

TAX MATTERS

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

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The Long Arm of the Board of Equalization

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"I don't live in California so I don't have to pay sales or use tax in California."

This statement has been made by many people who have subsequently been assessed use tax by the California State Board of Equalization (Board) on the purchase of a vessel or aircraft that was used in California. The Board assesses use tax on all vessels and aircraft which are used in California regardless of where they are purchased, where they are registered or where the owner resides. This may sound extreme, but remember, we are talking about a tax agency.

The California Sales and Use Tax Law and Regulations covering this area are explained below. Section 6201 of the Revenue and Taxation Code imposes a use tax on the storage, use or other consumption in California of tangible personal property purchased for storage, use or consumption. The general test for determining whether property was purchased for storage, use or consumption in California is set out in subdivision (b)(3) of Regulation 1620, which states as follows:

"Property purchased outside of California which is brought into California is regarded as having been purchased for use in this state if the first functional use of the property is in California. When the property is first functionally used outside of California, the property will nevertheless be presumed to have been purchased for use in this state if it is brought into California within 90 days after its purchase, unless the property is used or stored outside the state of California one-half or more of the time during the six-month period immediately following its entry into this state."

Other sections of law also create presumptions that property was purchased for storage, use or other consumption in this state. For example, Section 6246 provides:

"It shall be further presumed that tangible personal property shipped or brought into this state by the purchaser was purchased . . . for storage, use or other consumption in this state."

Simply stated, a vessel or aircraft is presumed to have been purchased for use in California if it is brought into the state within 90 days from the date of the purchase.

We will provide the following examples of real cases to illustrate our point. Because of confidentiality concerns, any data that might reveal the true identity of the taxpayer will be omitted.

Recently, we were contacted by someone who found out that you do not need to live in California to be assessed use tax by California. This individual purchased an aircraft in Arizona where he resides. The aircraft was registered and primarily used in Arizona after the purchase. However, the aircraft did enter California one time during the first ninety days of ownership. The aircraft landed in California, spent one night and then left the state. The individual subsequently received a bill from the Board for use tax on the purchase of the aircraft.

The substance of a transaction is the events that actually occurred. While this aircraft met the substance requirements to obtain an exemption from California use tax by complying with the six-month test period under Regulation 1620 (b) (3), even though it did fail the ninety day test period, the taxpayer must also provide the form. The form is the documentation that supports the substance.

In other words, the person must prove that he does not owe the tax. He must provide documentary evidence to the Board which supports that the aircraft was used and stored outside the State of California more than 50% of the time during the six month period following the aircraft's first entry into the state. Once a taxpayer provides documentation to support the aircraft met these requirements, he will be granted an exemption from use tax. However, he must go through an arduous process. He can not sit in his out-of-state residence and ignore the claim by California. If he ignores their communications because he knows he is not a resident of California, and also knows he met the requirements of Regulation 1620, California may place a lien on his aircraft.

By ignoring the California Board and allowing a Notice of Determination to go final, the only way the taxpayer can get an opportunity to prove his aircraft was exempt is to pay the tax and file a claim for refund.

Additionally, California does provide exemptions from sales and use tax for nonresidents who purchase aircraft in the state. Sales and Use Tax Regulation 1593 states in pertinent part:

"A nonresident will be considered as not using the aircraft other than to remove the aircraft from California if the aircraft is promptly removed from the state and is not returned to California within 12 months after its removal from this state."

However, a nonresident who attempts to use this exemption must be very aware of how it works. If a nonresident purchases an aircraft while it is in California, he must make no use of the aircraft in the state other than to immediately remove it from the state and the aircraft must not return to California for one year. This exemption applies only to aircraft.

To make this point we will provide the following example of an actual case. A few years ago a taxpayer who was not a resident of California purchased a vessel in California, removed it from the state, traveled to his home state of Washington and promptly paid the use tax to Washington. Subsequently, the taxpayer was notified by the California Board that he owed tax in California. When he contacted the California agency he informed them he was only a resident of Washington, he intended to only use the vessel in Washington, and that he had paid his use tax directly to Washington.

The Board informed him that because he took possession of the vessel inside California and did not purchase the vessel from a California retailer of vessels, the transaction was subject to use tax in California. The taxpayer then attempted to get a refund of the Washington use tax and discovered that because the tax in California had not been paid prior to the entry of the vessel into Washington, his payment to Washington was not subject to a credit for tax paid in another state.

The taxpayer then contacted the California Board and told them he would not pay the tax twice, and felt that since he owned no property inside California the Board had no lien rights. Unfortunately for the Washington resident, the collection department of the California Board of Equalization has very long arms and is very creative in ways of collecting what is owed them.

The Board can file a lien with all the national brokerage firms. They merely send a notice with the taxpayer's name to firms like Schwab, Morgan Stanley, and every other national firm. Because the Washington resident had money in an account that also had offices in California, the Board placed a lien on the brokerage account and was given the money.

Face it: the California State Board of Equalization is an equal opportunity taxing authority. If you purchase a vessel or aircraft and use it in California, even for one day, be aware that California may assess use tax on the purchase whether you live in California or not, and it will be up to you to prove that you do not owe the tax.