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July 21, 2004

Ms. M--- H---
Vice President
A--- & M---
Tax Professionals
XXXX --- --- --- Road, Ste. XXX, #XXX
---, CA XXXXX-XXXX

Re: A--- & M---
Legal Ruling Request

Dear Ms. H---:

This is in response to your March 6, 2004, letter in which you request information as to the proper sales and use tax application regarding the exemptions for common carriers found in Revenue and Taxation code Sections (Sections) 6366 and 6366.1. Specifically, you ask whether the use of the aircraft in two hypothetical scenarios you detail qualifies as common carrier use for purposes of meeting the common carrier exemption. With regard to the two scenarios, you explain:

“In each of the following examples, let us presume the taxpayer has taken delivery of the aircraft, made first operational use of the aircraft, therefore starting the one year test period, and the aircraft has been added to the air carrier certificate of the charter operator who is properly flying the aircraft under FAA Part 135 regulations.

- “1. The aircraft is based at Van Nuys, CA. The aircraft is flown from Van Nuys, California to Santa Ana, CA for the purpose of picking up a charter customer. There are no passengers on board during this leg of the trip. The aircraft takes the charter customer from Santa Ana, CA to San Francisco, CA and then returns the customer to Santa Ana, CA. The aircraft returns to its base at Van Nuys, CA with no passenger on board. The charter customer is charged for all of the hours put on the aircraft during this flight, beginning with take off from Van Nuys, CA and ending with the return flight to Van Nuys.

Since the charter customer was charged for the flight time to ferry/reposition the aircraft between Van Nuys, CA and Santa Ana, CA, do those hours count as common carrier/Part 135?

- “2. The aircraft is based at Sacramento, CA. The aircraft is flown from Sacramento, CA to Reno, NV for the purpose of dropping off its charter customer in Reno, NV. The aircraft then returns to its base in Sacramento, CA. The return flight does not include any passengers. The next day the aircraft returns to Reno, NV with no passengers on board for the purpose of picking up the charter customer and returning him/her to Sacramento, CA. The charter customer is charged for all of the hours put on the aircraft during these two flights including the two legs which did not include passengers.

Since the charter customer was charged all of the flight time including ferrying/repositioning the aircraft, do those hours count as common carrier/Part 135?

“Based on the above two fact patterns, it is our position that both types of ferry/repositioning flights qualify as common carrier/Part 135 use because the charter customer was charged for the flight time.”

Discussion

As you know, sales tax is imposed on all retailers, measured by a percentage of gross receipts from their retail sales of tangible personal property in this state, unless the sale is specifically exempt by statute. (Rev. & Tax. Code, § 6051.) Although sales tax is imposed on the retailer, the retailer may collect sales tax reimbursement (usually itemized on the invoice as “sales tax”) from the purchaser if the contract of sale so provides. (Civ. Code, § 1656.1.) When sales tax does not apply, use tax applies to the storage, use or other consumption of tangible personal property purchased from any retailer for storage, use or other consumption in this state, measured by a percentage of the sales price, unless that use is specifically exempt by statute. (Rev. & Tax. Code, § 6201.) “Gross receipts” (for purposes of the sales tax) and “sales price” (for purposes of the use tax) generally include all amounts received with respect to the sale or use of tangible personal property, with no deduction for the cost of materials used, labor or service costs, or other expenses of the retailer, unless there is a specific statutory exclusion. (Rev. & Tax. Code, §§ 6011, 6012.)

As to the particular exemptions you inquire about, Section 6366 provides for an exemption from sales or use tax for aircraft that are used as common carriers of persons or property. And, Section 6366.1 provides for a similar exemption for aircraft that are leased (or sold to persons for the purpose of leasing) to lessees using such aircraft as common carriers. California Code of Regulations, title 18, section (Regulation) 1593, which interprets and explains Sections 6366 and 6366.1, provides guidelines for when an aircraft is used as a common

carrier of persons or property for purposes of meeting these exemptions. Regulation 1593, subdivision (a)(2) defines a "common carrier" as:

"...[A]ny person who engages in the business of transporting persons or property for hire or compensation and who offers his or her services indiscriminately to the public or to some portion of the public."

To determine whether a purchaser or lessee is using that aircraft as a common carrier, Regulation 1593, subdivision (c) sets forth a test period of the first 12 consecutive months beginning with the first operational use¹ of the aircraft. During this test period, if the aircraft's operational use is as a common carrier for more than one-half of the test period, then the carrier's principal use of the aircraft will be deemed to be that of a common carrier.² In determining common carrier use under this test, each flight of the aircraft is examined separately. For these purposes, a flight is the powered navigation of the aircraft from one location on the ground or water to the first point on the ground or water at which the aircraft lands. Regulation 1593, subd. (c)(1)(C) sets forth when a flight qualifies as common carrier use; it states:

"(C) 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. Where the aircraft does not itself transport the person or property to a location on the ground (or water), the flight does not qualify as a common carrier flight for purposes of the exemption."

Applying this rule, Regulation 1593, subdivision (c)(1)(C)1. lists a number of examples of types of flights that do not qualify as common carrier use. As pertinent to this discussion, an example of flights that do not qualify as common carrier use are "[f]lights to position or reposition aircraft by flying the aircraft from one point to another ('ferry flights')."

As to the two scenarios you detailed in your letter, I assume that no property is being transported for the customer. Instead, I assume that the purpose of the flight is solely to reposition the aircraft in order to pick up customers or to return the aircraft to its base of operations after dropping off the customers at their destination. If this assumption is incorrect,

¹ "Operational use" means the actual time during which the aircraft is operated in powered navigation in the air. Operational use includes positioning or repositioning aircraft by flying the aircraft from one point to another ("ferry flights") except when such flights are solely for purposes of having the aircraft repaired. Ferry flights solely for the purpose of transporting the aircraft to a repair location, or solely to return from a repair location, are not operational use, nor are test flights as described in Regulation 1593, subdivision (d)(2) or personnel training as described in subdivision (d)(4). (Cal. Code Regs., tit. 18, § 1593, subd. (c)(1)(A).)

² I note that for aircraft sold after January 1, 1997, there is a presumption that an aircraft is not used as a common carrier of persons or property where the gross receipts from the use of the aircraft or the lease of that aircraft to persons for use as a common carrier do not exceed 20 percent of the purchase cost of the aircraft (in cases where the aircraft is leased to a person for use as a common carrier, it is the cost to the lessor) or fifty thousand (\$50,000), whichever is less. For aircraft purchased prior to January 1, 1997, there is a similar presumption, but with different threshold amounts for gross receipts. (See Cal. Code Regs., tit. 18, § 1593, subds. (c)(1)(D and E).)

my answer may be different. Under the scenarios you have described and the assumption I have made herein, these flights are “ferry flights” that qualify as operational use but not as common carrier use for purposes of the 12-month test period detailed above. It is immaterial whether customers are charged a separately stated price for these flights; since persons or property are not on these flights they do not qualify as common carrier flights. (See Cal. Code Regs., tit. 18, § 1593, subd. (c)(1)(C).)

Sincerely,

Chris A. Schutz
Tax Counsel

CAS/ef

cc: Sacramento District Administrator (KH)