Knowledge of California Taxes on Airplanes Can Save Thousands of Tax Dollars

"All you have to do is register the aircraft in Delaware and no tax but the county tax is due," one aircraft dealer told me. "If you register the aircraft anywhere outside of California the tax is avoided. That's the long and the short of it," another said. One advised me to "Park the plane in Oregon for 90 days and the tax is avoided completely."

Partial truths like these have sent many taxpayers screaming. Every lawyer doesn't know every law. Every accountant can't possibly know every regulation of every jurisdiction. What happens generally is that one taxpayer tries a strategy and it seems to work, he tells his friends and the rumor acquires the facade of fact. The basis for the kind of advice I received was probably born from the above scenario.

The mistake that is very common to all taxpayers is not knowing the depth to which a tax agency can create "loopholes" for them to collect taxes. Most tax collection agencies view their mission as "collect revenue from every imaginable source." Some agencies promote personnel based on collection statistics. The recent fiasco with the Senate hearings into the IRS has made this clear.

Armed with this basic knowledge, the following examples will illustrate the depths to which the Board of Equalization of the State of California will go to collect money. The good news is that in order to justify their collections, all agencies must create a very rigid set of policies, manuals and reliance on previous decisions. Their "methods of attack" create the best possible defense. In their desire to define exactly the guidelines that must be met, they inadvertently give the taxpayer the method to develop a defensible tax strategy.

The Supreme Court Justice Oliver Wendell Holmes declared that it is the duty of all taxpayers to aggressively pursue methods of avoiding taxes. However, misapplying rules isn't a defense. Justice Holmes merely supported your right to avoid taxes. It is illegal to evade taxes. He let you know that if you bother understanding the rules you can "avoid" taxes.

The following examples are intended to illustrate the kind of "well intentioned" mistakes that result in taxes being owed on airplane purchases.

<u>Example A</u>

A buyer owns residences in both Oregon and California. The buyer purchases an aircraft and establishes he is a resident of another state. Under certain circumstances the State of California can declare the buyer is a resident of California and demand the tax be paid.

In Garrett Corporation v. State Board of Equalization the court said the word "person" in section 6366 indicates a legislative intent that individuals and corporations, whether foreign or domestic, be subject to the same rule with respect to the exemption involved, so the word "resident" in the statute was not limited to a domiciliary concept but contemplated any factual place of abode or some permanency more than a mere temporary sojourn.

The court held that foreign corporations having their principal place of business in other states but doing considerable business in this state were not exempt from paying sales tax on airplanes purchased here and then immediately flown out of the state.

Example B

A buyer owns a business and purchases an aircraft from Seller (a dealer or private party). The buyer provides a valid resale permit number to the seller declaring that the aircraft is for resale. Even if the Board determined that the seller made a "good faith" effort to verify the buyer's representation and the seller was not liable to collect the tax, it doesn't preclude the Board from assessing the use tax on the buyer if very specific conditions are not met. In the opinion of the Board, if the buyer converts the aircraft to personal use, it can't be considered "being held for resale." The conditions of their ability to assess use tax on the transaction are very specifically written out.

Example C

Another example would be where the buyer actually takes delivery of the airplane outside of California. Just because the illusion can be created that the purchase was made entirely outside of California, the Board has rules which relate to the frequency of flights into the state, the initial date of a flight into California and even some payload requirements. If the new owner doesn't follow all the rules as they apply specifically to his purchase, they will assess use tax.

The previous examples are just a few cases where a taxpayer followed his business instincts based on his understanding of the rules. They were all assessed tax. The public records are filled with many instances of airplane purchases that have resulted in a tax liability. The sad part is that in many cases a proper strategy would have resulted in a non-taxable event. Considering the price of airplanes, this can save the buyer hundreds of thousands of dollars. What is more important, an aircraft dealer that can provide the proper tax strategy to his customers as part of his "value-added service" has a significant price advantage. The one who "knows it all" can put himself and the purchaser in jeopardy.

There are a few experts who know the law as it relates to purchases of vehicles, vessels and aircraft. If you follow the steps exactly as they lay them out, you have a chance of saving all or some part of the tax. If you think you know the law, or if you try to use someone else's strategy that worked in their case, you could be in for a shock. Each transaction lives or dies on its own merits. Only careful analysis can save you. If you have any questions regarding this article, other sales and use tax issues, or want to know if you qualify for an exemption contact Joseph Micallef at (916) 369-1200 or visit us on the web at www.aircraftexemption.com.

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