

Legislative Analysis



TAXES ON AIRCRAFT PURCHASED FOR SUBSEQUENT LEASE OR RENTAL

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House Bill 5855

Sponsor: Rep. Fulton Sheen

Committee: Tax Policy

Complete to 3-28-06

A SUMMARY OF HOUSE BILL 5855 AS INTRODUCED 3-14-06

The Use Tax Act permits a lessor (a person or entity that conveys property by lease) to elect to pay use tax on receipts from the rental or lease of the tangible personal property in lieu of paying sales or use tax on the full cost of the property at the time it was acquired. The act further provides that for tax years beginning after December 31, 2001, for an election to be valid, the lessor of an aircraft must obtain a use tax registration by the date set for the first use tax payment under the lease or rental agreement or 90 days after the lessor first brings the aircraft into the state, whichever is earlier.

House Bill 5855 provides that for the tax years that begin after December 31, 1999, and before January 1, 2002, for an election to be valid, the lessor of an aircraft must have obtained a use tax registration by the date set for the first use tax payment in the lease or rental agreement or 150 days after the lessor first brought the aircraft into the state, whichever was earlier.

MCL 205.95

FISCAL IMPACT:

There is insufficient information currently available to determine the bill's fiscal impact. The fiscal impact statement will be revised as information becomes available.

BACKGROUND INFORMATION:

Legislative History

The aircraft provision in MCL 205.95 was added with the enactment of Public Act 255 of 2002, with the apparent intent of providing clarification as to when the lessor election was to be made when the property subject to the use tax was an aircraft.

Rule 82 of the General and Specific Sales and Use Tax Rules

Rule 82 of the General and Specific Sales and Use Tax Rules (R 205.132) states, "A person engaged in the business of renting or leasing tangible personal property to others shall pay the Michigan sales tax or use tax at the time he purchases tangible personal

property, or he may report and pay use tax on the rental receipts from the rental thereof. A person remitting tax on the purchase price as a purchaser consumer or remitting tax on rental receipts as a lessor, shall follow 1 or the other methods of remitting for his entire business operation. A person remitting tax on rental receipts shall be the holder of a sales tax license, or a registration as is provided in the use tax act. Each month such lessor shall compute and pay use taxes on the total rental charges."

Revenue Administrative Bulletin 88-39

The lessor election is also addressed in the Department of Treasury's Revenue Administrative Bulletin 88-39. Under the bulletin, lessors electing to pay tax at the time the property is acquired (lessor/consumer) are subject to Michigan sales and use taxes on all tangible personal property to be leased in the state and other tangible personal property used in the business. Lessors electing to pay the tax based on rental receipts (lessors/retailers) must obtain a use tax registration from the Department of Treasury and are liable for use tax on the total rental receipts. Lessors/retailers are allowed to purchase tangible personal property (and necessary replacement parts) for lease or rental as necessary, tax-exempt.

To RAB 88-39, a recent decision of the Michigan Tax Tribunal held the bulletin "states that a taxpayer who wished to be classified as a Lessor/Retailer must first obtain a use tax registration...Implicated in this chronology is that the nature and character of the remittance of use tax must be determined prior to time at which use tax becomes due on the purchase price of acquired personal property, and [the Department of Treasury] must be rightly apprised of the method to use, as to not do so would predicate a proper use tax assessment on the purchased price." (See *Mack LLC v. Michigan Department of Treasury*)

Recent Michigan Tax Tribunal Decisions

Mack LLC v. Michigan Department of Treasury

The Michigan Tax Tribunal has issued several decisions related to MCL 205.95 and its applicability to aircraft. In *Mack LLC v. Michigan Department of Treasury* (MTT Docket No. 272776), the MTT stated, "A person engaged in the business of renting or leasing tangible personal property to others must pay the Michigan use tax at the time of acquisition, or may elect, at the time of purchase, to report and pay use tax on the rental receipts of the lease commenced with the acquired property. In whichever manner the taxpayer elects to pay the use tax, the taxpayer must make the election prior to or contemporaneous with the acquisition of such tangible personal property. A reasonable interpretation is that the election of one method or another must be made either prior to or contemporaneous with the acquisition of such property to avoid immediate use tax liability. Filing after acquisition would preclude the proper election of the exception. Such an election is also not indicated by intent, no matter how frequent or vociferously announced. There are some very specific steps that need to be followed in order to predicate this election."

It should be noted that the MTT's decision in *Mack* concerned the application of the use tax to an aircraft that was brought into the state in December 1997. At the time, the aircraft provision in MCL 205.95 was not yet in place. Although the MTT's decision was entered on February 11, 2003, subsequent to the enactment of Public Act 255, it did not address the aircraft provision itself.

Glieberman Aviation v. Michigan Department of Treasury

Additionally, the lessor election was also the subject of the MTT's decision in *Glieberman Aviation v. Michigan Department of Treasury* (MTT Docket No. 281362; entered March 10, 2005), which also concerned aircraft purchased prior to the enactment of Public Act 255 of 2002. In *Glieberman Aviation*, the MTT essentially affirmed its prior decision in *Mack* (and other decisions) as it relates to when the lessor election is to be made. According to the decision, *Glieberman Aviation* purchased an aircraft on or around August 16, 2000 and brought it into Michigan two days later, and obtained a use tax registration, via telephone, on December 15, 2000. (The department received a signed registration form on December 28, 2000.)

According to the MTT decision, *Glieberman* contended that at the time the aircraft was purchased there was no express requirement that a use tax registration be obtained prior to acquisition. This contention was based, in part, on the fact that the Use Tax Act was subsequently amended by Public Act 255. The Department of Treasury, in its brief, reiterated its position in RAB 88-39 and, in relying in the MTT's recent decision in *Mack* and other relevant decisions, further stated, "The rental receipts option is an exception to the general rule of the UTA. If a company is not registered for taxes with the State of Michigan, the company does not have the option of how to pay sales or use tax. Rather, the taxpayer would owe a use tax liability of six percent of the fair market value of the aircraft at the time of purchase or when it used the aircraft. Treasury has chronological criteria that are required to be in place before a lessor may submit use tax on rental receipts."

In determining whether *Glieberman* was required to obtain a use tax registration as a prerequisite to electing to pay use tax on rental receipts, the MTT decision relied on the Michigan Court of Claim's 1993 decision in *Vixen Air v. Melvin Van Vorst* and the MTT's recent decision in *Mack LLC v. Department of Treasury*. Quoting the Court of Claims, the MTT decision stated that the Use Tax Act and related rules, "make it plain that a taxpayer has a duty to pay use tax on the purchase of tangible personal property at the time he purchases said property, or before the transfer of tangible personal property, if it is a vehicle, ORV, mobile home, snowmobile watercraft, or, as in this case, an aircraft. This duty still applies even if the taxpayer elects to pay the use tax as a percentage of rental receipts by renting the tangible personal property at issue, as provided in Rule 82, R 205.132, and obtaining the necessary registration. This duty is not suspended pending the decision as to whether or not the taxpayer qualifies, or finally decides, or discovers, he may elect to pay the use tax as a basis or rental receipts received. The taxpayer has a duty to pay the use tax at the time of purchasing the tangible personal property or at that time, elect to make payments of the use tax as a percentage of rental receipts received

thereof...The Court is of the opinion that pursuant to the above analysis that the time to register and make the election is before or at the time of purchasing tangible personal property."

The MTT held that given the fact that Gliberman Aviation was not registered with the Department of Treasury at the time the aircraft was purchased, and did not actually register until more than four months later, could not elect to pay use tax based on rental receipts. Gliberman was subject to use tax of \$249,000, based on the aircraft's retail value of \$4,150,000, plus penalties and interest. The appeal is currently pending before the Court of Appeals.

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.