

Personal Use: SIFL

Special Valuation Rules

- Employee recognizes income using favorable standard industry fare level (“SIFL”) rates less the amount paid by the employee
- SIFL Calculation
 - Mileage Rate and Terminal Charge
 - Aircraft Take-off Weight Multiple
 - Control Employee

Personal Use: SIFL

<u>Date</u>	<u>Trip</u>	<u>Miles</u>	<u>Mileage Charge</u>	<u>Terminal Charge</u>	<u>Total</u>
8/22/03	Chicago to Minneapolis	354	67.12	34.66	101.78
8/25/03	Minneapolis to Chicago	354	67.12	34.66	101.78
12/10/03	Chicago to Tahiti	5,680	820.32	34.66	854.98
12/22/03	Tahiti to Chicago	5,680	820.32	34.66	<u>854.98</u>
	Control Employee Multiplier				<u>1,913.52</u>
	Total Income Imputed to Employee				<u>5,740.55</u>
					<u>300%</u>

Note: In this example, the maximum certified takeoff weight of the aircraft was 22,000 pounds. The graduated mileage rates in effect were \$.1896 per mile (< 500 miles), \$.1445 per mile (500-1,500 miles), and \$.1390 per mile (> 1,500 miles).

Personal Use: SIFL

Improper Calculation: Defined as an error made with regard to classification of a control employee or weight classification

- SIFL not available, must use fair market value of flight
 - Pilot provided by employer – Charter Rates
 - Pilot not provided by employer – Lease Rates for comparable plane and distance are used as fair market value
- Maintain detailed and accurate records

Illinois Sales and Use Tax on Aircraft

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General Rules

Retail Purchases

- General aviation aircraft are subject to state sales and use taxes unless there is a specific exemption.
- Five states do not have a sales tax.
- Several states exempt “flyaway” sales or visits for repairs.
- Some states exempt large aircraft.
- Many states exempt aircraft used for a particular purpose.
- Most states only try to tax aircraft registered or based in their state. Some states have adopted a first use doctrine.
- Some states try to apportion their sales tax based on usage.
- Some states grant a credit for taxes properly paid in other states.
- Some states will try to tax any aircraft that flies into the state.

- You must look at the tax consequences of operating an aircraft in all the states where it will fly.
- First plan the initial purchase of the aircraft and look at the taxes where the aircraft will be delivered, hangered and registered with the FAA.
- Other states should be examined for potential exposure that can be avoided.
- For example, if an aircraft sold outside of California is operated outside that state for more than 6 months, the presumption is that first use occurred outside of California and the aircraft will be exempt in the future even if there is substantial future flight activity.

Illinois Taxes on Aircraft

- **Aircraft purchased at retail inside of Illinois**
Retailer's Occupation Tax 6.25% to 9.25% rate depends both on the location of the seller and the location at which an aircraft is hangered or registered.
- **Aircraft purchased outside of Illinois**
Use Tax at 6.25% plus local and home rule use taxes on titled property imposed by the jurisdiction where an aircraft is hangered or registered.
- **Aircraft leased in Illinois**
Tax is due on the purchase price of the aircraft paid by the lessor. Tax is due up front even if there is an installment sale or a conditional sale! No state tax is due in the income stream. However, the City of Chicago Transaction Tax would apply to an aircraft leased in Chicago. This is a 6% tax on the lease stream and is in addition to the other taxes.
- **Aircraft purchased from private parties**
Aircraft Use Tax, effective July 1, 2003, imposes a 6.25% tax.

Illinois Tax Rates in Chicago Area

Illinois Use Tax	6.25%
Regional Transportation Authority Use Tax	.75% (Cook) .25% (Collar)
Chicago Home Rule Use Tax	1.00%
DuPage Water Commission Use Tax	.25%
Cook County Home Rule Use Tax	.75%
Chicago Transaction Tax (on lease stream, not purchase price)	6.00%

Tax Rates for Local Airports

- DuPage Airport, West Chicago 6.75%
- Aurora Airport, Kane County 6.50%
- Palwaukee in Wheeling 6.50%
- Chicago Midway Airport 8.75%
- If the transaction also included a lease in Chicago, the Chicago Transaction Tax at a rate of 6% would be imposed on the rental receipts in addition to the Chicago 8.75% tax.

Wisconsin Aircraft Based at Kenosha

- The tax rate would be 5.5%.
- There is no personal property tax.
- Aircraft registration fees based on weight.
- If the aircraft is leased there is no upfront tax and tax is imposed on the lease stream.

Indiana Aircraft Based at Gary

- The tax rate would be 5%.
- There is no personal property tax.
- If the aircraft is leased there is no upfront tax and tax is imposed on the lease stream.

Illinois Exemptions

Rolling Stock

- This exemption is claimed by airlines for airliners providing passenger service to the public as a common carrier. It is equally applicable to the freight carriers and package delivery operations such as UPS and Fed Ex. Small air charter/taxi operations may also claim the exemption as long as they are properly certified by the FAA as Part 135 common carriers for hire and operate in interstate commerce.
- The exemption extends to lessors leasing aircraft to these carriers and may permit an owner/lessor of a small aircraft to buy an aircraft tax free take advantage of the sales tax exemption, generate income to defray the cost of the aircraft and its operation, and still use the aircraft pretty much on an as needed basis.

- There is no specific number of hours, flights, or interstate trips that are required in a particular year to qualify for the exemption. The standard set in case law is “regular and frequent”.
- The lease must be executed or in effect at the time the aircraft is purchased by a lessor. The term of the lease must be for a year or longer. A lease for a year with a termination clause that ends the lease on 30 days notice will not qualify. The lessee must be a certified carrier and the aircraft must be used to transport passengers of cargo in interstate commerce.
- Interstate commerce flights for hire need not be the exclusive use of the aircraft. Owner use of the aircraft is not prohibited. However the Department closely examines the use of aircraft when this exemption is claimed.

Occasional Sale

Eliminated by Aircraft Use Tax

Effective July 1st, 2003

- When an aircraft was purchased from a person who is not a retailer of aircraft there used to be an exemption. This "loophole" was eliminated last summer. We had used this exemption frequently, especially with Federal like kind exchanges.

90 Day Business Relocation

This popular technique was eliminated more than 15 years ago and people are still trying to use it!

Trade-ins

- Trade-ins and Advanced Trade-in are still available when purchasing aircraft from retailers.
- Trade-ins are not available on swaps or purchases from non retailers. This is an unpublished IDOR opinion and is subject to challenge.
- Typically, in a trade-in situation with a retailer, the purchaser will tender the trade-in at the time of sale of the new aircraft. However, an advanced trade-in permits the purchaser to sell his aircraft to a retailer and purchase a replacement aircraft from the same retailer within 9 months and still take advantage of the trade-in credit. See, 86 Ill. Admin Code Sec. 130. 455. We obtained a letter ruling for a client that permits the use of advanced trade-ins for aircraft as well as motor vehicles. GIL 01-0126.
- Multiple trade-ins are also permitted.

Credit for Out-of-State Taxes

- There is a credit for tax properly paid to another state when an aircraft is purchased from a retailer in another state.
- The Department permits depreciation for out of state use of an aircraft before it is brought into Illinois.

Enforcement

- If the seller does not collect Illinois tax, the purchaser, has pay Use Tax.
- If a return is filed, the statute of limitations runs 3 to 3 1/2 years. If the return is not filed, the statute of limitations for Use Tax is 6 years.
- Penalties as of Jan of 2004 may be 40%.

IDOR Discovery Unit

- The Department has full time auditors assigned to finding aircraft in Illinois to tax. These auditors are very knowledgeable. They are familiar with aircraft values, the principal retailers and manufacturers of aircraft, the major leasing and financing firms and even many of the tax practitioners. They have tax exchange agreements in place with the other states and the IRS.
- The Department of Revenue receives information from the FAA on all aircraft registered at an Illinois address. The Department also gets US Customs Declaration information. The FAA information is compared to IDOT Department of Aeronautics registration information and IDOR tax return information and letters of inquiry are sent to the registered owners of aircraft that don't pass the initial examination.

- **Walking the Flight Line**

Some IDOR auditors have literally walked flight lines and hanger facilities writing down tail numbers on aircraft at Illinois airports seeking to determine if tax has been paid on a particular aircraft. We have seen the results of this at Palwaukee and Waukegan Airports.

- **Tracking Ads and Sales**

The Department subscribes to several trade journals and publications to track sales of aircraft. I have had at least one instance where an Illinois client advertised an aircraft for sale in a trade publication and was approached by the Department seeking information on the initial purchase of the aircraft.

- **Tips and Snitches**

Ex-spouses, disgruntled employees, and competitors are an unbelievable source of information for tax agencies. Illinois does not pay cash rewards for tips but still gets a good supply of information from these sources.

- **Flight Tracker software and FAA flight plan data.**
It is possible at very low cost to find out where a particular aircraft has flown based upon flight destinations filed with the FAA. If a state identifies a particular aircraft it can easily find out if the plane has flown into that state and how frequently.

- **Aircraft Spotters**

There are people who find the time to take photos of general aviation aircraft at airports world wide and post these photos on the internet with the date, time, location, and registration number.

- **Audits**

The Department can require the production of all records relating to the purchase of an aircraft if it is selected for an audit. This includes the log book and financing arrangements.

Conclusions

- Sales Tax planning may be a very important part of a purchase of an expensive aircraft.
- Many exemptions have been curtailed and enforcement has increased.
- There may still be ways of limiting or eliminating potential tax exposures.

Aircraft Ownership and Operations Planning: Tax and Regulatory Issues

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Aircraft Operations Planning: Objective of Legal Structure

- Liability protection planning
- Minimize state sales and use tax
- Maximize Federal tax deductions
- FAA compliance (often overlooked)

Aircraft Operations Planning

Corporate Attorneys, Risk Managers and CFO's who lack corporate aviation expertise often consider liability protection planning first, and conclude (incorrectly) that a Flight Department Company is required to minimize risk.

Flight Department Companies

Q: What is a Flight Department Company?

A: A Flight Department Company is a company formed for the sole purpose of acquiring (by purchase or lease) and operating an aircraft.

Flight Department Companies

Problems

Operations must be *within the scope of and incidental to the business of the company (other than transportation by air).*

Flight Department Companies DON'T QUALIFY.