A Practitioner's Guide to State Tax Issues Related to Private Aircraft Ownership and Operation

By Michael A. Cosby

Michael A. Cosby identifies and addresses the state tax issues a client faces when owning (or leasing) an aircraft.

As more clients place a greater value on executives' productivity/time and security, many clients look to utilize private aircraft to accomplish those goals. In doing so, clients are buying (or leasing) and operating highly mobile and valuable assets. Often these clients (even the most sophisticated) lack a broad understanding of the state tax issues impacting the client's purchase, use and eventual disposition of the aircraft.

This guide is intended to provide practitioners the basics for identifying and addressing the state tax issues a client faces when owning (or leasing) an aircraft. As a practical matter, clients that own and operate aircraft also face a number federal tax issues and regulatory oversight by the Federal Aviation Administration (FAA); both topics are beyond the scope of this guide. However, there is one regulatory matter that bears noting.

Under the Federal Aviation Regulations[1] (FARs) unless an operator of an aircraft holds a common carrier license issued by the FAA and Federal Department of Transportation, that operator may not receive any compensation for operating an aircraft.[2] So, advising a client to form a special purpose/single member entity (SPE) to own and operate an aircraft to isolate liability is a direct violation of federal law. Compensation as interpreted by the FAA includes any form (such as capital contributions to fund the operation of the SPE, intercompany bookkeeping entries to recover or allocate operating cost, and/or reimbursement by an employee or other passenger for any part of the cost of operation). There may be very legitimate reasons for an SPE to own the aircraft, but there is never a reason for an SPE to operate an aircraft. Advising a client to do so exposes the client to regulatory fines of $11,000 per operation (which can be assessed retroactively),

MICHAEL A. COSBY is a Partner with the firm or Husch Blackwell LLP and practices extensively in aviation law, focusing on tax and regulatory matters.

sanctions, fines, or revocation of qualification against the pilot(s) and the possibility that the insurance coverage procured to cover liability concerns would be void for conducting flight operations in violation of the FARs.

State Sales Tax Analysis

Most states (all but five[3]) have sales, gross receipts, transaction privilege, excise or retailer occupation tax, in some form. Be that as it may, many states exempt or limit the application of such taxes on the purchase of aircraft. For example, excluded from Delaware's retailers' license tax are the sales of aircraft with a certified gross takeoff weight of 12,500 pounds or more[4]; Massachusetts exempts the sale of aircraft and repair or replacement parts exclusively for use in aircraft from sales tax[5]; New York exempts "General aviation aircraft" (*i.e.,* aircraft used in civil aviation, but not for commercial use)[6]; and North Carolina limits the sales tax rate to 3.0% with a maximum tax of $1,500 per aircraft.[7]

In addition to the complete exemption or limited application of sales tax to the purchase of aircraft, many states provide some form of exemption to non-residents purchasing and taking delivery of aircraft in their jurisdiction.[8]

JURISDICTION	EXEMPTION REQUIREMENTS
Alabama	Not permanently domiciled in state and removed to another jurisdiction within 72 hours of sale
Arizona	No use in state other than removal
Arkansas	(a) Sold by manufacturer for exclusive use outside of state, or (b) sold by nonresident to another nonresident that will be based outside of the state, or (c) sold by a resident to a nonresident with a certified gross takeoff weight more than 9,500 pounds and will be based outside of the state
California	Promptly removed following sale and aircraft is not returned to state within 12 months of removal
Colorado	(a) Removed from state within 120 days or 30 days following completion of maintenance or refurbishment work in connection with sale and (b) aircraft is not used more than 73 days in Colorado during the three years following removal from the state
Connecticut	No use in state other than removal
Florida	Removed from state with 10 days of purchase or 20 days after completion of repairs or alterations
Georgia	New aircraft manufactured in Georgia and sold by the manufacturer and used exclusively outside of Georgia and possession by buyer following sale in Georgia is solely for removal of the aircraft
Hawaii	Taxable
Idaho	Prompt removal and not used in Idaho more than 90 days in any 12-month period
Illinois	Removed from state within 15 days of sale or return to service date following post-sale modifications or repairs and is not used in Illinois more than 10 days in each 12-month period following the sale
Indiana	Removed from state within 30 days of sale or completion of repairs or refurbishment and the aircraft is based or titled in another state
Iowa	Taxable
Kansas	Removed from state within 10 days of purchase
Kentucky	Taxable
Louisiana	Aircraft manufactured in the state with a seating capacity in excess of 50 or buyer's first use is outside of the state and the buyer is (a) properly registered for sales and use tax in the state of first use, (b) reciprocal immunity exists with state of first use and Louisiana and (c) buyer obtains certificate authorizing nontaxable purchase from the Louisiana Department of Revenue
Maine	Removed from state immediately upon delivery
Maryland	Use must be principally to cross state lines in interstate or foreign commerce
Massachusetts	All aircraft sales are exempt in state
Michigan	Removed from state within 15 days of sale or return to service date following post-sale modifications or repairs, and the aircraft was not based or registered in Michigan prior to the sale and is not based or registered in Michigan after the sale
Minnesota	Removed from state and not used in the state except in interstate commerce for isolated and occasional use, and the aircraft is registered in another state
Mississippi	Taxable
Missouri	Removed from state within 10 days of sale or return to service date following post-sale modifications or repairs
Nebraska	Removed from state with 10 days of purchase

JURISDICTION	EXEMPTION REQUIREMENTS
Nevada	Taxable
New Jersey	Buyer may not be engaged in any employment, business or profession in New Jersey that uses the aircraft in New Jersey, must provide seller with affidavit, aircraft may not return to New Jersey within 12 months of purchase other than transient use or for repair service
New Mexico	Taxable, but sales by the manufacturer are deducted from gross receipts when applying tax and 50.0% of sales by non-manufacturers of aircraft not registered in the state are deducted from gross receipts when applying tax
New York	All aircraft sales are exempt in state
North Carolina	Taxable
North Dakota	Removed from state, registered in another state and not used in North Dakota more than 30 days
Ohio	Taxable
Oklahoma	Selling price in excess of $2.5MM and removed from state immediately
Pennsylvania	Taxable
Rhode Island	All aircraft sales are exempt in state
South Carolina	Taxable
South Dakota	Prompt removal from state
Tennessee	Removal within 30 days of purchase
Texas	Removed from state promptly other than use for flight training and provide seller with exemption certificate
Utah	Taxable
Vermont	Taxable
Virginia	Removal within 60 days of purchase
Washington	Applies to aircraft with certified gross takeoff weight greater than 41,000 pounds, to non-residents of states that have sales tax rates higher than Washington, or to non-residents of states that permit Washington residents reciprocal exemption
West Virginia	Taxable
Wisconsin	No use in state other than removal
Wyoming	Taxable

As can be derived from Table 1, there are a number of favorable jurisdictions for taking delivery of aircraft by clients. Keep in mind that advising clients to utilize one of "fly-away" exemptions is complex and involves analysis of nexus and a variety of other factors.[9] Being a non-resident of the delivery jurisdiction is only the start of the analysis.

When advising clients on purchase and delivery of aircraft, other exemptions, such as trade-in allowance,[10] casual and isolated sale,[11] sale for re-sale[12] (or re-lease[13]) and common carrier,[14] should also be evaluated. As noted in the introduction, there are valid reasons for using an SPE to own an aircraft; one of those reasons would be sales and use tax planning. Under a commonly used structure, an aircraft is acquired using an SPE and then the SPE leases the aircraft of an affiliated entity for operation. This option shifts the payment of sales tax from the purchase of the aircraft by subjecting the lease payment stream to sales tax. It is important to fully evaluate the terms of a jurisdiction's sale for re-lease exemption[15] as well as the affiliate relationship between lessor and lessee. For example, in Missouri if the SPE (lessor) is a disregarding entity for income tax purposes and the lessee entity is either the lessor's sole member or a disregarded entity with the same sole member as the lessor the re-lease exemption will not apply (*i.e.,* you can't lease to yourself).[16] Additionally, it may be possible for the SPE owner to acquire the aircraft and lease the aircraft to a common carrier and avoid sales tax on the purchase and lease stream payment.[17]

> *Practitioners should also factor federal and state income tax implications, as well as state entity registration and franchise tax requirements.*

Beyond the purchase of the aircraft there are sales tax considerations related to the maintenance and repair of the aircraft. The cost of maintenance and repair of any high cost asset are also generally expensive, but for aircraft the maintenance requirement is also regulated by the FAA. As such, when a client is spending hundreds of thousands of dollars (or more) to repair or refurbish an aircraft, sales tax can become a significant factor for consideration.

As practitioners advising clients on private aviation state tax issues, you need to be aware of the variety of taxes that apply to a client's aviation operation.

As with the "fly-away" and other exemptions, many states have favorable sales tax treatment of repair parts and labor for aircraft. Eighteen states[18] have a full exemption related to aircraft repair parts, while 22 states[19] have some form of limited exemption. Likewise, of the states with a general sales tax, 43 states[20] have either full or limited exemption for repair labor on aircraft.

State Use Tax Analysis

Now that the purchase/delivery planning has been completed, and the aircraft will leave the delivery jurisdiction not subject to sales tax, many clients think that's all that's needed (particularly the client's employees or staff handling the flight operations). Unfortunately, there are a number of "airport legends" that provide misinformed or outright false advise.[21] This point is only raised so that non-aviation practitioners are prepared for resistance that may come from the client's flight department or the aircraft management company assisting the client with its operations.

As practitioners we know that, generally, a state's use tax is complementary to the state's sales tax and applies to the storage, consumption and use of tangible personal property in a state. The key is to understand the basis for a jurisdiction imposing use tax. Missouri takes the positon "any" use, storage or consumption in Missouri subjects the tangible personal property to Missouri's use tax.[22] California (as noted under the fly-away exemption) presumes the aircraft is subject to use tax if the aircraft returns to California during the 12 months following delivery.[23]

Because of the mobile nature of aircraft, a client's use patterns, state(s) of residence and domicile or state(s) of business locations and principal operations should be evaluated for application of use tax. Although infrequent/occasional use in a state may not, as a practical matter, subject a client to a state's use tax, overnight hangering, long-term hanger rental and other factors may point to a secondary base of operation of the aircraft.

State Registration Fee Analysis

As with motor vehicles, many states[24] have annual registration fees for aircraft. These registration fees are imposed based on the residency of the owner or the amount of time that an aircraft may be present in a state. For example, Arizona imposes its registration requirements on non-resident aircraft owners if their aircraft is in Arizona more than 90 days in a calendar year. The 90 days is total time and not consecutive days.

In some states, the registration fees may be a fixed amount.[25] In others, the registration fee is formulaic and is based on value,[26] weight,[27] seating capacity[28] or aircraft type.[29] In most states the aircraft registration fee replaces that state's personal property tax; however, for many of those states, proper registration of the aircraft is required,[30] or the aircraft will be subject to the state's personal property tax. Virginia imposes both a registration fee and personal property tax on aircraft.

State Personal Property Tax Analysis

Of the states that do not impose aircraft registration fees, 16 states[31] have some form of personal property tax on aircraft. The personal property taxes are generally administered at the county or local level and rates vary considerably. California allows for the apportionment of personal property taxes with other jurisdictions where the aircraft establishes situs. Missouri allows owners of "commercial aircraft"[32] to apply for and apportion personal property taxes with the Missouri State Tax Commission based on the aircraft's (or fleet if more than one aircraft is owned) miles flown in Missouri versus the total miles flown for the assessment period. Likewise Texas applies a formula based on take-offs from Texas versus departures from other states for apportioning personal property taxes.

Other State Taxes

In addition to the specific taxes outlined above, practitioners need to be aware of and advise clients regarding fuel taxes and employment taxes.

Every state has some form of tax on fuel. Generally, these taxes are paid "at the pump" and vary greatly based on the location and type of fuel.[33] Becoming familiar with a client's travel patterns and advising clients on exemptions or rebates offered by some states could provide a client with tax saving based on where fuel is purchased.

As with some of the other taxes, a client's "contacts" with a particular state may implicate state withholding or unemployment taxes for a client's employee flight crew. Special attention should be paid to locations where a client's crew may have frequent overnight stays and where the client may lease hanger and crew office space.

Conclusion

As practitioners advising clients on private aviation state tax issues, you need to be aware of the variety of taxes that apply to a client's aviation operation. This article is intended to be a general guide and is by no means an all-inclusive source for taxes imposed by every county, city or special taxing district. Practitioners should also factor federal and state income tax implications, as well as state entity registration and franchise tax requirements.

Even though your client is flying high with the thought of buying and using an aircraft, as an advisor, you must caution your client to be mindful and watch their step. Recognizing the mobile nature of aircraft and the complexities such mobility has on state tax planning is the best way to avoid having a state tax assessment ground your client from fully realizing the benefit and efficiency of private air transportation.

ENDNOTES

1 Title 14, Parts 1 to 399 of the U.S. Code of Federal Regulations, as amended.

2 There are a limited number of exceptions provided the operation of the aircraft is incidental to the operator's business. *See* 14 CFR Part 91.501; *see also* Legal Interpretation to Mike Nichols from Rebecca B. MacPherson, Assistant Chief Counsel for Regulations (Dec. 31, 2010).

3 Alaska (no state sales tax, but does have local sales tax), Delaware, Montana (no general state sales tax, but has taxes on rental of accommodations and campgrounds and on vehicle rentals), New Hampshire and Oregon.

4 Del. Code Ann. 30 §2909(l).

5 Mass. Gen. L. Chapter 64H §§6(uu) and (vv).

6 N.Y. Tax Law §115(a)(21-a).

7 N.C. Gen. Stat. §105-164.4(a).

8 Commonly known as the "fly-away" exemption.

9 As noted in many of the requirements, post-closing use of the aircraft in the delivery jurisdiction impacts the decision.

10 AL, AZ, AR, CO, CT, FL, GA, HI, ID, IL, IN, IA, KS, KY, LA, ME, MN, MS, MO, NE, NJ, NM, NY, ND, PA, RI, SC, SD, TN, TX, UT, VT, WA, WV, WI (note some jurisdictions have limitations or qualifications to receive a trade in credit for aircraft).

11 AZ, CN, GA, HI, KS, KY, LA, ME, NE, NV, NJ, NM, NC, ND, RI, SC, SD, TX, UT, WA, WV, WI (note some jurisdictions have limitations or qualifications to qualify as an isolated or occasional sale for aircraft).

12 AL, AZ, AR, CA, CO, CT, FL, GA, ID, IL, IN, IA, KS, KY, LA, ME, MD, MI, MN, MS, MO, NE, NV, NJ, NM, NC, ND, OH, OK, PA, RI, SC, SD, TN, TX, UT, VT, VA, WA, WV, WI, WY (note some jurisdictions have limitations or qualifications to qualify for a sale for re-sale exemption on aircraft).

13 AL, AZ, AR, CA, CO, CT, FL, GA, ID, IL, IN, IA, KS, LA, ME, MD, MI, MN, MS, MO, NE, NV, NJ, NM, NC, ND, OH, OK, PA, RI, SC, SD, TN, TX, UT, VT, VA, WA, WV, WI, WY (note some jurisdictions have limitations or qualifications to qualify for a sale for re-lease exemption on aircraft).

14 AL, AZ, AR, CA, CO, CT, FL, GA, HI, ID, IL, IN, IA, KS, KY, LA, ME, MD, MI, MN, MO, NE, NV, NJ, NM, NC, ND, OH, OK, PA, RI, SD, TN, TX, UT, VT, VA, WA, WV, WI, WY (note some jurisdictions have limitations or qualifications to qualify for a common carrier exemption on aircraft).

15 For example, Colorado, at the option of the Department of Revenue, may allow a lessor to acquire tangible personal property under a re-lease exemption if the lease is for three years or less. *See* CRS 39-26-713(1)(a).

16 *See* Missouri Private Letter Ruling, No. LR 7304, August 28, 2013.

17 Requirements to utilize the common carrier exemption vary significantly. Some jurisdictions require exclusive possession and use by the common carrier, others require predominate use.

18 CT, GA, IN, KS, MD, MA, MI, MN, MO, NJ, NM, NY, OH, OK, PA, RI, WI, WY.

19 AZ, AR, CA, CO, FL, HI, ID, IL, IA, KY, LA, ME, MS, NE, NC, SC, TN, UT, VT, VA, WA, WV.

20 Only HI and SD have no form of exemption for repair labor on aircraft.

21 The two most common "airport legends" are that corporations (or LLCs) formed in Delaware don't have to pay sales tax in any jurisdiction and that all aircraft used in interstate commerce are exempt from sales tax.

22 Mo. Rev. State §144.610.

23 Cal. Code Regs. Tit. 11 §1620.

24 AZ, CT, HI, ID, IL, IN, IA, ME, MA, MI, MN, MS, MT, NH, NM, ND, OH, OK, OR, RI, SD, UT, VA, WA, WI.

25 HI, IL, IN, VA, WA.

26 AZ, IA, ME, MN, UT.

27 CT, ID, MA, MI, MS, NH, NM, ND, OK, RI, SD, WI.

28 OH.

29 MT, OR.

30 ME, MI, MN, MS, OH, OR.

31 AL, AR, CA, GA, KS, KY, LA, MO, NE, NV, NC, SC, TN, TX, WV, WY.

32 Aircraft with a gross take-off weight of 3,000 pounds or more. *See* Mo. Rev. State §155.010(4).

33 Gasoline, Low-Lead aviation gas or jet fuel.