

ST 08-14

Tax Type: Sales Tax

Issue: Use Tax On Aircraft Purchase

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS)	
)	No. 07-ST-0000
)	IBT No. 0000-0000
v.)	Denial of Claim for Use Tax: 2/28/07
)	
ABC SERVICES, INC., TAXPAYER)	Kenneth J. Galvin, Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Mr. Larry Kajfes, Law Office of Larry S. Kajfes, Ltd. on behalf of ABC Services, Inc.; Mr. John Alshuler, Special Assistant Attorney General, on behalf of the Department of Revenue of the State of Illinois.

Synopsis:

This matter comes on for hearing pursuant to ABC Service’s (hereinafter “ABC” or “taxpayer”) protest of the Department’s MTC-29, “Notice of Tentative Denial of Claim for Use Tax,” dated February 28, 2007. The basis of the denial was the Department’s determination that ABC was not entitled to a refund for the payment of use tax on a 1994 Beechcraft King Air, B 200, Serial No. BB XXXX (hereinafter the “aircraft”) purchased on or about August 8, 2002. ABC protested the denial on April 26, 2007. An evidentiary hearing was held in this matter on January 29, 2008, with Mr. John Doe, 100% Shareholder and Vice-President of ABC, testifying. Following a review of the testimony and the evidence submitted by ABC, it is recommended that

the Notice of Tentative Denial of Claim for Use Tax be finalized as issued. In support thereof, the following “Findings of Fact” and “Conclusions of Law” are made.

Findings of Fact:

1. The Department’s *prima facie* case, inclusive of all jurisdictional elements, is established by the admission into evidence of the MTC-29, “Notice of Tentative Denial of Claim for Use Tax,” dated February 28, 2007, covering the period of August 8, 2002. Tr. pp. 10-11; Dept. Ex. No. 1.
2. On August 7, 2002, an “Aircraft Purchase Agreement” was executed between XYZ Company (“XYZ”) as Seller and XXX, LLC (“XXX”), as buyer, for a 1994 Beechcraft King Air, B 200, for \$1,644,750. Tr. p. 28; Taxpayer’s Ex. No. 1.
3. On August 7, 2002, an “Aircraft Purchase Agreement” was executed between XXX, LLC and ABC for a 1994 Beechcraft King Air, B 200, for \$1,644,750. Tr. pp. 14-16; Taxpayer’s Ex. No. 2.
4. A “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” dated August 8, 2002 for a Beechcraft King Air, B 200, shows “Seller” as XYZ and “Purchaser” as XXX, LLC. Tr. pp. 22-24; Dept. Ex. No. 3.
5. A “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” dated August 8, 2002 for a Beechcraft King Air, B 200, shows “Seller” as XXX, LLC and “Purchaser” as ABC Services, Inc. Tr. pp. 22-24; Dept. Ex. No. 4.
6. The NUC-1, Illinois Business Registration, for “XXX, LLC” lists its “principal business activity” as “dealer in aircraft.” The business was started in Illinois on March 21, 2002. “Retail” is checked on the NUC-1 as the “category that best describes your type of business.” Section 2 on the NUC-1, entitled “Sales Tax and Reseller Registration,” Question 1, asks

“[D]o you sell any merchandise at retail from a site in Illinois?” The response was “yes.” Question 9 asks “[D]o you sell new or used cars, trucks, motorcycles, watercraft, aircraft, trailers, mobile homes or salvage items?” The response was “yes.” Question 13 asks “[W]hen did you (or will you) make your first inventory purchase or taxable sale?” The response was “August 8, 2002.” The NUC-1 is signed by “XXXX,” as President. Tr. p. 11; Dept. Ex. No. 2.

7. On August 6, 2002, XYZ and Jones Exchange Corporation entered into a “Tax Deferred Exchange Agreement” in which Jones agreed to act as intermediary for the exchange of the aircraft at issue in this proceeding and a “new asset,” which would qualify as replacement property under Internal Revenue Service section 1031(k)-1(a). Tr. pp. 18-20; Taxpayer’s Ex. No. 4.
8. On August 8, 2002, XYZ notified XXX by letter that “pursuant to a certain Exchange Agreement between XYZ Company and Jones Exchange Corp., as Qualified Intermediary,” the rights under agreement to sell [the 1994 Beechcraft King Air B 200] to XXX, LLC had been assigned to Jones Deferred Exchange Corporation. “It is intended that this transaction be treated by the seller as part of a tax deferred exchange of the property rather than an outright sale.” Tr. pp. 19-20, 29; Taxpayer’s Ex. No. 5.
9. YYY Aviation was responsible for the pre-purchase inspection of the aircraft. The escrow agent for the sale was Insured Aircraft Title. ABC conveyed funds to the escrow agent and the title to the plane was deposited by XXX with the escrow agent. ABC received title on August 8, 2002. Tr. pp. 16-18.

Conclusions of Law:

In March, 2002, Mr. John Doe, Vice-President and 100% Shareholder of ABC Services, Inc., was advised by a pilot that XYZ was selling a Beechcraft King Air, B 200, Serial No. BBXXXX. Tr. pp. 5-6, 13-14. Mr. Doe contacted XYZ and an agreement was consummated. There was testimony at the evidentiary hearing that part of the agreement contained a proviso that either party, by giving written notice prior to the delivery date, could effect the sale and purchase of the aircraft by means of a trade-in and exchange of property that was intended to qualify as a tax-deferred “like kind exchange” under Section 1031 of the Internal Revenue Code. Section 1031(a)(1) of the Internal Revenue Code provides an exception to the general rule requiring the recognition of taxable gain upon the sale or exchange of property. Under this section, no gain or loss is recognized if property held for productive use in a trade-in or business, or for investment, is exchanged solely for property of like kind to be held for such purposes. The parties agreed to cooperate with one another to effectuate such a transaction, including but not limited to, permitting each other to assign their rights under the agreement to a third party who would act as a qualified intermediary and/or an exchange accommodation titleholder with respect to the transaction. XYZ subsequently requested that the transaction be handled in this manner. Tr. p. 6.

XYZ then assigned all of its rights to sell the aircraft to Jones Exchange Corporation, a Qualified Intermediary, with the intention that the transaction be treated as a tax deferred exchange of property rather than an outright sale. Tr. pp. 18-20; Taxpayer’s Ex. No. 5. On August 6, 2002, XYZ and Jones entered into a “Tax Deferred Exchange Agreement” in which Jones agreed to act as intermediary for the exchange of the aircraft at issue in this proceeding and a “new asset,” which would qualify as replacement property under Internal Revenue Code Section 1031(k)-1(a). Taxpayer’s Ex. No. 4. Jones did not take title to XYZ’s Beechcraft King Air B 200. “They would

only hold the funds and they would handle the exchange for XYZ when they [acquired] their new asset.” Tr. p. 7.

Title to the aircraft would be held by “XXX, LLC,” which, as represented at hearing, was acting as an “accommodation titleholder” in accordance with the agreement between XYZ and ABC. The agreement between XYZ and ABC was not admitted into evidence at the hearing. On August 7, 2002, XYZ and XXX entered into an “Aircraft Purchase Agreement” for the purchase of the Beechcraft King Air, B 200. Also on August 7, 2002, XXX entered into an “Aircraft Purchase Agreement” with ABC. The “Aircraft Purchase Agreement” was signed in Anywhere, Iowa at YYY Aviation. YYY Aviation was responsible for the pre-purchase inspection. The escrow agent for the sale was Insured Aircraft Title. ABC conveyed funds to the escrow agent and the title to the plane was deposited by XXX with the escrow agent. Tr. pp. 16-18.

ABC received title to the aircraft on August 8, 2002. A “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” signed August 8, 2002 shows “Seller” as XYZ and “Purchaser” as XXX, LLC. Tr. pp. 22-24; Dept. Ex. No. 3. A corresponding “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” signed August 8, 2002 shows “Seller” as XXX, LLC and “Purchaser” as ABC Services, Inc. Tr. pp. 22-24; Dept. Ex. No. 4. These Bills of Sale of sale were recorded with the Federal Aviation Administration on September 6, 2002.

The Department of Revenue audited the aircraft sale and determined that the sale was a retail sale subject to the application of use tax. The Department issued a Notice of Tax Liability assessing use tax upon ABC for the purchase of the aircraft. ABC paid the use tax and filed a claim for credit. Tr. p. 5. On February 8, 2007, the Department issued an MTC-29, “Notice of Tentative Denial of Claim for Use Tax.” Dept. Ex. No. 1. Section 12 of the UTA (35 ILCS 105/12)

incorporates by reference Section 4 of the Retailers' Occupation Tax Act (35 ILCS 120/1 *et seq.*), which provides that the claim denial issued by the Department is *prima facie* correct and is *prima facie* evidence of the correctness of the amount of tax due. *Id.* at 120/4. Once the Department has established its *prima facie* case by submitting the claim denial into evidence, the burden shifts to the taxpayer to overcome the presumption of validity. Clark Oil & Refining v. Johnson, 154 Ill. App. 3d 773 (1st Dist. 1987).

In order to overcome the presumption of validity attached to the claim denial, the taxpayer must produce competent evidence, identified with its book and records showing that the claim denial is incorrect. Copilevitz v. Department of Revenue, 41 Ill. 2d 154 (1968). Testimony alone is not enough. Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3d 203 (1st Dist. 1991). Documentary proof of tax-exempt status is required to prevail against an assessment of tax by the Department. Sprague v. Johnson, 195 Ill. App. 3d 798 (4th Dist. 1990). On examination of the record in this case, I find that ABC has failed to demonstrate by testimony, through exhibits or through argument, evidence sufficient to overcome the Department's determination that use tax is due on the aircraft purchase.

ABC argues that Illinois use tax did not apply to its purchase of the aircraft because the purchase was an exempt "occasional sale" under Section 2 of the Use Tax Act. 35 ILCS 105/2. "We believe that this should be treated as an occasional sale, looking at the substance and not the form of the transaction because none of – everything that was done by [ABC], I think will allow this to qualify as an occasional sale, not subject to the sales tax provisions of the State of Illinois." Tr. pp. 9-10.

The Use Tax Act, 35 ILCS 105/1 *et seq.* imposes a tax upon the privilege of using in this State tangible personal property purchased at retail from a retailer..." *Id.* at 105/3. "Retailer," as

defined in the UTA, can be either a person or a firm “engaged in the business of making sales at retail” or who “holds out” as being engaged (or who habitually engages) in selling tangible personal property at retail. 35 ILCS 105/2. An exception to the imposition of use tax is provided when the purchase is made from an individual or entity that only engages in isolated or occasional sales of such property. 35 ILCS 105/2. This exception is available when the selling entity does not hold itself out as being engaged or does not habitually engage in selling such tangible personal property at retail. *Id.*

On August 7, 2002, an “Aircraft Purchase Agreement” was executed between XYZ Company (“XYZ”) as Seller and XXX, LLC, as buyer, for a 1994 Beechcraft King Air, B 200, for \$1,644,750. Taxpayer’s Ex. No. 1. On August 7, 2002, an “Aircraft Purchase Agreement” was executed between XXX, LLC and ABC Services for a 1994 Beechcraft King Air B 200, for \$1,644,750. Tr. pp. 14-16; Taxpayer’s Ex. No. 2.

The record clearly establishes that ABC’s acquisition of title to the aircraft was preceded by a transfer of title to the aircraft from XYZ to XXX. A “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” dated August 8, 2002 for a Beechcraft King Air, B 200, shows “Seller” as XYZ and “Purchaser” as XXX, LLC. Tr. pp. 22-24; Dept. Ex. No. 3. A corresponding “U.S. Department of Transportation, Federal Aviation Administration, Aircraft Bill of Sale” dated August 8, 2002 for a Beechcraft King Air, B 200, shows “Seller” as XXX, LLC and “Purchaser” as ABC Services, Inc. Tr. pp. 22-24; Dept. Ex. No. 4.

The seller of the aircraft in this case, XXX, holds itself out as being engaged in selling tangible personal property at retail and is a “retailer” under the definition contained in the UTA. The NUC-1, Illinois Business Registration, for “XXX, LLC” lists its “principal business activity” as “dealer in aircraft.” The business was started in Illinois on March 21, 2002. “Retail” is checked

on the NUC-1 as the “category that best describes your type of business.” Section 2 of the NUC-1, “Sales Tax and Reseller Registration,” Question 1, asks “[D]o you sell any merchandise at retail from a site in Illinois? The response was “yes.” Question 9, asks “[D]o you sell new or used cars, trucks, motorcycles, watercraft, aircraft, trailers, mobile homes or salvage items?” The response was “yes.” Question 13 asks “[W]hen did you (or will you) make your first inventory purchase or taxable sale?” The response was “August 8, 2002.” The NUC-1 is signed by “XXXX,” as President. Tr. p. 11; Dept. Ex. No. 2.

The only person to testify at the evidentiary hearing was Mr. Doe, Vice-President and 100% Shareholder of ABC. No one from XXX testified at the evidentiary hearing. There is no testimony or documentary evidence in the record of this case showing that XXX was not a retailer. The record contains no plausible explanation as to why XXX would file a NUC-1 with the Department holding itself out as being engaged in selling tangible personal property at retail if the company is not engaged in selling tangible personal property at retail.

ABC is asking this tribunal to ignore the NUC-1 and conclude, based on Mr. Doe’s unsubstantiated testimony, that XXX was not a retailer. This testimony was not supported by books and records of XXX. Oral testimony, without corroborating books and records, is insufficient to overcome the Department’s *prima facie* case. Mel-Park Drugs, Inc. v. Department of Revenue, 218 Ill. App. 3d 203 (1st Dist. 1991).

Alternatively, ABC is asking this tribunal to ignore the plain language of the occasional sale exception to the imposition of use tax in the UTA and find that an occasional sale of an aircraft can be made by an entity that holds itself out as being engaged in selling aircraft at retail. A statute which exempts an entity from taxation must be strictly construed in favor of taxation and against exemption. All facts are to be construed and all debatable questions resolved in favor of taxation.

Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455 (2d Dist. 1995). The plain language of the statute clearly shows that the Legislature did not intend to exempt an “occasional” sale of an aircraft made by an entity holding itself out as making or engaged in making sales of aircraft.

Assuming, *arguendo*, that the sale from XXX to ABC could be disregarded and that the transaction in controversy could be treated as a purchase of the aircraft from XYZ, ABC would still not be able to overcome the Department’s *prima facie* case. ABC has presented no documentary evidence showing that XYZ was not engaged in making retail sales of aircraft and was not an aircraft dealer. Counsel for ABC stated in his opening statement that XYZ is an Illinois corporation “not engaged in the business of selling aircraft.” Tr. p. 6. This is all that the record of this case contains on the status of XYZ. Consequently, even if the record supported a conclusion that the transaction at issue could be treated as a sale of the aircraft by XYZ to ABC, ABC would still not overcome the Department’s *prima facie* case.¹

ABC owes use tax unless it meets one of the exemptions provided for in the tax code. ABC has not directed this tribunal to any section of the Illinois tax code or any case precedent for the proposition that Illinois use tax liability should be excused when the transaction qualifies as both a retail sale and a device to obtain federal income tax benefits under Section 1031 of the Internal Revenue Code. An exemption claimant must clearly and convincingly prove entitlement to the exemption claimed. United Air Lines, Inc. v. Johnson, 84 Ill. 2d 446 (1981). ABC has failed to

¹ Counsel for ABC argued during his closing statement that this case is similar to J1 Aviation, Inc. v. Illinois Dept. of Revenue, 335 Ill. App. 3d 905 (1st Dist. 2002), where J1 Aviation contracted with Richland Development Company to acquire Richland’s Gulfstream aircraft through an intermediary, “Nationsbanc,” in a Section 1031 exchange. The court found that Nationsbanc was a “conduit” and that the transaction had to be treated as a non-taxable sale by Richland to J1 Aviation. In the “Aircraft Acquisition Agreement” between J1 and Richland, “Richland made a representation to J1 Aviation that it was a non-retailer, that its sale of the Gulfstream II was an isolated or occasional sale, and that it was not engaged in the business of selling airplanes at retail.” *Id.* at 907. In the instant case, the agreement between XYZ and ABC was not admitted into evidence. The only statement in the record about the status of XYZ as a retailer is ABC’s counsel’s statement that XYZ is not engaged in the business of selling aircraft. Tr. p. 6.

prove, by clear and convincing evidence, that it is entitled to the occasional sale exemption, or any other exemption, and is therefore liable for use tax on the purchase of the Beechcraft King Air, B 200.

WHEREFORE, for the reasons stated above, it is my recommendation that the MTC-29, “Notice of Tentative Denial of Claim for Use Tax,” be finalized as issued.

ENTER:

May 22, 2008

Kenneth J. Galvin
Administrative Law Judge