

**BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO**

In the Matter of the Protest of )  
[Redacted], ) DOCKET NO. 23798  
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 )  
Petitioners. ) DECISION  
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\_\_\_\_\_ )

On December 16, 2010, the staff of the Tax Discovery Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (Notice) to [Redacted] (taxpayers) asserting sales tax, use tax, penalty, and interest for taxable period July 1, 2004, through June 30, 2010, in the total amount of \$14,148. In a letter received by the Commission on February 15, 2011, the taxpayers filed a timely appeal and petition for redetermination. At the taxpayers' request the Commission held an informal hearing on June 6, 2011. The Commission, having reviewed the file, information provided at the hearing, and documents received thereafter, hereby modifies the audit findings for reasons explained below. Additionally, this decision withdraws the liability held against [Redacted] for the reasons explained.

Introduction

The taxpayers are a married couple who owned a corporation called [Redacted]. [Redacted] was a [Redacted] training school in Idaho permitted to collect sales tax from July 1990 to June 2010, at which time the corporation was dissolved. The deficiency noted previously arises from a change in an individually owned [Redacted] from a tax-exempt to a non-exempt purpose. It also arises from the lease of an individually owned [Redacted] to the corporation. The liability was imposed against the individuals and not against the company.

[Redacted] owned a [Redacted] and [Redacted] owned [Redacted]. Both were registered with the [Redacted] in their personal names and were separately leased by them under their individual names to the corporation, [Redacted]. The auditor concluded that the cessation of the lease between [Redacted] and the corporation triggered taxable use of the [Redacted] by [Redacted]. The auditor also concluded the transactions between [Redacted] and the corporation to be taxable leases. The aircraft was leased “bare,” meaning that [Redacted] services were not provided. [Redacted] did not have a seller’s permit and did not collect sales tax from the corporation on the lease values. Both of the auditor’s findings are discussed in this Decision.

#### Applicable Tax Code

Idaho imposes a sales tax on the rental or lease of tangible personal property, among other transactions (Idaho Code § 63-3612(2)(h)). A lessor is a retailer required to collect sales tax from the purchaser, in this case the lessee (Idaho Code §§ 63-3610 and 63-3619) unless an exemption applies to the lease or rental transactions. The purchase of [Redacted], or any other tangible personal property which is intended to be sold or held for the purpose of lease or rental, can be purchased exempt from tax under a tax code provision commonly referred to as a resale exemption (Idaho Code § 63-3609). If tangible personal property no longer qualifies for the exemption for which it was purchased, use tax is due.

Use tax is a complementary tax to sales tax and is applicable only if sales tax has not been paid to a retailer and no exemption from tax applies. Payment of use tax extinguishes the sales tax obligation (Idaho Code § 63-3621). Collection of unpaid sales and use tax by the State of Idaho from a retailer is barred when a retailer files sales and use tax returns and the transactions at issue occurred more than three years from the time the returns were filed. For

those who operate without a permit and do not file returns, the statutory period is seven years (Idaho Code § 63-3633(a)).

[Redacted]

According to the auditor, [Redacted] purchased a [Redacted] exempt from tax in 1991 and leased it to [Redacted] from 1991 through 1996. From 1997 through 2007, the [Redacted] was used out-of-state by a company named [Redacted], after which it was returned to [Redacted] in Idaho and was no longer held by him for tax-exempt rental or lease purposes.

When the [Redacted] was returned to Idaho in 2008 for no purpose other than personal use, the auditor believed that this was a change from a non-taxable to taxable use and that use tax was due on its fair market value. However, [Redacted] indicates that the auditor is in error regarding the precise termination date of the [Redacted] lease between himself and [Redacted]. He states that there was a break in the lease period and asserts, on that basis, tax was due in 1996 or 1997, and that the seven-year statutory period for collecting tax has long expired. There is no lease termination document in evidence, but a copy of the 1991 lease states that it is in effect month-to-month until terminated by either party with a 30-day notice.

Further, [Redacted] disputes the auditor's contention that there was an unbroken timeline between the multi-year year lease period and the transfer of the [Redacted] to [Redacted]. He states there was a year's time lag between [Redacted] lease end date and the transfer of the aircraft to [Redacted].

The Commission concludes, for the purpose of this Decision, that it cannot refute [Redacted] claim and that it is unreasonable to presume that he would have a record of events from approximately 15 years ago, although some records from that time exist. If [Redacted] owed tax on the [Redacted] in 1996 or 1997, that tax period is now beyond the statutory date for

assessment, and his use in 2008 cannot be subject to tax. For this reason, the Commission hereby withdraws the liability against [Redacted].

[Redacted]

According to the auditor, [Redacted] purchased a [Redacted] tax exempt in 2000 and leased it to [Redacted] from July of that year to June 2010, specifying lease charges of \$35/[Redacted] hour. A total of 1,585 hours were logged, averaging 264 hours per year. She did not collect tax on the lease charges, nor did she have a seller's permit to do so. Further, the auditor did not believe that \$35/[Redacted] hour represented the fair market value of an arm's length transaction between [Redacted] and a company that she and her husband owned. The auditor substituted a higher figure based on local research and the taxpayers dispute the higher amount.

The Commission believes that the taxpayers' suggested figure is reasonable. While the higher rate suggested by the auditor may be an appropriate rate for a bare rental to a final customer, the liability at issue is for a rental between the taxpayer (owner) and a user ([Redacted]) who will [Redacted] for profit. [Redacted] would necessarily set its charges to students beyond its lease costs in order to make a profit (i.e., it would charge students enough to cover its lease costs, the instructors' fees, overhead, and profit). Therefore, for the purpose of this Decision, the Commission will accept the taxpayers' \$35/[Redacted] hour figure.

Confounding the dispute over hourly rates subject to tax is [Redacted] collection of tax from student pilots. [Redacted] contends that [Redacted] collected sales tax from [Redacted] and, therefore, she did not need to charge a tax for the lease to [Redacted].

The Commission's position, however, is that there is no exemption available for the sale, purchase, or lease of aircraft to provide [Redacted] instruction (Idaho Code § 63-3622GG). Further, [Redacted] do not rent [Redacted], and the fees charged for [Redacted] instruction are

not subject to tax. Rather, in general and in this specific case, [Redacted] is providing instruction, which is a non-taxable service, and its use of [Redacted] to provide that service is taxable to them, not to the students.

[Redacted] was obligated to collect tax from [Redacted] for the aircraft lease on the hourly charges:

**07.** Flying Instructions. Flying instructions or lessons which may include solo flights are a service and the fees are not subject to sales tax.

**a.** Aircraft purchased, rented, or leased to be used primarily for flying instruction are subject to sales or use tax. (IDAPA 35.01.02.07.)

Nevertheless, the taxpayers believe the Commission should offset the amounts [Redacted] collected from students against the amount asserted in the Notice. Since the tax amounts collected and remitted were in error because they were not due from students, the Commission refuses to allow an offset. Students who paid tax in error over the past three years could seek and obtain a refund. Additionally, the liability is against [Redacted] and not against [Redacted], the collector of the tax. No offset is permissible.

The taxpayers question why a tax can be imposed on the lease of the aircraft without the ability to recover it in taxable charges [Redacted] made to its students. The Commission replies that there is no statutory requirement that the framework of the Sales Tax Act behave in such a fashion. Further, there is no recompense for sales tax owed in the scenario posed by the taxpayers, as sales tax collected from customers is the property of the state, not the seller. Finally, tangible personal property used by a business in performing a nontaxable service is subject to sales or use tax (IDAPA 35.01.02.06).

Other issues were raised by the taxpayers but are moot due to the decision to withdraw from the liability the amount asserted against [Redacted].

THEREFORE, the Notice of Deficiency Determination dated December 16, 2010, is MODIFIED and, as MODIFIED, is AFFIRMED and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that taxpayers pay the following tax, penalty, and interest:

<u>PERIOD</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
7/1/2004 through 6/30/2010	\$3,210	\$803	\$652	<u>\$4,665</u>
			Less Payment	(\$ 500)
			TOTAL DUE	<u>\$4,165</u>

Interest is calculated through January 31, 2012.

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the taxpayers' right to appeal this decision is enclosed.

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2011.

IDAHO STATE TAX COMMISSION

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COMMISSIONER

**CERTIFICATE OF SERVICE**

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_ 2011, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[Redacted]

Receipt No.

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