

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 07-32**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Application of Tennessee sales and use tax to airplane leases.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[THE TAXPAYER] is a Tennessee corporation that buys airplanes for lease to other companies. In some instances, the Taxpayer leases airplanes to companies without a pilot. On other occasions, the Taxpayer provides a pilot when the airplanes are leased. The Taxpayer provided an executed copy of an Aircraft Lease Agreement in which the Taxpayer provided both the airplane and a pilot to the lessee.

QUESTIONS

1. The Taxpayer leases an airplane to Company B without a pilot at the rate of \$700 per hour. Company B provides its own pilot. Is this lease subject to Tennessee sales and use tax?
2. The Taxpayer leases an airplane to Company C with a pilot at the rate of \$800 per hour. The pilot is the owner of both [TAXPAYER] and Company C. Is this lease subject to Tennessee sales and use tax?

RULINGS

1. Yes.
2. No.

ANALYSIS

1. The Taxpayer will be subject to sales tax on the lease when the Taxpayer provides only the airplane to lessor and does not provide a pilot and/or crew.

The lease of tangible personal property is subject to sales tax pursuant to Tenn. Code Ann. § 67-6-204(a).¹ The sales tax on a lease is applied to

. . . the gross proceeds of all leases and rentals of tangible personal property in this state where the lease or rental is a part of the regularly established business, or the same is incidental or germane thereto. The tax is levied as follows:

- (1) At the rate of tax levied on the sale of tangible personal property at retail by the provisions of § 67-6-202 of the gross proceeds derived from the lease or rental of tangible personal property, as defined herein, where the lease or rental of such property is an

¹ Tenn. Code Ann. § 67-6-102(25) defines “lease or rental” as “the renting of tangible personal property and the possession or use thereof by the lessee or renter for a consideration, without transfer of the title of such property.”

established business, or part of an established business, or the same is incidental or germane to the business.

(2) At the rate of tax levied on the sale of tangible personal property at retail by the provisions of § 67-6-202 of the monthly lease or rental price by lessee or renter . . . to the owner of the tangible personal property.

Tenn. Code Ann. § 67-6-204(a).

In addition to the above statute, the Commissioner has promulgated TENN. COMP. R. & REGS. 1320-5-1-.32 as further guidance on the taxation of leases of tangible personal property. This rule provides, in pertinent part, as follows:

(1) The gross receipts or gross proceeds derived from or amount agreed to be paid for the lease or rental, within Tennessee, of all kinds or types of tangible personal property are subject to the Sales or Use Tax. The tax shall be computed on the gross receipts, gross proceeds, or rental payable without any deduction whatsoever for expense incident to the conduct of business.

(2) The terms of the contract under which such tangible personal property is leased or rented shall be the basis for computing the tax. The tax is to be computed on a billing basis, either on the lump sum at the time of execution, or on a monthly or periodical basis as provided in the contract.

For purposes of the sales tax, tangible personal property includes “personal property, which may be seen, weighed, measured, felt or touched or is any other manner perceptible to the senses.” Tenn. Code Ann. § 67-6-102(45)(A). The airplane meets the definition of tangible personal property; therefore, based upon the above statutes and regulations, the gross proceeds of the lease between the Taxpayer and Company B are subject to sales tax.²

2. The Taxpayer will not be subject to sales tax when the Taxpayer provides both the airplane and the pilot. This is a service not subject to sales tax.

As described above, the airplane is tangible personal property, the lease of which is subject to sales tax. Tenn. Code Ann. § 67-6-204(a)(1). If, however, tangible personal property is leased by an owner who exercises continuous supervision over the leased

² In addition to the 7% sales tax. Tenn. Code Ann. § 67-6-702(a) authorizes cities and counties to impose a local sales and use tax “on the same privileges” subject to state sales and use tax; however, the local tax has a limitation, commonly referred to as a “cap.” This cap restricts the application of the local sales and use tax to the first \$1,600 on the sale, lease, or use of any single article of tangible personal property. The state has also chosen to impose a higher tax rate on items and leases in which the price or lease payments exceed \$1,600. Tenn. Code Ann. § 67-6-202(a) provides for an additional state tax of 2.75% (above the regular state rate of 7%) which applies to the amount in excess of \$1,600 but less than or equal to \$3,200 on the sale, lease, or use of a single article of tangible personal property. Consequently, the local tax will apply to each lease payment up to \$1,600, and the additional 2.75% state tax rate will apply to the next \$1,600. Any amount of the lease payment in excess of \$3,200 will only be subject to the 7% state rate.

property and furnishes an operator or crew to operate the property, the owner is deemed to be rendering a nontaxable service for sales and use tax purposes. Tenn. Code Ann. § 67-6-204(b).

The Tennessee Supreme Court interpreted Tenn. Code Ann. § 67-6-204(b) in *Hyatt v. Taylor*, 788 S.W.2d 554 (Tenn. 1990). Upon reviewing the application of this provision to water treatment equipment leased to homeowners, the Court noted that the exemption is “limited to tangible personal property that requires the continuous presence of an operator or a crew in order to perform the function it is designed to accomplish. The primary example intended by the legislature was expressly stated in the last sentence of the Act, the owner of an airplane furnishing a pilot or crew to operate the airplane.” *Id.* at 556.

When the Taxpayer is providing both the airplane and pilot under the lease, the Taxpayer is deemed to be rendering a service; therefore the gross proceeds of the lease are not subject to sales tax. However, while the Taxpayer will not be required to collect sales tax on the charge to its customers under these facts, as a result of using the airplane primarily to provide a service, the Taxpayer will owe sales and use tax on the purchase price of the airplane.

To clarify the principles behind this conclusion, the purchase of an aircraft for resale is generally not subject to sales tax. *See* Tenn. Code Ann. § 67-6-102(34)(A)(defining a taxable retail sale). As noted above, pursuant to Tenn. Code Ann. § 67-6-102(25), a lease qualifies as a resale for purposes of this principle. If, on the other hand, an airplane is purchased primarily for one’s own use, such purchase is subject to use tax. *Op. Tenn. Att’y Gen.* 84-213 (1984).

In order for the purchase of the aircraft to be treated as a purchase for resale, and thus not subject to sales tax, the purchaser must present a valid resale certificate to the seller at the time of purchase. In addition, the purchaser must actually lease or resell the aircraft. In the case where a subsequent sale of the aircraft serves as the “resale” that excuses the taxpayer from paying sales tax on its purchase, the taxpayer must not make use of the aircraft before such sale. In the case where leasing the aircraft serves as the applicable “resale,” leasing must be the primary purpose for which the aircraft is held, in comparison with any other use such as providing services with a taxpayer-furnished operator. Otherwise, the taxpayer will be subject to use tax on the aircraft.

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APPROVED: Reagan Farr
Commissioner

DATE: 11/20/07

