

TAX MATTERS

A newsletter dedicated to informing California Aircraft and Vessel owners about taxes

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When Delay Can Turn an Exemption into a Disaster

By Thomas A. Alston—

Failure to take quick and pertinent action can be frustrating and costly when it comes to sales and use taxes exemptions on aircraft and vessels. In fact, delay can sometimes turn a transaction that should be exempt into a taxable one.

"One of the most common problems we see is the unwitting acceptance of myths about exemptions of aircraft or vessels," explains Tom Alston, President of Aero & Marine Tax Professionals, a Sacramento, California-based consultancy that specializes in advising tax counselors and owners of aircraft and vessels on state sales and use tax exemptions. "Purchasers often accept misinformation from dealers or other owners that all they need to do to gain a California exemption is register an aircraft or vessel out of state and keep it away from California for three months. Accepting that as a sole criterion is a big mistake, and may result in charges of fraud by the Board of Equalization (BOE), which will cost the owner an additional 50% in penalties."

Alston says that while tax counselors may be familiar with sales and use tax laws, often the owners are not, and that a failure to comply can inadvertently cause exposure to penalties and interest that skyrocket tax liabilities.

"At first glance, seeking an exemption seems simple enough," Alston says. "For several reasons, though, ensuring that your client is completely absolved of any sales or use tax involves several complicated steps, extensive documentation, and often several trips to the state capital in Sacramento. One misstep can completely undermine those efforts, leaving your client with a stiff tax levy."

Alston says that one of the major problems he sees is very basic: the owner thought they were exempt because they purchased and registered the airplane out of California, but didn't know they needed to file the tax return. "When you don't file the tax return, which you must within a year from the purchase date, it opens up the statute of limitations an additional eight years. This can result in problems and costs that the owner never dreamed of."

Alston points out that many owners of large aircraft buy and sell fairly frequently, well within the nine-year period of an extended statute of limitations. If the documentation needed to support an exemption is discarded when an aircraft is sold, the owner is almost certainly exposed to taxes, interest and penalties – even if the earlier purchase transaction would have qualified for an exemption.

"This problem often occurs when the BOE learns from another agency, such as a property tax collector or the FAA, that an unexempted aircraft is being used inside California," Alston explains. "After all, it is the BOE's job to find these things out. Yet, the BOE may take no immediate action. This is like money in the bank to them. Because the aircraft owner is subject to a statute of limitations totaling nine years, the BOE can take its time in notifying the owner to learn if the aircraft qualifies for exemption. As time goes by, penalties and interest accrue. So, if the exemption is not granted because of inadequate documentation or necessary procedures were not fully followed, the owner is liable for a transaction that may otherwise have been non-taxable."

As with other states, the California tax code provides for legitimate sales and use tax exemptions. But the state BOE also readily punishes those who do not follow the law to the letter. In instances when taxes, interest and penalties accrue due to failure to file or other

non-compliance, investments in business aircraft or vessels can become financial nightmares.

In one documented case an original \$80,000 sales tax bill incurred \$8,000 in penalties and \$65,000 in interest because the out-of-state owner of the aircraft ignored the notice of tax assessment for eight years, says Alston. The state finally issued a Notice of Determination, at which point the only way the taxpayer could obtain a hearing to prove exemption was to pay the entire tax and file a claim for refund. However the aircraft owner could not recover the documentation to support the rightful exemption, and had to forfeit the entire amount.

While Alston's experience with thousands of aircraft and vessel transactions includes many exemptions that were granted after sales, he says the right time to hire a "tax" professional is before a purchase is made, thereby avoiding the danger of failing an audit.

"When the purchaser or their tax counselor hires us before the transaction starts, we give them a written guarantee that they'll legally avoid California sales and use tax. To do that they only have to follow our instructions," Alston says.

If an owner has already purchased an aircraft or vessel and is going through a BOE sales and use tax audit, Alston advises that they do not delay. "Send me copies of everything you've got and I'll do an analysis of it at no initial cost. I can then come back to you and tell you what documents you need for the transaction to be exempt, or I'll tell you right away if there is no choice but to pay the tax, how soon you ought to pay it, and whatever interest rates and penalties might be involved."

Alston asserts that while tax advice is largely within the province of CPAs and attorneys, when it comes to sales and use tax of aircraft and vessels, a specialist who is geared for a quick and thorough resolution can be a vital resource to these tax counselors.

"Some attorneys and CPAs are inclined to do this work themselves because they want to protect their clients and it's a source of

revenue,"he says. "However, getting this type of sales and use tax exemption is not typically an attorney's or CPA's type of work. It includes looking through log books, keeping track of various flight requirements, where the airplane or vessel has gone, and who's been on it. It doesn't take a legal or financial background to do that kind of work. But since we're a specialist, a confidential third-party service to the CPA or attorney, we can often help them resolve a client's problem more economically, with a higher degree of confidence and much more quickly than they can do it themselves."

Before companies like his came along, most money professionals only had the time to print copies of the regulations, send them to their client with some instructions, and then wish them good luck, Alston adds. "Rightfully so, their time is too valuable to do any follow-up. On the other hand, specializing in legally avoiding sales tax on aircraft and vessels is all we do."

Alston attributes much of his success to researching years of decisions and recommendations by the BOE. "These are like a legal brief of every case that went before one of the hearing officers. What you get is the BOE's entire case laid out with evidence, and their decision, along with the 'why' of it. Our firm has developed a checklist of all the failure points, and we apply 100% of the points to every one of our customers. As a result, there isn't any way for them to fail to win their exemption."

Tom Alston is the CEO of Aero & Marine Tax Professionals located in Sacramento, California. Alston and his associate Madelyn Helmle are California's most well known specialists in legally avoiding sales tax on aircraft, having won countless exemptions for their clients and publishing many articles on the subject. Aero & Marine Tax Professionals is a professional company with the expertise to help its clients save money by legally avoiding sales tax on the purchase of aircraft and vessels.

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