TO STEM THE RISING TIDE OF AIRCRAFT SALES AND USE TAX ENFORCEMENT

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I. Introduction: State Revenue Departments’ Current Aggressive Tax Policy

From the Bible\(^1\) to Benjamin Franklin\(^2\) to the Beatles,\(^3\) the taxman has been coming, darkening doors for millennia.


\(^2\) "Our new Constitution is now established, and has an appearance that promises permanency; but in this world nothing can be said to be certain, except death and taxes." Letter from Benjamin Franklin to Jean-Baptiste Leroy (1789) (emphasis added), available at http://wist.info/franklin-benjamin/21050/.

\(^3\) Let me tell you how it will be
There’s one for you, nineteen for me
‘Cause I’m the taxman, yeah, I’m the taxman
Should five per cent appear too small
Be thankful I don’t take it all
‘Cause I’m the taxman, yeah I’m the taxman.
This article addresses the current trend, arising largely from the financial malaise of the last six years, whereby revenue departments of various states throughout the United States are aggressively searching for aircraft potentially based in their respective states and billing aircraft owners for sales, use, and property taxes.4 The search for such aircraft is often aided by the fact that aircraft purchases and operations are “documented by an FAA paper trail.”5 Once a state revenue department identifies an aircraft it believes to be hangared in, operated in, or registered to a company or individual located in that state, it sends a tax bill to the aircraft owner that includes taxes for the original purchase or ongoing use taxes, as well as property taxes.6 Because there has often been a substantial time lag between the purported taxable event and the notice of assessment and billing, the aircraft owner is also hit with large penalty and interest assessments.7 Therefore, these tax bills often reach six or seven figures.8 Due to states’ eagerness to collect these large sums of money, revenue departments have begun ignoring or “reinterpreting” long-established exemption principles.9 And revenue departments are not the only ones making efforts to restrict sales and use tax

THE BEATLES, Taxman, on REVOLVER (Capitol Records 1966).


5 See Moore, supra note 4, at 1 (“Experience shows that the Texas Comptroller’s Office routinely receives transaction records from the FAA in order to monitor compliance with the Texas sales and use tax.”).


8 See Levy, supra note 4.
exemptions—many state legislatures are passing amendments that narrow the application of exemptions.10

Part II of this article provides an overview of sales and use taxes; it then explains how those taxes are applied to aircraft. Part III discusses some of the most common types of exemptions found in states throughout the United States. Part IV offers information regarding the receipt of an assessment and the subsequent administrative and judicial appeal process. This section focuses on Texas as an example, but the process varies by state. Part V contains a recent case analysis to demonstrate how taxing authorities and courts in various states are strictly interpreting statutory law so as to deny aircraft sales and use tax exemptions to taxpayers. Part VI explores an additional avenue of aircraft taxation by local authorities: property taxes. This section once again draws on Texas as an example by discussing some of its laws and recent cases. Part VII concludes by discussing how the recent stances taken by state and local taxing authorities have impacted how taxpayers and their attorneys develop aircraft taxation strategies.

II. APPLICABILITY OF SALES AND USE TAX ENFORCEMENT TO AIRCRAFT TRANSACTIONS AND ONGOING OWNERSHIP

Sales and use tax is a significant cost that factors into the purchase and ownership of an aircraft.11 Tax planning that is intended to reduce the amount of taxes owed to state and local authorities is necessarily complicated by the “transitory nature” of aircraft.12 Even though a taxpayer may be able to purchase an aircraft in a state with little13 or no14 sales tax or where an ex-

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10 See, e.g., N.Y. DEP’T OF TAXATION & FIN., AMENDMENTS AFFECTING THE APPLICATION OF SALES AND USE TAX TO AIRCRAFT, VESSELS AND MOTOR VEHICLES 1, TSB-M-09(4)S (May 12, 2009), available at http://www.tax.ny.gov/pdf/memos/sales/m09_4s.pdf (discussing how certain “exemptions applying to commercial aircraft and to nonresident purchasers have been amended to restrict the application of these exemptions in certain situations”).

11 See Levy, supra note 4.

12 See Moore, supra note 4, at 1.

13 States with low tax rates include Massachusetts, South Carolina, and North Carolina. Levy, supra note 4.

emption can be claimed, this does not foreclose the assessment of use tax by a state (or states) that believes the aircraft is operated or based within its boundaries. Ideally, aircraft owners and operators will be able to assert an exemption from use tax in addition to asserting an exemption from sales tax or paying little to no sales tax.

Jurisdictions vary in their technical definitions of sales and use tax. In general, a sales tax is a tax on “retail sales by which ownership of tangible personal property is transferred.” Sales tax is computed based on the sales price of the item purchased. Some states, such as Texas, reduce the sales price by the value of a trade-in before calculating the sales tax. When an aircraft sales transaction occurs, both the buyer and seller may hold obligations with respect to the payment of sales tax. Sellers are often required to collect sales tax when a non-tax exempt purchase of an aircraft is made. If an exemption from sales tax is claimed, the parties must generally complete some sort of exemption certificate or form. In Texas, the buyer is ultimately liable for payment of sales tax, but “the seller has a statutory collection responsibility and the Comptroller can audit either the buyer or the seller in any order to collect the tax.”

an aircraft in Delaware are subject to tax, however, unless the aircraft has a “certified takeoff weight of 12,500 pound[s] or more.” Aircraft Sales in Delaware, St. Del., http://revenue.delaware.gov/services/Business_Tax/aircraft_sales.shtml (last updated Mar. 6, 2007).

One such exemption is the flyaway exemption, which allows an aircraft purchaser to avoid sales tax if the purchased aircraft is “immediately removed from the state and registered elsewhere.” Levy, supra note 4. These and other exemptions are discussed in more detail below. See infra Part III.

See Levy, supra note 4.

See id.


See id. South Dakota is one state that does not allow a deduction for the value of a trade-in. S.D. Codified Laws § 50-11-19.1 (2004) (“[T]he purchase price is . . . the total consideration for the aircraft whether received in money or otherwise.”).

See Moore, supra note 4.

when a sales contract "allocate[s] sales tax responsibility to the buyer," the taxing authority is "not bound [by] such contractual provisions." 29

In general, use tax is assessed "on the consumer for the privilege of storing, using, or consuming . . . any tangible personal property." 24 New York, for instance, defines the "exercise of any right or power over tangible personal property . . . [including] the receiving, storage[,] or any keeping or retention for any length of time, . . . or any consumption of such property" as a use subject to tax. 25 Texas requires the payment of use tax when an aircraft is used in the state more than 50% of the time or if the aircraft is hangared within the state. 26 Use tax, like sales tax, is also computed based on the sales price of the item purchased. 27

Within a single state, these taxes are usually mutually exclusive, meaning a state will not assess both sales tax and use tax on an aircraft. 28 For instance, if the purchase of an aircraft is exempt from sales tax in a particular state, that state will still assess use tax on the aircraft if it is stored or used in that state (unless a use tax exemption applies). 29 One author describes the use tax as a "complementary enforcement mechanism of the sales tax." 30 The Florida Division of Administrative Hearings has called the use tax "a protective measure [that is] applied to prevent citizens from escaping the sales tax in their jurisdiction by going to another state and buying the same item tax free." 31 States often grant credit for sales or use tax paid in another state, 32 but not always—aircraft owners and operators must thus

29 Id.
24 Levy, supra note 4.
26 Moore, supra note 4. Whether an aircraft is "hangared" in Texas is determined by analyzing several factors. See 34 Tex. Admin. Code § 3.297(c)(4) (listing the following as factors for consideration: "where the aircraft is rendered for ad valorem taxes"; "whether the owner owns or leases hangar space in this state"; and "declarations made to the Federal Aviation Administration, an insurer, or another taxing authority concerning the place of storage of the aircraft").
28 Levy, supra note 4; see, e.g., Fla. Admin. Code Ann. r. 12A-1.091(1) (2013) ("The Florida Sales and Use Tax Act imposes a tax on the use, consumption, distribution, and storage for use or consumption in this state of tangible personal property purchased in such manner that the sales tax would not be applicable at the time of purchase." (emphasis added)).
30 Moore, supra note 4.
take care not to "inadvertently subject [their] aircraft to sales or use tax in multiple jurisdictions."\textsuperscript{33}

Since 2000, a group of twenty-four states has adopted a Streamline Sales and Use Tax Agreement in an effort to "expand taxation on interstate transactions and provide basic uniformity in sales tax administration."\textsuperscript{34} The Streamlined Sales Tax Governing Board states that the Agreement's purpose is to "simplify and modernize sales and use tax administration in order to substantially reduce the burden of tax compliance."\textsuperscript{35} While this effort may eventually simplify the rules that aircraft owners and operators must follow when tax planning and claiming exemptions, it may also make it easier for states to collaborate and collect asserted tax deficiencies.\textsuperscript{36}

III. TAX AVOIDANCE LEGISLATION & REGULATIONS

States are often "very restrictive" in offering exemptions from sales and use tax, and where exemptions are available, their requirements are "strictly construe[d]."\textsuperscript{37} According to the Texas taxing authority, "[t]he express terms of an exemption statute must be met, and exemptions from taxation are subject to strict construction because they are the antithesis of equality and uniformity and because they place a greater burden on other tax-paying businesses and individuals."\textsuperscript{38} In other words, "[t]ax exemptions undermine equal and uniform taxation and are subject to strict construction."\textsuperscript{39} State tax departments have begun to carefully analyze not only the form but also the substance of asserted exemptions.\textsuperscript{40} Taxpayers, along with their attorneys and accountants, should therefore be cautious when claiming exemptions and be meticulous when confirming that their aircraft

\textsuperscript{33} Levy, \textit{supra} note 4.
\textsuperscript{36} State collaboration could arguably even help taxpayers in the long-run. If multiple states believe they are entitled to sales or use tax with respect to a certain aircraft, perhaps collaboration among those states prior to assessing tax deficiencies will prevent the filing of duplicative claims.
\textsuperscript{37} Levy, \textit{supra} note 4.
\textsuperscript{40} See Levy, \textit{supra} note 4.
purchase and usage complies with all exemption requirements. The following discussion offers an overview of some of the most common types of exemptions and provides some specific state examples, but it is by no means exhaustive.

A. Flyaway Exemption

Aircraft purchases may be exempt from sales and use tax when an aircraft is sold to an out-of-state buyer who then flies it out of the purchase state. The parties must generally complete an exemption certificate at the time of sale. Depending on the state, the buyer may need to remove the aircraft from the state within a certain time period. In Florida, an aircraft sale between a registered dealer and a nonresident buyer who does not conduct business in Florida is exempt from sales tax if the buyer removes the aircraft within ten days after the date of purchase and meets other documentation requirements; if after the sale “the aircraft is immediately placed in a registered repair facility,” the buyer has twenty days following completion of repairs to remove the aircraft from Florida. An aircraft owned by a nonresident that enters Florida for less than twenty-one days during the first six months after purchase is also exempt from use tax. California exempts the payment of sales and use tax by a nonresident if an aircraft is “promptly removed” and does not return to the state within twelve months after being removed.

States vary by how restrictive they are regarding the use of aircraft within the state before its removal. In Texas, for instance, the exemption applies to an aircraft sold for “use and registration in another state . . . before any use in this state other than flight training in the aircraft and the transportation of the aircraft out of this state.” Florida, as stated above, allows an aircraft to undergo repairs or alterations in a registered repair facility before being removed from the state. Subsequent use

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41 See Moore, supra note 4.
42 See id.; see, e.g., Tex. Tax Code Ann. § 151.328(f) (West 2013) (detailing the requirements associated with filling out an exemption certificate at the time of sale); 34 Tex. Admin. Code §§ 3.287, 3.297(c)(9) (2013).
46 Tex. Tax Code Ann. § 151.328(a)(4); 34 Tex. Admin. Code § 3.297(c)(9). A Texas Comptroller publication also states that “[b]ringing the aircraft back into Texas for training, repair or refurbishment is not considered divergent use.” Aircraft and the Texas Sales and Use Tax, supra note 18.
of the aircraft within the state after the initial removal may subject the taxpayer to a use tax assessment unless another exemption applies. 48

According to a fourteen-state study conducted in 2008, states with a flyaway exemption included Arizona, California, Florida, Illinois, Iowa, Michigan, Minnesota, South Dakota, Texas, and Wisconsin. 49

B. Resale Exemption

Generally, aircraft acquired in a wholesale transaction and held in inventory are not subject to sales and use tax because no retail transaction occurs. 50 Such wholesale transactions include situations where an aircraft is acquired for the purpose of resale or lease. 51 A dealer’s acquisition of the aircraft is not taxed, but the subsequent resale of the aircraft to a buyer is taxed; similarly, the acquisition of an aircraft for leasing purposes is not taxed, but subsequent lease payments are subject to tax. 52 Ultimately, the “effect of the sale for resale exemption . . . is to shift the tax to the final purchaser or consumer.” 53

For instance, in Florida, the purchase of an aircraft by a registered dealer is exempt from sales tax if the purchase is made exclusively for resale purposes. 54 However, if the dealer uses the aircraft “for any purpose for which income is received . . . including charter, rental, flight training, and demonstration where a charge is made,” then the dealer must pay a 1% monthly use tax on the value of the aircraft. 55 In Texas, only an individual or entity that holds a valid Texas resale certificate can claim a resale exemption. 56 Personal uses of aircraft held as inventory will result in the assessment of use tax. 57 California offers a resale exemption “provided the purchaser makes no use of the property except demonstration and display in the course

48 For instance, see the discussion below in Part III.E regarding interstate commerce and out-of-state use.
49 Conklin & de Decker, supra note 14.
50 Levy, supra note 4; Moore, supra note 4.
51 Levy, supra note 4.
52 Id.
54 FLA. ADMIN. CODE ANN. r. 12A-1.007(10)(g), 12A-1.039 (2013).
55 Id. r. 12A-1.007(10)(g).
56 Moore, supra note 4.
57 Id.
of offering the property for sale.” 58 Use tax will be due if any personal use of the aircraft is made. 59 Possible evidence used to substantiate a claim for a resale exemption includes copies of the taxpayer’s “valid seller’s permit, county business license, dated advertisements in newspapers and trade magazines, logs of engine hours or miles verifying the demonstration, and any other documentation which shows efforts made to sell the property.” 60

According to a fourteen-state study conducted in 2008, states with a resale exemption included Arizona, California, Delaware, Florida, Iowa, Michigan, North Dakota, Pennsylvania, South Dakota, Texas, and Wisconsin. 61

C. OCCASIONAL, ISOLATED, OR CASUAL SALE EXEMPTION

Some states exempt aircraft sales from tax when the sale is made by an individual or company that is “not regularly engaged in the aircraft sale[s] business.” 62 Whether a sale by such an individual or company qualifies for this exemption depends on a state’s definition of an occasional, isolated, or casual sale. In Texas, “one or two sales of taxable items . . . at retail during a [twelve]-month period by a person who does not habitually engage, or hold himself out as engaging, in the business of selling taxable items at retail” qualify as tax-exempt occasional sales. 63 A third sale in any twelve-month period transforms the seller into a retailer who must obtain a sales permit; tax must be collected on the third and any subsequent sales unless another specified exemption applies. 64 If a seller possesses a sales tax permit in Texas “or similar licenses or permits in any other state,” then the sale cannot qualify for the exemption. 65 Occasional sales in Texas also include “the sale of the entire operating assets of a business or of . . . [an] identifiable segment of a business,” which could include aircraft. 66 Finally, if an individual who does

59 Id.
60 Id.
62 Levy, supra note 4.
63 TEX. TAX CODE ANN. § 151.304(a), (b)(1) (West 2013); see 34 TEX. ADMIN. CODE § 3.316(a)–(b) (2013).
64 34 TEX. ADMIN. CODE § 3.316(b)(2).
65 AIRCRAFT AND THE TEXAS SALES AND USE TAX, supra note 18.
66 TEX. TAX CODE ANN. § 151.304(b)(2).
not hold a sales tax permit sells an aircraft that was originally purchased by the individual or a family member for personal use by the individual and his family, then the sale will be tax exempt if the aircraft is not sold by an auctioneer or broker and the "total receipts from sales of the individual’s tangible personal property in a calendar year do not exceed $3,000." The occasional sale exemption does not apply to leases or rentals.\(^{68}\)

California exempts the payment of sales or use taxes on an aircraft when the seller is "not engaged in the business of selling the type of property for which the exemption is claimed" and the seller is "the parent, grandparent, child, grandchild, or spouse, or the brother or sister if the sale . . . is between two minors related by blood or adoption, of the purchaser."\(^{69}\)

Other states, however, have occasional or isolated sale exemptions but "specifically carve out aircraft from the exempt property designation" and tax their sale.\(^{70}\) Florida is one such state, with its statute reading as follows: "The occasional or isolated sale of an aircraft . . . is taxable."\(^{71}\)

According to a fourteen-state study conducted in 2008, states with an occasional or isolated sale exemption included Arizona, California, Michigan, North Dakota, Texas, and Wisconsin.\(^{72}\)

D. Common Carrier Exemption

Common carrier exemptions exist in several states and are often not limited to aircraft—they may apply generally to "transportation equipment used in the movement of persons and property for hire."\(^{73}\) The scope of the exemption varies by state, sometimes pertaining only to commercial airlines operating under Federal Aviation Regulation (FAR) Part 121, sometimes including charter operations under FAR Part 135, and sometimes even extending to "aircraft operators serving members of their controlled group and operating under FAR Part 91."\(^{74}\)

\(^{67}\) Id. § 151.304(b)(5).

\(^{68}\) Moore, supra note 4; Aircraft and the Texas Sales and Use Tax, supra note 18.


\(^{70}\) Levy, supra note 4.


\(^{72}\) Conklin & de Decker, supra note 14.

\(^{73}\) Levy, supra note 4.

\(^{74}\) Id. FAR Part 91 governs noncommercial general aviation, FAR Part 135 governs commercial general aviation, and FAR Part 121 governs commercial air carrier aviation. Conklin & de Decker, supra note 14; see generally 14 C.F.R. pts. 91, 121, 135 (2013).
In Texas, a taxpayer may claim an exemption when "authorized by the appropriate United States agency or by the appropriate state agency within the United States to operate an aircraft . . . as a common or contract carrier transporting persons or property for hire in the regular course of business." A similar exemption exists in California for either the sale or lease of aircraft used as common carriers, but with an added rebuttable presumption: if an aircraft purchased on or after January 1, 1997, and used as a common carrier generates yearly gross receipts that are less than 20% of the purchase price of the aircraft or $50,000, whichever is less, then the taxpayer is presumed to not be engaged in business as a common carrier and the exemption does not apply. California also explains in detail how an aircraft can qualify for common carrier use. Only the first twelve consecutive months after the aircraft's "first operational use" are considered; during this "test period," more than one-half of the aircraft's operational use must be for common carrier purposes. The California Code of Regulations lists various kinds of flights that do and do not qualify as a common carrier use.

According to a fourteen-state study conducted in 2008, states with a common carrier exemption included, among others, California, Florida, Iowa, Michigan, Pennsylvania, Texas, and Wisconsin.

E. INTERSTATE COMMERCE & OUT-OF-STATE USE EXEMPTION

Some states do not subject aircraft to sales or use taxes when they are used primarily in interstate commerce or purchased from an out-of-state seller and then used outside the state. The applicability of the exemption "generally turns on the level of interstate use, and the degree [to which the aircraft] resides in the state."

For instance, California distinguishes between aircraft purchased for in-state use and out-of-state use for purposes of use

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76 Cal. Rev. & Tax. Code §§ 6366(a), 6366.1(a) (West 2013).
77 Id. § 6366(b).
79 See id.
80 Conklin & de Decker, supra note 14.
81 Levy, supra note 4.
82 Id.
tax calculation. Depending on the time period at issue, either the 90-Day Test or 12-Month Test will apply. If the first “functional use” of an aircraft is within California, it is presumed to be purchased for use in California and use tax will apply. Under the 90-Day Test, if the first functional use is outside California, the aircraft is still presumed to have been purchased for use in California if brought into California within ninety days after purchase, unless (1) the aircraft is used or stored outside California “one-half or more of the time during the six-month period immediately following its entry into [the] state”; or (2) “one-half or more of the flight time traveled by the aircraft during the six-month period immediately following its entry into the state is commercial flight time traveled in interstate or foreign commerce.” Under the 12-Month Test, if the first functional use is outside California, the aircraft is still presumed to have been purchased for use in California if it is brought into California within twelve months after purchase and it is (1) purchased by a California resident; (2) subject to property tax in California within the first twelve months of ownership; or (3) purchased by a nonresident and is used or stored in California more than one-half of the time within the first twelve months of ownership. This presumption can be rebutted (and use tax will not apply) if the taxpayer proves that (1) the “aircraft was purchased for use outside [California] during the first [twelve] months of ownership”; or (2) “one-half or more of the flight time traveled by the aircraft during the six-month period immediately following its entry into the state is commercial flight time traveled in interstate or foreign commerce.” As if the complicated nature of this exemption were not enough, according to one source, California’s taxing authority “aggressively audits this exemption and will look to evaluate a number of documents in order to verify that the qualifications have been met.”

85 Id. § 1620(b)(3).
86 Id. § 1620(b)(4).
87 Id. § 1620(b)(5).
88 Id.
California also provides a general exemption from use tax where an aircraft is "purchased for use and used in interstate or foreign commerce prior to its entry into [California], and thereafter used continuously in interstate or foreign commerce both within and without California and not exclusively in California." As discussed in the preceding paragraph, this exemption becomes more complicated if the aircraft first enters California within either ninety days or twelve months (depending on whether the 90-Day Test or 12-Month Test applies) after purchase. In either case, the taxpayer seeking the interstate commerce exemption must show that "one-half or more of the flight time traveled by the aircraft during the six-month period immediately following its entry into the state is commercial flight time traveled in interstate or foreign commerce." Florida offers an exemption for aircraft purchased for use outside the state. Normally, where an aircraft is purchased outside Florida but then "titled, registered, or licensed" in Florida, it is presumed taxable. The taxpayer can rebut this presumption with evidence that the aircraft was purchased outside Florida six months or more prior to being brought into Florida and was used in other states for six months or more "under conditions which would lawfully give rise to the taxing jurisdiction of another state . . . and any lawfully imposed tax was paid to such state" before the aircraft was brought into Florida.

In Texas, "[a]n aircraft is not subject to use tax if it is hanged outside [the] state and is used more than 50% outside [the] state." Aircraft owners and operators "must maintain sufficient records" to prove the percentage of time that an aircraft is used in Texas. Use of an aircraft in Texas includes the "portion of interstate flights in Texas airspace."

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90 Cal. Code Regs. tit. 18, § 1620(b)(2)(B). The California regulations offer examples of use that qualify as interstate or foreign commerce. See id. § 1620(b)(7).
91 See Buyer Beware – California Sales/Use Tax Issues on Aircraft Purchases, supra note 89.
94 Id.
95 Id. (emphasis added). However, evidence of prior use or tax paid outside Florida does not prevent the assessment of tax on the rental or lease of aircraft that is used or stored in Florida. Id.
97 Id.
98 Id. § 3.297(c)(3)(A).
F. OTHER MISCELLANEOUS EXEMPTIONS

States often provide exemptions from sales and use tax where an aircraft is used for flight instruction purposes and other requirements are met. In Texas, an aircraft used to provide flight instruction is exempt from sales and use tax if the taxpayer holds a sales tax permit and the flight instruction is "recognized by the Federal Aviation Administration (FAA), under the direct or general supervision of an FAA certified flight instructor, and designed to lead to a pilot certificate or rating issued by . . . the FAA."99 Similarly, a student renting an aircraft for flight training purposes who meets certain requirements can claim a tax exemption.100

As mentioned before, some states offer a partial exemption in the form of a trade-in allowance. The value of the trade-in aircraft is excluded from the purchase price of the new aircraft for the purpose of sales tax calculation.101 States usually require that the "trade-in be a simultaneous two-party exchange."102 For instance, in Florida, the value of an aircraft trade-in can be deducted from the sales price for tax purposes when the trade-in is accepted by a registered dealer and the sale and trade-in comprise one transaction.103 A trade-in allowance is also available when an individual who is not a registered dealer accepts an aircraft "in part payment or full payment as trade-in or exchange."104

Aircraft transfers in the corporate context may qualify for an exemption. In California, if an aircraft is "transferred into a commencing corporation solely in exchange for first issue stock," it is not subject to tax as long as the corporation acknowledges receipt of the aircraft and the stock is the only consideration for the transfer.105 These "entity purchases" are often exempt because while sales tax is imposed on sales involving tangible personal property, stock or membership interest is intangible property.106 Many other states offer exemptions for "bulk sales of property as part of an ongoing trade or business, statu-

99 Id. § 3.297(c)(7); Tex. Tax Code Ann. § 151.328(a)(2) (West 2013).
100 34 Tex. Admin. Code § 3.297(c)(8).
101 Levy, supra note 4.
102 Id.
104 Id.
106 Levy, supra note 4.
IV. OVERVIEW OF THE ADMINISTRATIVE LAW PROCESS

Even when a taxpayer has properly claimed an exemption from sales and use tax, a state taxing authority will not be deterred from attempting to collect tax on the acquisition or operation of an aircraft. If a taxpayer disagrees with a tax assessment, he must contest it in one of the manners permitted by the state. The assessment and review process for sales and use taxes varies by jurisdiction. It is important to provide an overview of this process before discussing recent Comptroller and state court decisions because whether a taxpayer properly follows the administrative law process can greatly impact his or her case. This article will provide an overview of the process by discussing the procedure as it exists in Texas.108

The process begins when the Texas Comptroller of Public Accounts (Comptroller) assesses a deficiency in the sales or use taxes owed on the purchase or ownership of an aircraft.109 The taxpayer is notified with a deficiency statement entitled “Notice of Tax Due” or “Texas Notification of Audit Results.”110 The deficiency statement will list the tax, interest, and penalties claimed to be owed by the taxpayer.111 If the taxpayer does not file a request for redetermination, the claimed deficiency is due ten days after it becomes final;112 the determination becomes final thirty days after service of the deficiency statement.113 In the event that a taxpayer ultimately fails to pay taxes, the “attor-
ney general shall bring suit in the name of the state to recover delinquent state taxes, tax penalties, and interest owed.”

If the taxpayer disagrees with the Comptroller’s assessment, he can take one of the following courses of action: (1) request a redetermination and navigate the applicable administrative hearing process; (2) pay the asserted deficiency, file a claim for refund, and navigate the applicable administrative hearing process; (3) pay the asserted deficiency “under protest and sue the Comptroller and Texas Attorney General in Travis County District Court to recover the taxes without a prior administrative hearing”; or (4) file an action for an injunction.

A. Request for Redetermination

Under the first option, the taxpayer must submit a written petition for redetermination within the prescribed time period. “To be considered timely, the request for a hearing must be filed within 30 days from the date of the deficiency determination.” The request for redetermination must include a Statement of Grounds that “contain[s] the reasons the taxpayer disagrees with the action of the agency.” Additional evidence beyond that contained in the Statement of Grounds or the audit may be acquired through a preliminary conference, discovery, written or oral requests for evidence, or an audit amendment. The taxpayer is charged with the burden of proving by clear and convincing evidence that an exemption applies to the transaction at issue; alternatively, the taxpayer must demonstrate by a


115 Lipstet, supra note 110; see generally Tex. Tax Code Ann. ch. 112.


117 34 Tex. Admin. Code § 1.5. Extensions may be requested as provided under Section 1.6. See id. § 1.6.

118 Id. §§ 1.5, 1.7. Specifically, within the Statement of Grounds, the taxpayer must list and number the items or transactions, individually or by category, with which he disagrees. For each contested item or category of items, the taxpayer must also state the factual basis and the legal grounds to support why the taxpayer argues that the tax should not be assessed or the tax should be refunded. If the taxpayer disagrees with the agency’s interpretation of the law, specific legal authority must be cited in support of the taxpayer’s arguments.

Id. § 1.7.

119 Id. § 1.7.
preponderance of the evidence that an action or proposed action is "otherwise unwarranted."\textsuperscript{120}

At this point, the taxpayer’s contentions may be accepted or the parties may reach a resolution; in either case, the Comptroller may amend the determination, issue an amended billing, or "agree to a refund or credit request rather than issue a Position Letter."\textsuperscript{121} If the taxpayer’s contentions are not resolved in this manner, the Tax Division’s assistant general counsel will issue a Position Letter accepting or rejecting each of the contentions.\textsuperscript{122} In other words, the assistant general counsel will deem the relevant sale or use of the aircraft either "subject to or exempt from taxation."\textsuperscript{123} Within forty-five days, the taxpayer must then either agree with the Position Letter (and pay the amount calculated in the amended determination or final billing, unless the taxpayer disagrees with that amount and files a motion for rehearing) or disagree with the Position Letter (and submit a Reply to the Position Letter containing arguments and evidence in support of his position along with a request for a hearing).\textsuperscript{124} If the Reply raises new facts or legal arguments, the assistant general counsel will issue a Response.\textsuperscript{125}

If at this point "the parties are unable to resolve or settle all contested matters, the Tax Division will" refer the case to the State Office of Administrative Hearings (SOAH) by filing a Request to Docket Case form.\textsuperscript{126} The Comptroller transferred the administrative hearing function and the administrative law

\textsuperscript{120} Id. § 1.40; see SOAH Docket No. 304-12-5311.26, CPA Hearing No. 103,052, 2012 WL 3783106, at *7 (Tex. Comp. Pub. Accounts July 2, 2012) (noting the taxpayer’s burden of proving an exemption by clear and convincing evidence); SOAH Docket Nos. 304-09-0632.26 & 304-09-0361.26, CPA Hearing Nos. 47,782 & 48,443, 2009 WL 8106289, at *2 (Tex. Comp. Pub. Accounts Aug. 19, 2009) (explaining that once Comptroller staff presented a prima facie case that use tax was properly assessed, the burden shifted to the taxpayer to prove by a preponderance of the evidence that the assessments were incorrect).

\textsuperscript{121} 34 TEX. ADMIN. CODE § 1.8. If the agency undertakes one of these actions, it becomes final twenty days after notice is given; an "amended billing or determination is payable [twenty] days after it becomes final unless otherwise specified.” Id.

\textsuperscript{122} Id. § 1.9.

\textsuperscript{123} Id.

\textsuperscript{124} Id. §§ 1.10, 1.15. If the taxpayer fails to respond, the Comptroller “may dismiss the contested case.” Id. § 1.10.

\textsuperscript{125} Id. § 1.16.

\textsuperscript{126} Id. § 1.22; 1 TEX. ADMIN. CODE §§ 155.51, 155.103 (2013); see 34 TEX. ADMIN. CODE § 1.1; Frequently Asked Questions, St. Off. Admin. Hearings, http://www.soah.state.tx.us/about-us/faq/tax-division.asp (last visited Jan. 28, 2014). The SOAH Rules of Procedure found in Title 1, Chapter 155 of the Texas Ad-
judges (ALJs) to SOAH in 2007; the transfer was later formalized by legislative action. The purpose of docketing a case with SOAH is to set the contested case for a hearing, assign an ALJ, or request alternative dispute resolution. The parties may begin the discovery process and file motions once SOAH has obtained jurisdiction over the case (i.e., when the Request to Docket Case form is filed).

If the case is set for a hearing, the Comptroller will send the taxpayer a formal hearing notice. The taxpayer will elect to conduct either a written submission hearing or an oral hearing before a SOAH ALJ. The taxpayer may represent himself or select an attorney, accountant, or other authorized representative as counsel at the SOAH hearing. The “administrative law judge who conducts a contested case hearing shall consider applicable agency rules or policies in conducting the hearing, but the state agency deciding the case may not supervise the administrative law judge.” For instance, in determining the burdens of proof, the ALJ primarily considers “the applicable statute, the referring agency’s rules, and the referring agency’s policy.”

Ultimately, the ALJ will issue a proposal for decision to the Comptroller. The parties may submit exceptions and replies to the ALJ and the Comptroller. The ALJ then has the authority to respond to the exceptions and replies by amending the proposal for decision. The Comptroller issues a final decision after reviewing the proposal for decision and any exceptions filed by the taxpayer or assistant general counsel. In making

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127 Frequently Asked Questions, supra note 126.
130 See id. § 155.305 (discussing general motion practice).
131 Id. § 155.51.
132 Id. § 155.401; Frequently Asked Questions, supra note 126.
134 Id. § 1.4.
137 See id. § 155.507; 34 Tex. Admin. Code § 1.27.
140 34 Tex. Admin. Code § 1.28. The Comptroller may issue a decision prior to “the issuance of a proposal for decision if the parties are in agreement on all contested issues or if the parties agree to waive issuance of a proposal for decision.” Id.
its decision, the only circumstances under which the Comptroller may change an ALJ's finding of fact or conclusion of law or may vacate or modify an ALJ's order are where the Comptroller determines:

(1) that the ALJ "did not properly apply or interpret applicable law, then existing comptroller rules or policies, or prior administrative decisions";
(2) that the ALJ "issued a finding of fact that is not supported by a preponderance of the evidence"; or
(3) "that a comptroller policy or a prior administrative decision on which the [ALJ] relied is incorrect."\

If the Comptroller modifies an ALJ's finding of fact, conclusion of law, or order, it must state the "specific reason and legal basis" for doing so.\

Following the Comptroller's decision, the taxpayer may file a motion for rehearing. The motion "must state each specific ground upon which the party believes the comptroller's decision is erroneous." If no motion for rehearing is filed, the Comptroller's decision regarding the deficiency becomes final twenty days after service of the notice of the decision. If the Comptroller's decision assesses a deficiency, the amount is due twenty days after the redetermination hearing decision becomes final. Accordingly, the taxpayer essentially has forty days after the Comptroller issues its decision to pay the deficiency. If the taxpayer fails to pay the amount of a determination within this time period, "a penalty of [10%] of the amount of the determination, exclusive of penalties and interest, shall be added." A taxpayer "who has exhausted all administrative remedies available within a state agency [but] who is aggrieved by a final

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142 Id.
143 34 Tex. Admin. Code § 1.29.
144 Id.
145 Id. § 1.28; Tex. Tax Code Ann. § 111.009 (West 2013).
146 Tex. Tax Code Ann. § 111.0081. No tax, interest or penalty is due from a taxpayer that has timely filed a Petition for Redetermination with the Comptroller in response to a deficiency determination unless and until there is a final Comptroller's Decision issued. Interest, however, does continue to run during the pendency of the administrative process unless a payment has been made.

Lipstet, supra note 110.
147 Lipstet, supra note 110.
decision in a contested case is entitled to judicial review." The taxpayer must file a petition no later than thirty days after the Comptroller's decision becomes "final and appealable." The district courts in Travis County hold exclusive jurisdiction over suits challenging a collection action by the Comptroller.

B. PAYMENT AND FILING OF A CLAIM FOR REFUND

Alternatively, if the time period for requesting a timely redetermination hearing has expired, if the taxpayer desires an additional hearing before the Comptroller, or if the taxpayer believes he has erroneously paid sales or use taxes, the taxpayer may request a refund after paying the deficiency. The refund claim must be in writing and must "state fully and in detail each reason or ground on which the claim is founded." A timely refund claim must "be filed before the expiration of the applicable limitation period as provided by [the Tax Code] or before the expiration of six months after a jeopardy or deficiency determination becomes final, whichever period expires later." If the Comptroller determines "that an amount of tax, penalty, or interest has been unlawfully or erroneously collected," that amount will either be credited "against any other amount when due and payable by the taxpayer" or refunded. If the Comptroller denies a refund claim, the taxpayer may request a refund hearing. The written request must be filed within thirty days after the denial and must contain a Statement of Grounds like that required for a redetermination hearing. After the refund hearing, the Comptroller's decision becomes final twenty days after service of the notice of decision. The taxpayer can then file a motion for rehearing that sets forth "each specific ground of error" and the amount of the refund requested.

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150 See id. § 2001.176.
151 Tex. Tax Code Ann. § 111.0102.
152 34 Tex. Admin. Code § 1.5 (2013); Lipstet, supra note 110.
154 Id.
155 Id.
156 34 Tex. Admin. Code § 1.5.
157 Id.; Tex. Tax Code Ann. § 111.105. Extensions may be requested as provided under Section 1.6. See 34 Tex. Admin. Code § 1.6.
159 Id.
Comptroller may also decide to conduct an informal review of a refund claim.\textsuperscript{160}

If a taxpayer has filed a tax refund claim under Section 111.104, has filed and been denied a motion for rehearing under Section 111.105, and has "paid any additional tax found due in a jeopardy or deficiency determination that applies to the tax liability period covered in the tax refund claim," then the taxpayer may file suit against the Comptroller and Attorney General in district court to recover the tax refund sought.\textsuperscript{161} The taxpayer must file suit within thirty days after the denial of the motion for rehearing is issued.\textsuperscript{162} The issues considered are limited to the grounds of error asserted in the motion for rehearing.\textsuperscript{163}

\textbf{C. Payment Under Protest and Suit to Recover Taxes}

If a taxpayer believes the tax assessment cannot lawfully be collected, another alternative is for a taxpayer to submit a protest along with the payment.\textsuperscript{164} The written protest must detail the reasons supporting recovery of the tax payment.\textsuperscript{165} Like a refund claim, the protest must "be filed before the expiration of the applicable limitation period as provided by [the Tax Code] or before the expiration of six months after a jeopardy or deficiency determination becomes final, whichever period expires later."\textsuperscript{166} Paying the tax under protest allows the taxpayer to bring suit against the state to recover the tax before exhausting

\begin{itemize}
\item \textsuperscript{160} Id. § 111.1042. An informal review does not constitute a hearing or contested case, does not impair the taxpayer’s right to a formal refund hearing, and "does not toll the limitation period for any subsequent claim for refund on the same period and type of tax for which the claim for refund was fully or partially denied." \textit{Id.}
\item \textsuperscript{161} Id. § 112.151. In contrast, \textit{[i]f payment is made under protest (as opposed to denial of a refund claim), there is no requirement that the taxpayer exhaust administrative remedies prior to filing the suit for refunding the contested amount ([i.e.,] it is not necessary in payment under protest actions to file a refund claim with the Comptroller and have it denied).}
\item \textsuperscript{162} TEX. TAX CODE ANN. § 112.151.
\item \textsuperscript{163} \textit{Id.} § 112.051.
\item \textsuperscript{164} \textit{Id.} § 112.051.
\item \textsuperscript{165} \textit{Id.}
\item \textsuperscript{166} \textit{Id. §§ 111.104, 112.051.}
\end{itemize}
all administrative remedies.\textsuperscript{167} Suit must be filed within ninety-one days after the protest payment was made.\textsuperscript{168} The taxpayer must file suit against the Comptroller, the Attorney General, and "the public official charged with the duty of collecting the tax."\textsuperscript{169} If the trial court’s judgment is appealed, the taxpayer must "continue to pay additional taxes under protest as the taxes become due during the appeal," but the taxpayer need not file an additional suit for those taxes.\textsuperscript{170} If the lawsuit results in a ruling that "all or part of the money paid under protest was unlawfully demanded by the public official and belongs to the taxpayer," then that amount will be credited or refunded to the taxpayer.\textsuperscript{171}

D. INJUNCTION

A final alternative allows the taxpayer to file an action for a restraining order or injunction prohibiting the Comptroller from assessing or collecting a tax.\textsuperscript{172} The taxpayer must first file "a statement of the grounds on which the order or injunction is sought" with the attorney general.\textsuperscript{173} The taxpayer must also pay all taxes, interest, and penalties "then due" or file a bond that sufficiently guarantees the payment of taxes, interest, and penalties "in an amount equal to twice the amount . . . then due and that may reasonably be expected to become due" while the injunction is in effect.\textsuperscript{174} A taxpayer seeking an injunction “must

\textsuperscript{167} Id. § 112.052; see Lipstet, supra note 110. Section 112.052 states that a person may bring suit to recover “occupation, excise, gross receipts, franchise, license, or privilege” taxes. TEX. TAX CODE ANN. § 112.052. At least one Texas Court of Appeals case has involved a party seeking recovery of aircraft “use tax, penalties, and interest paid under protest”; although the taxpayer exhausted its administrative remedies prior to filing suit (which is not required when payment is made under protest, as opposed to when the taxpayer merely seeks a refund), the court cited Tax Code Section 112.052 as “authorizing [the] taxpayer suit after payment under protest.” Energy Educ. of Mont., Inc. v. Tex. Comptroller of Pub. Accounts, No. 03-10-00644-CV, 2013 WL 1831453, at *2 (Tex. App.—Austin Apr. 25, 2013, pet. denied) (mem. op.).

\textsuperscript{168} TEX. TAX CODE ANN. § 112.052.

\textsuperscript{169} Id. § 112.053.

\textsuperscript{170} Id. § 112.057.

\textsuperscript{171} Id. § 112.060.

\textsuperscript{172} Id. § 112.101.

\textsuperscript{173} Id.

\textsuperscript{174} Id. Section 112.108 prohibits a court from issuing declaratory relief other than that allowed under Subchapter C of Section 112 but seems to excuse the requirement of prepayment if the taxpayer files “an oath of inability to pay the tax, penalties, and interest due” and the court, “after notice and hearing, finds that such prepayment would constitute an unreasonable restraint on the party’s
show that he will be irreparably injured if the injunction is not issued, that he has 'no other adequate remedy' available to him, and that he 'has a reasonable possibility of prevailing on the merits of the claim.'

If the court decides to grant an injunction, then it must determine whether the taxes sought to be assessed or collected are due to the state.

V. RECENT CASE ANALYSIS—CURRENT TAXING AUTHORITY POSITIONS AND STRATEGIES

State revenue departments' desire to collect potentially large aircraft sales and use tax deficiencies has led to stricter interpretation (and sometimes even reinterpretation) of previously well-established exemption principles. This shift is demonstrated by the analyses and rationales in administrative and judicial decisions rendered in cases involving aircraft sales and use taxes across the United States.

A. TEXAS—OCASIONAL SALE EXEMPTION

A decision by the Texas Comptroller in 2012 demonstrates the lengths that state tax departments will go to in searching for ways to reject the application of an exemption. After the Comptroller's Business Activity Research Team (BART) was notified of the registration of a Cessna 305C aircraft, the taxpayer claimed that the purchase qualified as a tax-exempt occasional sale. The taxpayer provided a Statement of Occasional Sale in which the seller stated "that he did not hold a sales tax permit in Texas or any other state and that he had not made a sale of more than one other taxable item within the previous [twelve]
months." A BART examiner conducted searches on the Internet and determined that the purchase "was not exempt because the seller authored and sold aviation photography books at Amazon.com and at vulturesrow.com." Use tax was assessed based on the taxpayer's storage and use of the aircraft in Texas; the taxpayer requested redetermination, the case was referred to SOAH, and a hearing was ultimately held before an ALJ.

In its decision, the Comptroller first asserted that "[s]ales made by persons who hold themselves out as engaged in the business of selling, leasing, or renting taxable items (i.e., retailers) . . . are not occasional sales, even if the item sold is not the type of item that the retailer . . . normally sells." The Comptroller then cited an example from the Texas Administrative Code where a lump-sum contractor sells a backhoe, typewriter, and crane within a twelve-month period; the sale of the backhoe and typewriter qualify as exempt occasional sales, but the crane does not because the third sale of a taxable item within a twelve-month period causes the seller to become a retailer.

Ultimately, the Comptroller held that the taxpayer failed to establish with clear and convincing evidence that an exemption applied. The taxpayer submitted a Statement of Occasional Sale along with affidavit evidence demonstrating that the seller "was not in the business of buying and selling aircraft, did not sell more than one other taxable item in the [twelve] months that preceded the instant aircraft sale, and did not hold a sales tax permit in any state." Despite this showing, the Comptroller held that "the persuasiveness of [the taxpayer's] evidence [was] undermined such that there [could] be no finding as to [the seller's] status as a seller." Apparently the BART examiner's provision of Internet documents suggesting the seller is an aerial photographer who sells books of compiled photographs to the public was enough to undermine the taxpayer's affidavit evidence. The taxpayer's argument that the sales were in reality made by a corporation, not the individual seller,

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179 Id.; see supra Part III.C (discussing the requirements for an occasional sale exemption in Texas).
181 Id. at *1.
182 Id. at *3 (emphasis added).
183 Id.; see 34 TEX. ADMIN. CODE ANN. § 3.316(b)(2) (2013).
185 Id. at *4.
186 Id.
187 See id.
was also dismissed based upon the fact that the corporation was referenced on vulturesrow.com but not on Amazon.com.188

B. FLORIDA—FLYAWAY EXEMPTION

A 2009 proposed recommended order from the Florida Division of Administrative Hearings demonstrates the level of scrutiny that Florida applies to the applicability of exemptions.189 The nonresident taxpayer, Wells Fargo, claimed a flyaway exemption on the purchase of a Cessna jet; pursuant to the relevant statute, the aircraft was removed from the state on July 2, 2007, which was within twenty days after the completion of repairs.190 Wells Fargo was notified that it would be subject to a use tax assessment if the aircraft was brought back into Florida within six months for non-repair purposes.191 In September 2007, the Florida Department of Revenue began tracking the aircraft through the FlightAware service to determine whether it returned to Florida and for what purposes.192 Because the aircraft returned to Florida and Wells Fargo was initially “unable to provide repair documentation” for those flights, the Department determined that Wells Fargo forfeited its exempt status.193 The Department ultimately assessed $461,916.28 in use tax, penalties, and interest on April 15, 2008.194

The Department found that the aircraft was in Florida on “at least nine occasions” during the six-month period following its departure.195 Four of those occasions were eventually determined to be tax exempt, but the Department determined that

\[188\] Id. at *2.
\[190\] Id. at *3–4.
\[191\] Id. at *4. The statute currently reads that a taxpayer is liable for use tax if the aircraft “return[s] to [Florida] within [six] months from the date of departure, except as provided in s. 212.08(7)(f)(f).” Fla. Stat. Ann. § 212.05(1)(a) (West 2013) (emphasis added). Section 212.08(7)(f)(f) provides an exception from use tax for aircraft temporarily present in Florida: “An aircraft owned by a nonresident is exempt from the use tax imposed under this chapter if the aircraft enters and remains in this state for less than a total of [twenty-one] days during the [six]-month period after the date of purchase.” Id. § 212.08(7)(f)(f).
\[192\] Wells Fargo Nw., N.A., 2009 WL 2578225, at *4–5. The ALJ later states that the use of FlightAware and jboweb.com to obtain flight tracking information was a reliable method of obtaining evidence. See id. at *17.
\[193\] Id. at *7.
\[194\] Id. at *6. This figure was composed of $224,400.00 in use tax, $13,116.28 in interest, and a $224,400.00 penalty. Id.
\[195\] Id. at *8.
no maintenance or repairs were undertaken on the five other occasions.196 Wells Fargo did provide a repair invoice for one of those five occasions, but the Department noted the contrast between the length of that visit (1.5 hours) and other documented, tax-exempt repair visits (three to eight days).197 The Department therefore made a finding that Wells Fargo did not demonstrate the aircraft was in Florida for tax-exempt purposes on September 22, September 29, October 1, December 21, or December 23, 2007.198 The ALJ assigned to the case also dismissed Wells Fargo’s argument that the aircraft merely had a “de minimus transitory presence in Florida.”199 Ultimately, the ALJ concluded that Wells Fargo failed to prove by a preponderance of the evidence that it qualified for an exemption.200

C. TEXAS—FLYAWAY & OUT-OF-STATE USE EXEMPTION

The Texas Court of Appeals in Austin recently addressed the proper construction of an exemption statute.201 True to the trend, the court limited the extent of the statute’s application.202 The taxpayer, Energy Education of Montana, Inc. (EEM), filed a tax refund suit against the Comptroller to recover use tax that it paid under protest.203 EEM claimed it qualified for the exemption described in former Section 151.328(a)(4) of the Texas Tax Code: “an aircraft is exempt from sales and use taxes if the aircraft was ‘sold to a person for use and registration in another state or nation before any use in this state other than flight training in the aircraft and the transportation of the aircraft out of this state.’”204

196 Id.
197 Id.
198 Id.
199 Id. at *13.
200 Id. at *19.
202 See id. at *4.
203 Id. at *1.
204 Id. at *1–2 (quoting TEX. TAX CODE ANN. § 151.328(a)(4) (West 2002) (amended 2007) (current version at TEX. TAX CODE ANN. § 151.328(a)(4) (West Supp. 2013)). The current version of the statute states that aircraft are exempt from sales and use tax (“the taxes imposed by this chapter”) if “sold in this state to a person for use and registration in another state or nation before any use in this state other than flight training in the aircraft and the transportation of the aircraft out of this state.” TEX. TAX CODE ANN. § 151.328(a)(4) (West Supp. 2013) (emphasis added). As currently worded, the exemption would probably be classi-
EEM is a Montana corporation and a wholly-owned subsidiary of Energy Education, Inc. (EEI), which is a Texas corporation. EEM purchased a corporate jet to "transport EEI personnel on EEI business." Prior to the sale, EEM sent a "Texas Aircraft Exemption Certification Out-of-State Registration and Use" form to the seller. The form claimed an exemption from Texas sales tax because it would be registered and used outside Texas before any use in Texas; the form also claimed it would be registered and hangared in Helena, Montana. EEM did subsequently register the aircraft in Montana. EEI's president boarded the jet in Little Rock, Arkansas, and flew to Helena, Montana, to take delivery of the aircraft on behalf of EEM. The EEI president flew the aircraft to California for a few days before returning it to Wichita Falls, Texas. Despite originally intending to hangar the aircraft in Oklahoma, EEM hangared the aircraft in Wichita Falls; furthermore, "the majority of its flights originated in Texas." The Comptroller assessed $890,601.19 in use tax, penalties, and interest.

The Comptroller argued that former Section 151.328(a)(4) created an exemption only from sales tax "for aircraft sold in Texas to be used and kept in another state." EEM argued that former Section 151.328(a)(4) created both a sales and use tax exemption because its plain text did not require that the aircraft be purchased in Texas; furthermore, EEM argued that it complied with the statute by purchasing and registering the aircraft in Montana and then using it in Montana and California before using it in Texas. After discussing other relevant statutes and the applicable rules of statutory construction, the court agreed with the Comptroller that former Section 151.328(a)(4) "applies only to aircraft purchases made in Texas and, relatedly,
does not create a use-tax exemption.”216 The court explained that the exemption and the use tax are mutually exclusive because an exemption covering “aircraft sold ‘for use . . . in another state’” does not also cover aircraft sold for use in Texas (and subject to Texas use tax).217 In other words, the court found that “it would be unreasonable to construe former section 151.328(a)(4) to create a tax exemption for a tax that it does not impose.”218 Furthermore, the court held that “the only reasonable construction of former section 151.328(a)(4) is to limit its application to aircraft sold in Texas.”219 As support, the court cited: a subsequent subsection referring to “the person purchasing the aircraft in this state”; the fact that the statute allows the aircraft “to be flown ‘out of this state’”; and, based on its earlier decision that the exemption only applies to sales tax, the fact that sales tax is only assessed on “items sold in Texas.”220 Thanks to the court’s anti-exemption statutory interpretation, the state gained nearly $900,000 in tax revenue.

D. CALIFORNIA—COMMON CARRIER EXEMPTION

One recent California Court of Appeals case resulted in a favorable outcome for the taxpayer.221 In 2004, a Los Angeles County Assessor levied a property tax assessment of $1,025,000.00 on an aircraft owned by CKE Associates; the assessment “included a hypothetical sales tax as an element of value” despite the State Board of Equalization’s determination in 2001 that the aircraft qualified for the common carrier sales and use tax exemption.222 The Assessor filed a petition for a writ of administrative mandamus after the Appeals Board held that the Assessor improperly included the sales tax.223 The Assessor then appealed the trial court’s denial of the petition.224

The Assessor argued that CKE’s use of the aircraft as an “on-demand, unscheduled air taxi did not qualify it for the common carrier exemption from sales tax” and that, alternatively, there

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216 Id. at *3–4, *6.
217 Id. at *4.
218 Id.
219 Id.
220 Id.
222 Id. at 106, 108, 115.
223 Id. at 107.
224 Id.
was no evidence that the aircraft qualified for the exemption when the property tax assessment was made.\textsuperscript{225} The court first held that the use of the jet as an unscheduled air taxi met the definition of a common carrier and qualified for the exemption "even though the aircraft was not a commercial aircraft used for scheduled airline operations."\textsuperscript{226} In so holding, the court commented that it was "not uncommon for private . . . companies owning corporate jets, as here, to enter into agreements with charter companies to charter the jets for use by third parties."\textsuperscript{227} CKE had previously shown that 329 of the aircraft's 521.6 operational hours in the first twelve months of use were for charter purposes.\textsuperscript{228} The court found that there was "no dispute that the aircraft met the statutory or regulatory criteria for the common carrier exemption," citing the requirement that an aircraft must be "'used as a common carrier for more than one-half of the operational use during the [twelve-month] test period.'"\textsuperscript{229} According to the California Code of Regulations, "[a] flight qualifies as a common carrier use of the aircraft for purposes of the exemption only if the flight is authorized or permitted by the governmental authority under which the aircraft is operated and involves the transportation of persons or property."\textsuperscript{230} The court also stated that "'[t]he definition of a common carrier in [Section 1593] is broad enough to include unscheduled air taxi operations as well as large commercial airlines.'"\textsuperscript{231}

Next, the court held that the Assessor was charged with the burden of proving that the aircraft was not operated as a common carrier on the date of the assessment and that he had not met that burden.\textsuperscript{232} Finally, in determining whether sales tax should have been included in the property tax assessment despite the application of the exemption, the court cited several sources from the State Board of Equalization itself that indicated a rule contrary to the Assessor's contention.\textsuperscript{233} One opinion letter from 2001 explicitly stated that sales tax should not be included as an element of an aircraft's value if the aircraft was

\textsuperscript{225} Id.
\textsuperscript{226} Id.
\textsuperscript{227} Id.
\textsuperscript{228} Id. at 108.
\textsuperscript{229} Id. at 108 n.3 (quoting \textit{Cal. Code Regs.} tit. 18, § 1593(c)(1)(B) (2008)).
\textsuperscript{230} \textit{Cal. Code Regs.} tit. 18, § 1593(c)(1)(C) (2013).
\textsuperscript{231} Auerbach, 85 Cal. Rptr. 3d at 116.
\textsuperscript{232} Id. at 107, 114.
\textsuperscript{233} Id. at 114–15.
not subject to sales tax. The "Assessors' Handbook" also stated that "there are exceptions to the general rule [that sales tax is an element of value]." Therefore, the court held that the hypothetical sales tax amount should not have been included in the valuation for purposes of assessing the property tax.

E. Texas—Flight Instruction Exemption

A taxpayer who purchased and hangared an aircraft in Texas attempted to assert several different exemptions after the Comptroller assessed sales tax on the aircraft purchase. The denial of the flight instruction exemption claim in particular demonstrates how narrowly the Texas taxing authority interprets exemption provisions.

The taxpayer held a sales tax permit and therefore met the first requirement for the exemption under Section 151.328 of the Tax Code. For the exemption to apply, the taxpayer also had to show that the aircraft was sold to someone who "uses the aircraft for the purpose of providing flight instruction"; furthermore, the flight instruction must have been:

1. "recognized by the [FAA];"
2. "under the direct or general supervision of a flight instructor certified by the [FAA];" and
3. "designed to lead to a pilot certificate or rating issued by the [FAA] or otherwise required by a rule or regulation of the [FAA]."

The taxpayer introduced evidence showing the aircraft was used to provide flight instruction to the taxpayer and another person. The taxpayer also "testified that at all times since the purchase of the aircraft he was a student pilot, and that the aircraft was flown only under the direct or general supervision of flight instructors certified by the FAA." The Tax Division responded by arguing that under the statute's plain language, the

\[234\] Id. at 114.
\[235\] Id. at 114–15 (alteration in original).
\[236\] Id. at 106–07.
\[238\] See id. at *3–4.
\[239\] Id. at *2.
\[242\] Id.
exemption is only available to those "who purchase an aircraft for the purpose of providing flight instruction" and that the taxpayer and other student were merely recipients of flight instruction.\textsuperscript{243} The Tax Division further argued that the taxpayer "made numerous solo flights for his own personal use"; the taxpayer countered that all flights were "part of a course of instruction designed to lead to private pilot's certificates."\textsuperscript{244} Finally, the Tax Division argued that the tax exemption for aircraft rentals for flight training in Section 3.297 of the Administrative Code did not apply.\textsuperscript{245}

The ALJ and Comptroller held that the taxpayer did not meet the requirements under the Tax Code, Administrative Code, or prior Comptroller taxability rulings.\textsuperscript{246} Although the taxpayer provided evidence that he and the other student "obtained FAA-approved flight instruction, no documentation was presented that all the flight time was approved as part of a qualified flight program."\textsuperscript{247} The Comptroller also noted that the taxpayer failed to provide an exemption certificate "or other proof demonstrating an intent at the time of purchase to use the aircraft only for the purpose of flight instruction."\textsuperscript{248} While the taxpayer's attempt to assert several different exemptions (occasional sale, resale, and flight instruction)\textsuperscript{249} may raise an eyebrow, the Comptroller's decision does not seem to stand on very solid ground. First, the authority cited for the propositions that the taxpayer was required to complete an exemption certificate and maintain records for all flights was a State Tax Automated Research System (STAR) Document from 1998 that discussed only the rental of aircraft by students—not the exemption provided by Section 151.328 of the Tax Code.\textsuperscript{250} The Comptroller also never appeared to rule on the issue of the meaning of "providing" flight instruction under the exemption in Section 151.328.\textsuperscript{251} Furthermore, that statute does not indicate a requirement that the purchaser demonstrate that his in-

\textsuperscript{243} Id. (emphasis added).
\textsuperscript{244} Id.
\textsuperscript{245} Id. at *3–4.
\textsuperscript{246} Id. at *4.
\textsuperscript{247} Id. (emphasis added). The total flight time was 114 hours. Id.
\textsuperscript{248} Id.
\textsuperscript{249} See id. at *2.
\textsuperscript{250} See id. at *4.
\textsuperscript{251} See id.
tent at the time of purchase was to use the aircraft only for flight instruction.\textsuperscript{252}

F. \textbf{Texas—Resale Exemption}

Several recent administrative cases from Texas demonstrate the strictness with which resale exemptions are interpreted and the deference given to taxing authority policies. Aircraft purchasers often claim resale exemptions when they acquire aircraft for the purpose of leasing or renting them “in the regular course of business.”\textsuperscript{253} The Administrative Code defines a lease or rental as “[a] transaction . . . in which possession but not title to tangible personal property is transferred for a consideration.”\textsuperscript{254} For the exemption to apply, the taxpayer must provide clear and convincing proof that the aircraft “was purchased for the purpose of reselling it or leasing it to another person.”\textsuperscript{255} Furthermore, “the leases must reflect a fair market value—otherwise the transactions lack economic substance [or a true] financial business purpose.”\textsuperscript{256} The Texas Comptroller’s Audit Division often uses a benchmark to determine fair market value: “monthly lease payments should equal or exceed [1\%] of the aircraft’s purchase price.”\textsuperscript{257} If a taxpayer’s proffered evidence is “sketchy at best and at times contradictory,” the Comptroller will refuse to apply the exemption.\textsuperscript{258}

The Texas Comptroller and SOAH carefully scrutinize purported lease or rental agreements to determine whether the resale exemption applies. In one case, the Comptroller held that the exemption did not apply because an alleged lease “more closely resemble[d] a service agreement,” which does not qualify

\begin{footnotes}
\footnotetext[252]{See \textit{Tex. Tax Code Ann.} § 151.328(a)(2) (West 2013).}
\footnotetext[255]{SOAH Docket No. 304-11-8767.26, 2011 WL 7110482, at *4.}
\footnotetext[257]{SOAH Docket No. 304-10-5895.26, 2011 WL 7070185, at *11.}
\end{footnotes}
as a lease for purposes of the exemption. The agreement gave only limited operational control to the purported lessee (Company B), had language indicating the agreement was a service agreement, contained provisions regarding the payment of a “management fee and expense reimbursements” to Company B, and did not list any agreed lease or rental price. According to another case, if an aircraft owner “retains or reserves control over the aircraft during the term of an agreement with a carrier, there is no transfer of exclusive possession and control and the transaction is not a lease.” Because the taxpayer “retained some degree of control,” the Comptroller held that the aircraft was not purchased for the “sole purpose of leasing or renting it to another person,” and therefore the exemption did not apply.

Another case involving a purported lease between related entities resulted in the denial of a resale exemption. The ALJ and Comptroller first noted that the application of the resale exemption would not be denied solely because the taxpayer held a sales tax permit or did not issue a resale certificate. The decision next discussed the consequences of executing a lease between related entities. Generally, the Comptroller “honor[s] the existence and business purposes of [separate legal] entities even if related or commonly owned.” Specifically, an “aircraft charter between related entities will be recognized when the related entities pay a fair market value rate for the aircraft, . . . [and] the existence of the related business entities serve[s] a legitimate business purpose.” Evidence regarding fair market rental values was not introduced, so the Comptroller

260 The taxpayer argued that the purported lessee was given “exclusive operational control” of the aircraft, but the agreement contained a clause stating that the “[o]wner shall have the right to use the Aircraft on an as-desired basis provided owner conforms to [Company B’s] online scheduling system.” Id. (internal quotation marks omitted).
261 Id.
265 Id. at *4.
266 See id.
267 Id.
268 Id.
scrutinized the agreements themselves.\textsuperscript{269} The aircraft was utilized by three of the L.L.C. taxpayer's members; written rental agreements were not executed until approximately a year after the aircraft was purchased, "and two of the three agreements presented were not completely signed and executed."\textsuperscript{270} Therefore, the Comptroller held that the exemption did not apply because the taxpayer did not show by clear and convincing evidence that the aircraft was purchased solely for resale purposes.\textsuperscript{271}

In another case involving related entities, the ALJ conducting the SOAH hearing first explicitly found "that the Comptroller's policy that a sale for resale in the regular course of business does not include an aircraft lease between related parties that is not at fair market value, and which would not occur between unrelated parties, is a reasonable interpretation of the Tax Code."\textsuperscript{272} In this case, the Tax Division did not question the legitimacy of the related entity itself; rather, it questioned the legitimacy of the aircraft lease formed between the related entities as "lack[ing] economic substance."\textsuperscript{273} To demonstrate that the lease rate was not negotiated at fair market value, BART examiners prepared a "Lease Rate Schedule" reflecting aircraft lease rates that were posted on the Internet for comparable aircraft; those lease rates were 1.49\% of the aircraft sales price.\textsuperscript{274} The ALJ and Comptroller held that the taxpayer failed to rebut this evidence and that the exemption did not apply.\textsuperscript{275}

G. ILLINOIS—FLYAWAY EXEMPTION

In May 2009, the Illinois Department of Revenue issued a Private Letter Ruling (PLR) in response to an inquiry from a potential aircraft buyer.\textsuperscript{276} The buyer was planning to purchase, register, and hangar an aircraft outside of Illinois, but it anticipated making occasional flights into Illinois.\textsuperscript{277} The PLR request inquired as to whether Illinois's flyaway exemption would apply

\textsuperscript{269} Id. at *5.
\textsuperscript{270} Id.
\textsuperscript{271} Id.
\textsuperscript{273} Id.
\textsuperscript{274} Id.
\textsuperscript{275} Id.
\textsuperscript{276} See Letter No. ST 09-0073-GIL, 2009 WL 1561488 (Ill. Dep't Revenue May 22, 2009).
\textsuperscript{277} Id. at *1.
to the aircraft, assuming it would not be stored or used in Illinois more than ten days in any twelve-month period.278 The flyaway exemption applies if an aircraft is purchased in Illinois, is removed from the state within fifteen days after purchase (or maintenance and repair), is not based or registered in Illinois, and the purchaser submits an exemption certification.279 An aircraft is “based” in Illinois if it is “hangared, stored, or otherwise used” in the state “for [ten] or more days in each [twelve]-month period” following the sale and any authorized post-sale maintenance and repair.280

The purchaser argued that although the flyaway exemption does not, on its face, apply to an aircraft purchased outside of Illinois, it “arguably reflects a legislative determination that an aircraft that is flown into Illinois less than ten (10) days a year should not be subject to use tax regardless of where the aircraft is purchased.”281 The Illinois Department of Revenue explicitly disagreed with this argument and noted that “‘[e]very presumption is against the intention to exempt property from taxation.’”282 Instead, the Department noted that the outcome in this case depends upon whether the aircraft is purchased from a retailer or from a person who is not in the business of selling aircraft.283 If purchased from a retailer, the aircraft may possibly qualify for an exemption under the Use Tax Act for the “use, in [Illinois], of tangible personal property acquired outside [Illinois] by a nonresident individual and brought into [Illinois] ... for his or her own use while temporarily within [Illinois] or while passing through [Illinois].”284

H. Texas—Common Carrier Exemption

A case that was recently docketed with SOAH concerned the application of the common carrier exception to an aircraft that is leased to an aircraft charter management company.285 RM Aircraft Holdings, Inc., the sole member of 307RM, LLC, pur-

278 Id. at *1–2.
279 Id.; see 35 ILL. COMP. STAT. ANN. 120/2-5(25-7) (West 2013).
280 Letter No. ST 09-0073-GIL, 2009 WL 1561488, at *2; see 35 ILL. COMP. STAT. ANN. 120/2-5(25-7) (West 2013).
282 Id. at *4 (quoting United Air Lines, Inc. v. Johnson, 419 N.E.2d 899, 904 (1981)).
283 Id. at *3.
284 Id. (citing 35 ILL. COMP. STAT. ANN. 105/3-55(a)).
chased the aircraft in Wichita, Kansas, and immediately “contributed the aircraft to 307RM.” A Charter Management Agreement was simultaneously entered into with RVR Aviation, LLC, an unrelated third party. RVR Aviation is “a licensed and certificated carrier under F.A.R. Part 135” and was charged with: hiring and training pilots for the aircraft’s operation; managing the aircraft, pilots, and crew; maintaining logbooks; and providing maintenance, fuel, and an aircraft hangar. The Charter Management Agreement gave “sole and exclusive operational control of the [a]ircraft” to RVR Aviation. A BART examination led the Comptroller to determine that the common carrier exemption did not apply because “the Charter Management Agreement is inadequate” and exclusive control was “somehow . . . forfeited” when “a principal of the owner of the [a]ircraft [flew] on the [a]ircraft.” 307RM subsequently contested the sales and use tax assessment.

Section 151.328 of the Texas Tax Code exempts aircraft from sales and use tax when “sold to a person using the aircraft as a certificated or licensed carrier of persons or property.” In other words, this section exempts “the lease or rental of an aircraft to a person who is licensed and certificated by the [FAA] to operate an aircraft as a common or contract carrier in transporting persons or property for hire in the regular course of business.” The Comptroller has “uniformly and consistently” held that common carriers authorized to operate under FAR Part 135 qualify as exempt licensed and certificated carriers.

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287 Id. at 2.
288 Id.
289 Id. A relevant portion of the Charter Management Agreement provided: “On All flights, RVR shall be known as and shall be the operator of the Aircraft for all purposes and RVR shall have operational control of the Aircraft, including but not limited to control of its dispatch, scheduling, flight following, crews, and all instances of control associated therewith.” Id. at 4. RVR Aviation also agreed to “[m]aintain operational control of the aircraft on all flights.” Id.
290 Id. at 3.
291 Id. at 1.
292 TEX. TAX CODE ANN. § 151.328(a)(1) (West 2013); see 34 TEX. ADMIN. CODE § 3.297(d)(1) (2013).
293 Brief for Petitioner, supra note 286, at 2.
tion is authorized under Part 135 and is therefore exempt from sales and use taxes "on its proceeds from the lease of the [a]ircraft from 307RM." 307RM argued that it is similarly exempt from sales and use taxes because it "immediately transferred the [a]ircraft to a qualified air carrier" through the Charter Management Agreement. 307RM cited several authorities to support the argument that the Charter Management Agreement qualifies as a lease for purposes of exemption from sales and use tax. In a previous Letter Ruling, the Comptroller stated that a Charter Management Agreement that qualifies as a lease must "give exclusive control and possession of the aircraft to a Carrier over the life of the Agreement." Where an owner is able to "take 'operational control' for . . . flights in which [the] owner hires and pays the flight crews as independent contractors and agents of the owner pursuant to a pilot services agreement," the owner retains operational control—exclusive control and possession is not given to the Carrier, and the Agreement does not qualify as a lease.

The Tax Code and other Comptroller decisions have defined a lease as a transaction "in which [exclusive] possession, [use, and enjoyment,] but not title, to tangible personal property is transferred for a consideration for a certain time period." Operational control is generally indicative of exclusive possession. Because a pilot is generally presumed to have operational control over an aircraft, whoever hires, pays, and controls the pilot ultimately controls the aircraft. Furthermore, the FAA considers an aircraft that is maintained and piloted by an FAA certified carrier to "be under the operational control of the carrier."

Unlike the Charter Management Agreement in the 2007 Letter Ruling, the Agreement between 307RM and RVR Aviation "clearly sets out that the exclusive control and possession of the aircraft was to remain with the charter management com-

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295 Brief for Petitioner, supra note 286, at 2.
296 Id. at 2-3.
297 Brief for Petitioner, supra note 286, at 3; see also Tex. Comptroller Ltr. Rul. 200702945L (Feb. 1, 2007).
298 See Brief for Petitioner, supra note 286, at 3.
299 Tex. Comptroller Ltr. Rul. 200702945L; see also Brief for Petitioner, supra note 286.
300 Brief for Petitioner, supra note 286.
301 Tex. Comptroller Ltr. Rul. 200702945L; Brief for Petitioner, supra note 286, at 4.
pany." The owner, 307RM, "did not reserve the right to make flights in the aircraft in which [the] owner would take operational control and possession of the aircraft back from the charter management company." Likewise, 307RM has no part in hiring and paying the flight crews. 307RM furthermore argues that "[t]he fact that a principal of the aircraft owner was a passenger on the aircraft does not affect the facts necessary to determine whether the charter management agreement was a lease." While it is true that the Comptroller has denied exemptions where a "purchaser operates an aircraft solely under Part 91," the aircraft owned by 307RM is operated by a common carrier under Part 135 and there is no evidence that the owner took operational control of the aircraft when one of its principals was a passenger on the plane. Immediately prior to the matter being heard by the SOAH ALJ, the Comptroller changed course and agreed to render a decision upholding the exemption, finding no tax due.

VI. APPLICABILITY OF LOCAL PROPERTY TAX ENFORCEMENT TO AIRCRAFT TRANSACTIONS AND ONGOING OWNERSHIP

Sales and use taxes are not the only taxes that should concern aircraft owners and operators. Property taxes (i.e., ad valorem taxes) assessed on aircraft represent another potential source of income for local authorities—especially considering they are imposed annually. In Napa County, California, for instance, the county assessor collected property taxes on 235 aircraft that had a combined fair market value of $39,591,737 during the 2001-2002 tax year. Property taxes are usually collected by

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303 Brief for Petitioner, supra note 286, at 4–5.
304 Id. at 5.
305 Id.
306 Id.
308 Brief for Petitioner, supra note 286, at 2, 5.
the county (or other applicable local authority) in which an aircraft is domiciled and hangared (as opposed to where it is registered). The amount of tax is generally calculated by multiplying a set rate by the aircraft’s fair market value (or some portion thereof). The determination of an aircraft’s fair market value is a significant point of contention for aircraft owners that challenge property tax assessments.

A. Aircraft Property Taxation in Texas

In Texas, for example, tangible personal property used to produce income is subject to a property tax assessment by the local taxing authority. “Non-income-producing personal property,” including a personal aircraft, is exempt “unless the governing body of a taxing unit takes an official action to tax non-income-producing personal property.” In general, the “state has jurisdiction to tax tangible personal property if [it is] . . . located in [Texas] for longer than a temporary period,” is “temporarily located outside [Texas] and the owner resides in [Texas],” or is “used continually, whether regularly or irregularly, in [Texas].” More specifically, income-producing property is taxable by the local taxing unit if:

312 Stubbs, supra note 309.
313 Tax rates are generally established by the governing body of each taxing jurisdiction. See, e.g., How to Calculate Your Taxes and Who to Call, TARRANT APPRAISAL DISTRICT, http://www.tad.org/webpages/how_to_calculate_your_taxes.cfm (last visited Feb. 4, 2014). In Texas, for instance, property might be taxed by the city, county, and school district in which the property has its tax situs; each of these jurisdictions will impose its own tax rate. See, e.g., id.; Tax Rates and Levies by County, TEX. COMPTROLLER PUB. ACCOUNTS, http://www.window.state.tx.us/taxinfo/proptax/taxrates/ (last visited Feb. 4, 2014); Truth in Taxation Summary, HARRIS COUNTY TAX OFF., http://www.hctax.net/Property/JurisdictionTaxRates (last visited Feb. 4, 2014).
314 See Stubbs, supra note 309.
316 See TEX. TAX CODE ANN. § 11.14(a) (West 2013); Moore, supra note 4.
318 TEX. TAX CODE ANN. § 11.01(c). The Texas Court of Appeals in Dallas has interpreted the meaning of “used continually” and has held that an aircraft was continually used in Texas (and was properly assessed property taxes) when 23% (nine of forty-two) of its total departures were from Texas. Alaska Flight Servs., LLC v. Dall. Cent. Appraisal Dist., 261 S.W.3d 884, 888–90 (Tex. App.—Dallas 2008, no pet.).
(1) it is located in the unit on January 1 for more than a temporary period;
(2) it normally is located in the unit, even though it is outside the unit on January 1, if it is outside the unit only temporarily;
(3) it normally is returned to the unit between uses elsewhere and is not located in any one place for more than a temporary period; or
(4) the owner . . . maintains the owner’s principal place of business in [Texas] . . . in the unit and the property is taxable in [Texas] but does not have a taxable situs pursuant to Subdivisions (1) through (3) of this subsection.319

The Texas Tax Code contains special property tax provisions for commercial aircraft and business aircraft.320 A commercial aircraft is an “instrumentality of air commerce that is: (1) primarily engaged in the transportation of cargo, passengers, or equipment for others for consideration; (2) economically employed when it is moving from point to point as a means of transportation; and (3) operated by a certificated air carrier.”321 Where a commercial aircraft is used both within and outside of Texas, “the appraisal office shall allocate to [Texas] the portion of the fair market value of the aircraft that fairly reflects its use” in Texas.322 Allocation, in other words, is the determination of “the ratio of usage of personal property within each taxable situs when the property has more than one taxable situs.”323 The property tax value is calculated using a formula that implicates, among other factors, the aircraft’s fair market value and the number of revenue departures from Texas; this formula is generally more “taxpayer friendly” than the business aircraft

319 Tex. Tax Code Ann. § 21.02(a); see Fairchild Aircraft, Inc. v. Bexar Appraisal Dist., 47 S.W.3d 577, 580 (Tex. App.—San Antonio 2001, pet. denied) (reciting Section 21.02 and finding that an appraisal district’s “jurisdiction to tax exists based on the length of time property is located in the taxing unit within Texas”).
321 Id. § 21.05(e).
322 Id. § 21.05(a).
formula, discussed below.\textsuperscript{324} The applicable tax situs is designated by the aircraft’s certificated air carrier as “either the carrier’s principal office in Texas or [the] Texas airport from which the carrier has the highest number of Texas departures.”\textsuperscript{325} Even though the FAA considers FAR Part 135 certificate holders to be “certificated air carriers,” local “appraisal districts are currently taking the position that . . . [the] ‘commercial’ formula only applies to ‘regularly scheduled’ departures and is not available for Part 135 [charter] operations.”\textsuperscript{326}

A business aircraft is one that is “used for a business purpose of the owner” but does not qualify as a commercial aircraft.\textsuperscript{327} In other words, it does not “transport cargo, passengers, or equipment for others for consideration.”\textsuperscript{328} If an aircraft “is taxable by a taxing unit, and is used continually outside [Texas], whether regularly or irregularly,” then the appraisal office makes an interstate allocation of the fair market value that reflects the aircraft’s use in Texas.\textsuperscript{329} The property tax value is calculated using a formula that implicates the aircraft’s fair market value, the number of departures from Texas, and the total number of departures.\textsuperscript{330}

Although the language of the commercial aircraft and business aircraft provisions seems to place a duty upon the local appraisal offices to assess property taxes only on a fair market value figure that represents the amount of use of an aircraft in Texas, the interstate allocation will only be made if a taxpayer applies for the allocation.\textsuperscript{331} The taxpayer must file an allocation application in the appraisal district where the business or commercial aircraft has its taxable situs.\textsuperscript{332} This application must be re-filed

\textsuperscript{324} See Tex. Tax Code Ann. § 21.05(b); Moore, supra note 4. For instance, in one Texas Court of Appeals case, an aircraft’s fair market value in 1999 was $10,065,440, its property tax value under the business aircraft provision was $3,970,770, and its property tax value under the commercial aircraft provision was $74,110. See SLW Aviation, Inc. v. Harris Cnty. Appraisal Dist., 105 S.W.3d 99, 102 (Tex. App.—Houston [1st Dist.], no pet.).

\textsuperscript{325} Tex. Tax Code Ann. § 21.05(d).

\textsuperscript{326} Moore, supra note 4.

\textsuperscript{327} Tex. Tax Code Ann. § 21.055(a), (c).


\textsuperscript{329} Tex. Tax Code Ann. § 21.055(a).

\textsuperscript{330} Tex. Tax Code Ann. § 21.055(b); Moore, supra note 4.

\textsuperscript{331} See Tex. Tax Code Ann. § 21.09(a).

\textsuperscript{332} See id.
each year the allocation is claimed. As discussed below, recent case law has played a major role in interpreting the timing requirements of applying for interstate allocations.

B. RECENT TEXAS CASE ANALYSIS

Several recent cases in Texas concern challenges to property tax assessments where requests for interstate allocation were waived or denied because taxpayers either filed their allocation applications too late (or not at all) or their aircraft did not fall within the commercial aircraft or business aircraft provisions so as to qualify for an allocation. In 2000, the Texas Court of Appeals in Texarkana essentially held that a taxpayer waived its right not to have an aircraft “taxed on the full appraised value.” The taxpayer, Aramco, argued that “because [its] aircraft was an instrument of foreign and interstate commerce, its value was required to be allocated and apportioned among the taxing authorities in which the aircraft had a taxable situs.”

While the court’s holding was based on Aramco’s failure to properly follow the statutory procedures for protesting property tax assessments for multiple tax years, the court also noted that it was “difficult to see how Aramco can complain about the tax when it did not protest the appraised amount for the vehicle and did not ask for or provide a showing that it was entitled to the allocation.” According to the court, a taxing authority cannot “be expected to know that a taxpayer is entitled to an allocation unless the taxpayer provides this information.”

The Texas Court of Appeals in Houston (1st District) explicitly held in 2009 that a taxpayer waived its right to allocation when it first failed to submit information regarding an allocation contemporaneously with a rendition and then subsequently attempted to submit the information too late. The Harris County Appraisal District (HCAD) “discovered the air-

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333 See id. § 21.09(b).
335 Id. at 363 (emphasis added).
336 Id. at 366.
337 Id. at 365–66.
339 Id. at 750.
plane” and added it to the “tax appraisal roll for Harris County” in 2006.340 The taxpayer, Starflight, was obligated to “file [a] rendition form after January 1 and not later than April 15,” but it “never requested or received permission to file a [late] rendition statement.”341 Starflight argued that a letter it sent in August 2006 qualified as a late rendition letter, but the court rejected this argument and noted that the letter contained no allocation information.342 Furthermore, the court held that Starflight’s eventual submission of allocation information in December 2006 when it filed suit in district court “came too late” because precedent required Starflight to submit “information showing entitlement to allocation at the time of rendition.”343 It should be noted that one justice filed a dissenting opinion with respect to the issue of whether Starflight’s aircraft was present “in Harris County, Texas, for more than a temporary period” and could therefore be taxed in the first place.344 The majority had addressed this issue before discussing the rendition and allocation issue, and it found that the evidence was sufficient to support the trial court’s finding that the aircraft was present in Harris County on more than a temporary basis.345

In 2011, the Texas Court of Appeals in Houston (14th District) addressed a similar but distinct issue: “whether [a] taxpayer waives the right to interstate allocation when the allocation request is submitted contemporaneously with an untimely rendition.”346 HCAD “discovered [an] aircraft hangared” in northwest Harris County in August 2006 and requested information for establishing the aircraft’s taxable situs; the taxpayer, Sturgis, failed to respond and HCAD sent a Notice of Appraised

340 Id. at 744.
341 Id. at 748.
342 Id. at 748–49.
343 Id. at 749–50 (citing Tex. Gas Transmission Corp., 105 S.W.3d at 94) (emphasis added).
344 Id. at 750–53 (Jennings, J., dissenting).
345 Id. at 746–47 (majority opinion). Such evidence included, among other things: the aircraft was housed at Hobby Airport in Harris County after Hurricane Katrina; the aircraft “served only the owners and partners of its Houston affiliates exclusively”; Starflight had a place of business in Houston; the aircraft’s original hangar in New Orleans was not rebuilt after Hurricane Katrina destroyed it; “Starflight’s employees, including the plane’s pilot, relocated to Houston after Hurricane Katrina”; and flight logs showed that the majority of the aircraft’s flights in 2005 departed from Houston. Id.
Value.\textsuperscript{347} Sturgis then rendered its business aircraft in October 2006 and November 2006 for tax years 2006 and 2005, respectively, and requested interstate allocation.\textsuperscript{348} The court started its analysis by noting that the business aircraft provision in the Texas Tax Code "does not expressly condition the entitlement [of an allocation] on the timeliness of the rendition."\textsuperscript{349} A Texas Court of Appeals had previously determined, however, that the Code "necessarily implied" a requirement that taxpayers submit "allocation information at the time of rendition."\textsuperscript{350} Despite the fact that Sturgis did contemporaneously submit allocation information along with the rendition, the court held that it waived its right to allocation because the rendition itself was untimely.\textsuperscript{351} The court cited an "overriding concern for timeliness that echoes in [precedent cases]" and the "cardinal rule that . . . provisions tantamount to tax exemptions . . . must be strictly construed against the taxpayer and in favor of the taxing authority."\textsuperscript{352} Therefore, "taxpayers must timely render their aircraft before [receiving] an allocation entitlement."\textsuperscript{353}

The Texas Court of Appeals in Houston (1st District) recently clarified whether a taxpayer may request the correction of past appraisal rolls under Section 25.25(c)(3) to account for an interstate allocation.\textsuperscript{354} Prior case law indicated that an aircraft "owner's failure [to] timely . . . render property for taxation [did] not prevent a taxpayer from filing a correction of the appraisal roll to reflect an interstate allocation within the five-year deadline set forth in section 25.25(c)(3)."\textsuperscript{355} Section 25.25(c)(3) provides for the correction of an appraisal roll where property

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{347} Id. at 383.
\item \textsuperscript{348} Id. Sturgis reported the number of departures its aircraft made from Texas and "sought to apportion its final tax in Texas to roughly 47% of the aircraft's actual value for 2005, and 35% of its value for 2006." Id.
\item \textsuperscript{349} Id. at 384.
\item \textsuperscript{350} Id. (citing Harris Cnty. Appraisal Dist. v. Tex. Gas Transmission Co., 105 S.W.3d 88, 92 (Tex. App.—Houston [1st Dist.] 2003, pet. denied) (en banc)).
\item \textsuperscript{351} Id. at 385–86.
\item \textsuperscript{352} Id. at 385–87. The court also rejected Sturgis's argument that the penalty provision for delinquent renditions in Section 22.28 reveals a legislative intent to permit untimely allocations because the 10% penalty for untimely renditions sufficiently penalizes taxpayers. Id. at 386–87.
\item \textsuperscript{353} Id. at 387.
\item \textsuperscript{354} Tex. Gas Transmission Co., 105 S.W.3d at 90; see Tex. Tax Code Ann. § 25.25(c)(3) (West 2013). This case also promulgated the rule, discussed above, that taxpayers must submit allocation information at the time of rendition. Tex. Gas Transmission Co., 105 S.W.3d at 94.
\item \textsuperscript{355} Tex. Gas Transmission Co., 105 S.W.3d at 94 (emphasis added).
\end{enumerate}
\end{footnotesize}
has been included “that does not exist in the form or at the location described in the appraisal roll.”\footnote{356} After applying rules of statutory construction, attempting to ascertain legislative intent, and considering the impact of departing from precedent, the court held that the term “location” refers to the “actual, physical presence of property at the place described in the appraisal roll.”\footnote{357} This definition effectively limits the provision in Section 25.25(c)(3) to cases where an aircraft “did not physically exist at the appraisal roll location \textit{at any time} during the taxable year.”\footnote{358} Therefore, the court held that the Tax Code does not allow a correction to the appraisal roll for interstate allocation.\footnote{359}

The Texas Court of Appeals in Houston (1st District) has also interpreted the Tax Code’s commercial aircraft provision.\footnote{360} The taxpayer, SLW, claimed that its aircraft qualified as a commercial aircraft under Section 21.05 instead of a business aircraft under Section 21.055.\footnote{361} SLW’s aircraft had a fair market value of $10,065,440 in 1999.\footnote{362} Employing the formula in Section 21.055 for business aircraft, HCAD claimed that the aircraft had a property tax value of $3,970,770.\footnote{363} If the formula in Section 21.05 for commercial aircraft was applied, the aircraft would have a property tax value of only $74,110.\footnote{364} Unfortunately for SLW, the court held that the aircraft did not qualify as a commercial aircraft because it did not meet the statutory requirement that it be “operated by a certificated air carrier.”\footnote{365} SLW argued that the aircraft did in fact meet this requirement because the aircraft itself was a “‘certified air carrier’” that was “engaged in interstate or intrastate commerce under authority of the U.S. Department of Transportation.”\footnote{366} The court, however, noted that the “statute clearly requires that the \textit{operator} be a certificated air carrier” and that the record did not show this

\footnote{356} Tex. Tax Code Ann. § 25.25(c)(3).
\footnote{357} Tex. Gas Transmission Co., 105 S.W.3d at 97–99.
\footnote{358} Id. (emphasis added).
\footnote{359} Id. at 99.
\footnote{361} Id. at 102.
\footnote{362} Id.
\footnote{363} Id.
\footnote{364} Id.
\footnote{365} Tex. Tax Code Ann. § 21.05(e)(3) (West 2013); SLW Aviation, Inc., 105 S.W.3d at 103.
\footnote{366} SLW Aviation, Inc., 105 S.W.3d at 103.
requirement was met.\textsuperscript{367} The classification of the plane as a business aircraft was therefore upheld.\textsuperscript{368} In contrast, the Texas Court of Appeals in San Antonio rejected the Bexar Appraisal District's (BAD) attempt to deny the application of Section 21.05's commercial aircraft allocation formula to two different taxpayers' aircraft in 2001.\textsuperscript{369} In each case, the court first rejected BAD's argument that an aircraft's status and location on January 1 alone determines whether the commercial aircraft provision applies.\textsuperscript{370} Instead, whether an aircraft qualifies as "'commercial' is determined by looking back in time to the aircraft's use in the year preceding January 1 of the applicable tax year."\textsuperscript{371} The court stated that it would be absurd to "take an aircraft out of Section 21.05's scope if the company that owned the aircraft leased it to a [certificated] air carrier every day of the year, except on January 1."\textsuperscript{372} The fact that the aircraft in both cases were "between leases" or not being actively flown did not prevent the application of the commercial aircraft provision.\textsuperscript{373} Finally, the court also held in both cases that the allocation provision of Section 21.05 was not unconstitutional, as alleged by BAD.\textsuperscript{374} A recent Texas Court of Appeals case in Dallas denied a change to the appraisal roll under Section 25.25(c)(1) that would have resulted in a refund of $25 million in property taxes.\textsuperscript{375} The taxpayer, Southwest Airlines, used the allocation formula for commercial aircraft found in Section 21.05 to compute its tax liability to Dallas County.\textsuperscript{376} Southwest later discovered that because it calculated the allocable fair market value of

\textsuperscript{367} Id. (emphasis added).

\textsuperscript{368} Id.


\textsuperscript{370} Fairchild Aircraft, Inc., 47 S.W.3d at 579–80; First Aircraft Leasing, Ltd., 48 S.W.3d at 220–21.

\textsuperscript{371} Fairchild Aircraft, Inc., 47 S.W.3d at 581; First Aircraft Leasing, Ltd., 48 S.W.3d at 222.

\textsuperscript{372} Fairchild Aircraft, Inc., 47 S.W.3d at 581; First Aircraft Leasing, Ltd., 48 S.W.3d at 222.

\textsuperscript{373} Fairchild Aircraft, Inc., 47 S.W.3d at 582; First Aircraft Leasing, Ltd., 48 S.W.3d at 223.

\textsuperscript{374} Fairchild Aircraft, Inc., 47 S.W.3d at 582–83; First Aircraft Leasing, Ltd., 48 S.W.3d at 224–25.


\textsuperscript{376} Id. at *1.
the fleet as a whole instead of using the formula to calculate the allocable value of each individual aircraft, the company paid nearly $25 million more in taxes.\textsuperscript{377} Southwest sought to correct the appraisal roll by asserting that its mistake was a clerical error correctable under Section 25.25(c)(1).\textsuperscript{378} Despite the trial court's holding that Section 21.05 required allocation on an aircraft-by-aircraft basis and Southwest's calculation was a clerical error requiring correction, the appellate court reversed and simply held that Southwest made no clerical error permitting correction.\textsuperscript{379} "Clerical error" is defined in Section 1.04(18) as an error "that is or results from a mistake or failure in writing, copying, transcribing, entering or retrieving computer data, computing, or calculating."\textsuperscript{380} According to the court's plain language review, Southwest made no mathematical error in "computing" or "calculating" the value of its aircraft—Southwest "used precisely the figures it intended to use and then correctly computed or calculated those figures within the formula it intended to use."\textsuperscript{381} The court rejected Southwest's argument that "the failure to use the proper allocation formula was a mistake or failure in calculating or computing the allocated value."\textsuperscript{382} The court's reversal conveniently saved the county $25 million.

C. RECENT DEVELOPMENT—LOCAL TAXING AUTHORITIES IN TEXAS MOVING AWAY FROM ALLOCATING PROPERTY TAXES ON A PRO RATA BASIS

Aircraft can potentially "acquire a tax situs" in not only multiple states\textsuperscript{383} but also multiple local taxing units within a particular state. Historically, in Texas, local taxing authorities have assessed property taxes on a pro rata basis—they only tax an aircraft based on the amount of time spent in a jurisdiction or the number of takeoffs and landings in that taxing jurisdiction.\textsuperscript{384} A taxing jurisdiction uses the pro-rata taxation formula as way to

\textsuperscript{377} Id.
\textsuperscript{378} Id.; see \textit{Tex. Tax Code Ann.} § 25.25(c)(1) (West 2013).
\textsuperscript{379} \textit{Sw. Airlines Co.}, 2012 WL 210964, at *2–4.
\textsuperscript{380} Id. at *3. The Code offers an alternative definition, but Southwest did not rely on that definition. Id.
\textsuperscript{381} Id.
\textsuperscript{382} Id.
incentivize aircraft owners and operators to hangar their planes in that jurisdiction and as a method to receive at least some tax revenue (some tax revenue is better than no tax revenue). For example, Tarrant County has been more aggressive in granting pro-rata property tax calculations than Dallas County; this has resulted in many taxpayers storing their aircraft in Tarrant County even if they must make frequent trips to Dallas County to pick up Dallas-based owners or to conduct other business. Recently, however, some local taxing authorities have begun assessing the full property tax amounts on an aircraft it has jurisdiction to tax. Part of the reason for this shift is aircraft owners’ failure to pay tax for several years in a row. Local taxing authorities are much less likely to grant the more favorable pro-rata tax when a taxpayer has neglected to pay several years’ worth of tax.

VII. CONCLUSION: TAXPAYER RESPONSES TO CURRENT TRENDS AND PRACTICE TIPS FOR ATTORNEYS

State taxing authorities’ aggressive enforcement of sales and use taxes, along with their reinterpretation of exemption requirements, means that aircraft purchasers should carefully plan their transactions and aircraft owners should be aware of the tax laws implicated by the use and storage of their aircraft. State agencies often go to great lengths to create “loopholes” in order to collect taxes from taxpayers who mistakenly believe that they have covered all their bases. In fact, according to one source, “[m]ost tax collection agencies view their mission as ‘collect revenue from every imaginable source.’”

Relying solely on partial truths and the experiences of other aircraft owners to form a tax strategy could result in the forfeiture of a claimed exemption and a ruling for the payment of taxes, penalties, and interest. Furthermore, general tax pro-

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385 See Levy, supra note 4.
387 Id.
Professionals may not be properly equipped to deal with aircraft transactions because they are not experienced with the intricacies of aircraft sales, use, and property taxation. Employing an attorney who specifically has aircraft taxation experience would better insure against surprise tax assessments and adverse rulings from a state taxing authority. In fact, aircraft owners and purchasers may be best protected and informed by obtaining a ruling or advisement from their state taxing authority. Because changes in the tax laws and rulings that reinterpret tax exemptions and provisions could occur at any moment, aircraft owners and their tax attorneys must also keep up to date regarding aircraft sales, use, and property taxes.

If an aircraft owner receives a tax assessment and decides to contest it, he or she must be proactive. Experience has shown that if taxpayers and their attorneys are timely with meeting deadlines and are assertive during the administrative law process, then they may obtain more favorable outcomes. Being proactive even before an assessment occurs can improve a taxpayer’s chances with the state taxing authority. Many aircraft owners face problems during the assessment process due to prior insufficient record keeping. Aircraft owners should consider retaining an attorney to not only advise them regarding the proper exemption(s) to claim but also help them comply with the requirements for claiming the exemption (including filing and storing the proper paperwork). Although no amount of planning may ultimately deter a state taxing authority from sending a sales, use, or property tax assessment, a well-prepared, proactive, and aggressive taxpayer response is more likely to obtain a favorable outcome from a SOAH proceeding or state court lawsuit. The taxman is coming. Will your clients be ready? We believe this analysis will help you make sure they are.

389 Swirsky & Younger, supra note 387.
390 See id.
391 See Levy, supra note 4.
393 See Fields, supra note 314.
Comments