STATE BOARD OF EQUALIZATION

June 29, 1971

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Attorneys at Law
XXX --- --- ---
--- ---, CA XXXXX

SR -- XX XXXXXX
The G--- Corporation
dba A--- A---
Company

Attention: Mr. D--- R. S---

Gentlemen:

Reference is made to the March 17, 1971 preliminary hearing regarding the July 16, 1970 petition for redetermination filed by your client, The G--- Corporation, dba A--- A--- Company, with respect to tax assessed for the audit period January 1, 1966 to December 31, 1968. As the result of the audit, it was determined that the taxable measures were understated in several respects. At the hearing you questioned the inclusion of a portion of the amount of $92,470 and the inclusion of the amount of $262,476 in the taxable measures, Items C and J of the audit report, respectively. This is to advise you of the conclusions we have reached with respect to these disputed items.

Item C – A--- A--- L--- Convair 440

From the evidence available, in 1967 your client entered into a contract with A--- A--- L--- (AAL) to modify an auxiliary power unit (unit) on an A--- Convair 440 aircraft at its [California 1] facility. Acceptance of the unit by AAL was to occur in [City], Indiana. Concurrently, AAL contracted with P--- A--- C--- (PAC) for the installation of [---], engines on that aircraft at PAC's [California] facility. The aircraft was thereafter delivered to PAC in [California 2] and PAC performed a portion of the engine conversion. The aircraft was then flown from [California 2] to [California 1] for modification of the unit. Upon the completion of that modification, the aircraft was flown from [California 1] back to [California 2] for completion of the engine conversion. On August 20, 1967, the aircraft was flown from [California 2] to [City] where it was delivered by PAC to [---]'s representative. That same date, the aircraft was delivered to and accepted by AAL's representative.

Your client has asserted that the modification of the unit was exempt from tax under the provisions of sales and use tax ruling No. 55 in that the aircraft, with the unit installed, was delivered to AAL outside California pursuant to the contract of sale by its agent. While the aircraft was ultimately received by AAL in [City], upon your client's completion of the modification, the aircraft was initially delivered to/received by PAC at its [California 2] facility. There is no evidence that your client was under a contractual obligation to deliver the aircraft with the unit elsewhere. The March 31, 1967, letter agreement provided only that acceptance of the aircraft by AAL would be outside California. Neither is there any evidence that PAC was your client's agent in receiving the aircraft with the unit from your client at its [California 2] or in delivering the aircraft to [---]'s representative in [City].

Under ruling 55(a)(1)(C), sales tax does not apply to sales of property which is shipped to a point outside the state, pursuant to a contract of sale, by delivery by the retailer to such point by any of several specified means. Ruling 55(a)(2)(B) provides, however, that sales tax applies to sales of property which is sold and delivered to the purchaser or his representative in the state, whether or not the disclosed or undisclosed intention of the purchaser is to transport the property outside the state, and whether or not the property is actually so transported. Thus, where an out-of-state owner of an aircraft engine and mount assembly entered into agreements with an engine overhauler to overhaul the engine and with a mount repairman to repair the mount, the former shipped the engine and mount to the repairman, the repairman removed the engine, the overhauler obtained the engine from the repairman, overhauled it, and returned it to the repairman, and the repairman installed the overhauled engine in the overhauled mount and returned the engine and the mount to the owner, as the repairman took delivery of the overhauled engine as a representative of the owner, the parts used to overhaul the engine were regarded as sold and delivered to the owner's representative here and sales tax applied per ruling 55(a)(2)(B) to sales of repair parts used by the overhauler in overhauling the engine (Cal. Tax Serv. Ann. No. 1521.35 (July 1, 1965).

As your client's relationship to PAC and AAL is comparable to the overhauler's relationship to the repairman and owner in Annotation 1521.35, we have concluded that PAC took delivery of the aircraft with the unit from your client as a representative of AAL and thus, that sales tax similarly applied per ruling 55(a)(2)(B) to your client's sale of the unit to AAL. At the hearing, you advised that the taxable measure was excessive in that your client's charges for installing the unit were improperly included therein. To the extent that such charges are included in the taxable measure, they will be deleted therefrom. Upon deletion of such charges, we will recommend that the remaining tax be redetermined without adjustment.

Item J – M--- Aircraft

In April 1967, your client became the exclusive United States distributor of M--- aircraft. In May 1967, it purchased two M--- aircraft for use as demonstrators, aircraft No. 2 to be based at its [California 1] facility and aircraft No. 7 to be based at its New York facility.

Aircraft No. 2 was flown to [California 1], placed in use there as a demonstrator, and subsequently leased to a Texas company in April 1968. Among others, the following uses of the aircraft were made while the aircraft was in use here as a demonstrator.

> Flights by your client's president: June 1967 (50 minutes), July 1967 (3 hours and 45 minutes), August 1976 (7 hours and 35 minutes); flights by C--- S--- C---'s pilots: August 1967 (38 hours and 9 minutes), September 1967 (36 hours and 58 minutes); flights for your client's business: December 1967 (20 minutes), January 1968 (1 hour and 30 minutes), February 1968 (2 hours and 20 minutes).

Aircraft No. 7 was also flown to [California 1] for installation of avionics. Upon completion of that work, the aircraft was used to fly your client's executives to Phoenix, Arizona and back (September 1967, 3 hours and 32 minutes) and for flights by S--- O--- C---'s executives (September 1967, 2 hours). Thereafter, it was flown to New York, placed in use there as a demonstrator, and subsequently sold. Among others, the following uses of the aircraft were made while the aircraft was in use there as a demonstrator:

> Flights for your client's business: February 1968 (20 minutes), July 1968 (2 hours and 40 minutes).

Your client has asserted that all these uses of these aircraft constituted demonstration uses for purposes of the law, uses not subject to tax thereunder. It has also asserted that aircraft No. 7 was purchased for use as a demonstrator in New York, not California, and thus, that if not all uses of the aircraft constituted demonstration uses for purposes of the law, tax should not apply to aircraft No. 7 because it was not purchased for use as a demonstrator here.

In 1967, Sales and Use Tax Law section 6244 provided that if a purchaser who gave a resale certificate or purchased property for the purpose of reselling it made any storage or use of the property other than retention, demonstration, or display while holding it for sale in the regular course of business, the storage or use was taxable as of the time the property was first stored or used. With respect to aircraft, however, for the reasons set forth within, BTGB 66-6 permitted corporations which were dealers in aircraft purchased for resale to, in lieu of paying tax measured by the purchase price of an aircraft used for purposes other than or in addition to demonstration, elect to pay tax measured by the fair hourly rental value of the aircraft for every hour it was used for any purpose, including demonstration, while being held for resale. As the auditor regarded the above-mentioned uses of aircraft Nos. 2 and 7 as uses for purposes other than demonstration, tax was assessed pursuant to the provisions of BTGB 66-6.

With regard to aircraft No.2, we have concluded that those uses were used for purposes other than or in addition to demonstration, and that tax was properly assessed pursuant to BTGB 66-6. The use of an aircraft to transport executives and other people on one-way trips, such people not being potential purchasers, does not constitute demonstration, and it is a taxable use (Ann. No. 1340.10 (January 12, 1955)). Similarly, the use of an aircraft to transport your client's president, he not being a potential purchaser, did not constitute demonstration, and it was a taxable use. Although the avowed purpose of those flights was to familiarize your client's president with the aircraft, presumably, the aircraft was demonstrated to him or to other of your client's executives prior to April 1967 when your client became the exclusive distributor of M--- Aircraft. As noted, those flights occurred several months after that date.

In addition, the loaning of property to a purchaser who has purchased comparable property and who is awaiting delivery of that property does not constitute demonstration, and it is a taxable use (Ann. No. 1350.30 (letter) (April 25, 1958)). Again, such a person, having already contracted to purchase the property, is not a potential purchaser. Similarly, the loans of the aircraft to C--- S--- C---'s pilots, C--- S--- C--- having already contracted to purchase a M--- aircraft and awaiting delivery of its aircraft, did not constitute demonstration, and they were taxable uses.

Finally, the December, January, and February entries in your client's flight books indicate that the aircraft was used for company business, not demonstration, and those uses would be taxable.

With regard to aircraft No. 7, we have concluded that some of those uses were uses for purposes other than or in addition to demonstration, and that tax was properly assessed pursuant to BTGB 66-6. As noted with respect to aircraft No. 2, the use of an aircraft to transport executives does not constitute demonstration, and it is a taxable use. Again, the aircraft was presumably demonstrated to your client's executives prior to April 1967 when your client became the exclusive distributor of M--- aircraft. Again, the September flight occurred several months after that time. Thus, the use of the aircraft to transport your client's executives to Phoenix, Arizona and back, they not being potential purchasers, did not constitute demonstration, and it was a taxable use. Also, the February and July entries in your client's flight book indicate that the aircraft was used for company business, not demonstration, and those uses would be taxable uses.

Neither do we agree that tax should not apply because the aircraft was not purchased for use as a demonstrator in California. There is no exemption from tax because property is not purchased for use as a demonstrator here. Rather, tax does not apply to property purchased for use as a demonstrator because being purchased under a resale certificate or purchased for the purpose of being resold, the property is purchased for resale, not for storage, use or other consumption in California or elsewhere. Otherwise, it is presumed that property to California by the purchaser is purchased for storage, use or other consumption in California (§6246). As your client purchased the aircraft for the purpose of reselling it, brought it to California, and then used it to transport its executives to Phoenix, Arizona, and back, used it for a purpose other than retention, demonstration or display while holding it for sale in the regular course of business, the use was taxable as of the time the aircraft was first so used (§6244), and tax applied under section 6201 or pursuant to BTGB 66-6.

Under the circumstances, we will recommend that the tax assessed with respect to these aircraft be redetermined without adjustment.

Item J – D--- Aircraft

During the audit period, your client was also a sales agency for D--- aircraft, and it obtained two D--- aircraft for use as demonstrators and for use in company business, aircraft No. 25149 (49) for use at its [California 1] facility, and aircraft No. 25151 (51) for use at its New York facility. Aircraft No. 49 was acquired in August 1967, and was used in California until August 6, 1968 when it was transferred to your client's New York facility. During that time your client paid tax pursuant

to the provisions of BTGB 66-6. Aircraft No. 51 was acquired in September 1967 and was flown to [California 1] for installation of avionics. Upon completion of that work, it was placed in service, was used as a demonstrator (February 14 and 15, 1968), and was used to fly your client's executives to Phoenix, Arizona and San Antonio, Texas and back (February 19, 1968, 6 hours and 25 minutes). On February 22, 1968 aircraft No. 51 was flown to New York and was used there until August 3, 1968 when it was transferred to your client's [California 1] facility. During that time your client did not pay tax pursuant to BTGB 66-6.

In July 1968, Mrs. J--- P--- decided to purchase a D--- aircraft from your client, and she selected aircraft No. 49 because of its interior. As part of the transaction, Mrs. P--- was to lease the aircraft back to your client for use as a par-time demonstrator at its New York facility. For these reasons, the aircraft were, as noted, transferred in August 1968. Thereafter, aircraft No. 49 was used for demonstration at the New York facility until October 1968. On October 5, 1968, it was flown to Texas for display at a convention, on October 8 it was used for demonstration in Texas, and on October 9 it was flown to [California 1] for maintenance. Upon completion of the maintenance, it was flown to New York where the sale to Mrs. P--- was completed on October 14, 1968. During that time your client did not pay tax pursuant to BTGB 66-6. Aircraft No. 51 was used for demonstration and for company business at the [California 1] Facility. Your client paid tax pursuant to BTGB 66-6 until November 1968 when section 6244 was amended.

Your client has asserted that tax should not apply to uses of these aircraft during the time they were based at its New York facility. It has also been asserted that aircraft No. 51 was purchased for use as a demonstrator in New York, not California, and thus, that tax should not apply to aircraft No. 51 because it was not purchased for use as a demonstrator here. In this regard, it was pointed out that aircraft No. 51 was transferred to [California 1] only because Mrs. P--- decided to purchase aircraft No. 49.

Reference to the election provided by BTGB 66-6 has previously been made in connection with the M--- aircraft. By letters dated January 18, 1967 and April 26, 1968, we advised your client of the manner in which BTGB 66-6 was being applied, and in the latter, we advised that use specified therein would be subject to tax at the fair hourly rental value regardless of the location of the use. Thus, tax was assessed pursuant to BTGB 66-6 and those letters on the hourly rental value of the uses of these aircraft during the time they were based at the New York facility.

With regard to aircraft No. 49, we have concluded that tax was properly assessed pursuant to BTGB 66-6 up to October 14, 1968. At that time, the aircraft was first used in California for other than retention, demonstration or display, the use was taxable as of that time, the tax being measured by the purchase price of the aircraft. In lieu of paying tax measured by the purchase price of the aircraft, your client elected to ay tax pursuant to BTGB 66-6, to pay tax measured by the fair hourly rental value for every hour the aircraft was used for any purpose while being held for resale. As noted, BTGB 66-6 provided corporations which were dealers in aircraft an alternative to the usual taxable measure, the purchase price of the aircraft. Where a corporation elects to use that alternative, tax is measured as set forth therein, regardless of where the aircraft is based.

At the hearing it was agreed that tax was improperly assessed pursuant to BTGB 66-6 on and after October 14, 1968.

With regard to aircraft No. 51, we have concluded that tax was properly assessed pursuant to BTGB 66-6 from February to August 3, 1968. On February 19, 1968, when the aircraft was first used in California for other than retention, demonstration or display, the use was taxable as of that date, the tax being measured by the purchase price of the aircraft. Again, in lieu of paying that tax, your client elected to pay tax pursuant to BTGB 66-6. Again, where a corporation so elects, tax is measured as set forth therein, regardless of where the aircraft is based.

Again, we do not agree that tax should not apply because the aircraft were not purchased for use as a demonstrator in California. As in the case of M--- aircraft No. 7, your client purchased the aircraft for the purpose of reselling it, brought it to California, and then used it to transport its executives to Phoenix, Arizona and San Antonio, Texas and back, used it for a purpose other than retention, demonstration or display while holding it for sale in the regular course of business, and that use was taxable as of the time the aircraft was first so used (§6244). Tax applied under section 6201 or pursuant to BTGB 66-6.

Under the circumstances, we will recommend that tax assessed pursuant to BTGB 66-6 on and after October 14, 1968 (aircraft No. 49) be deleted from the taxable measure and that the remaining tax assessed with respect to these aircraft be redetermined without adjustment.

In conclusion, our recommendations to the board will be as hereinabove set forth. If we do not hear from you within 30 days from the date of this letter, we shall assume that you concur in our recommendations, and we shall present the matter to the board for final action. In this event, you will receive official notice of the board's action in due course. In the event that you do not concur with our recommendations and you desire an oral hearing before the board, please notify Mr. J. L. Martin, P. O. Box 1799, Sacramento, CA 95808, of this fact within the 30-day period and he will inform you of the time and place of hearing.

Very truly yours,

J. Kenneth McManigal
Tax Counsel

JKM:smb