

OHIO BOARD OF TAX APPEALS

A.M. & J.B., Inc.,)	
)	
Appellant,)	CASE NO. 99-T-1387
)	
vs.)	(USE TAX)
)	
Thomas M. Zaino, Tax)	DECISION AND ORDER
Commissioner of Ohio,)	
)	2002-Ohio-7225
Appellee.)	Affirmed on Appeal Dec. 26, 2002

APPEARANCES: Appeal Filed Jan. 11, 2002 Cuyahoga Cty. Court of Appeals

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ENTERED: December 14, 2001

Mr. Johnson, Ms. Jackson, and Ms. Margulies concur.

The Board of Tax Appeals considers this matter pursuant to a notice of appeal filed by A.M. & J.B., Inc. A.M. & J.B. appeals from a final determination of the Tax Commissioner, in which the Commissioner affirmed, with modification, a use tax assessment previously issued against A.M. & J.B. as a result of a purchase audit conducted for the period of July 1993 through June 1996. The assessment, as conditionally modified, is in the amount of \$848,111.72, including tax, penalty, and

interest. Our consideration of this matter includes a review of the statutory transcript certified to this Board by the Commissioner pursuant to R.C. 5717.02 and the briefs filed by the parties. Both parties waived their opportunity to present additional evidence at a hearing before this Board.

The assessment is based upon a single transaction, A.M. & J.B.'s purchase of a "Gates Lear Jet 60" in December 1993. The airplane is the only asset owned by A.M. & J.B. Before the Commissioner, A.M. & J.B. represented that it acquired the aircraft with the intent to lease the plane to another entity, known as Corporate Wings, Inc. ("CWI") CWI, in turn, was to provide charter services to the shareholders of A.M. & J.B. and related corporations, as well as to others. Consequently, A.M. & J.B. paid no tax on the purchase of the Lear Jet, claiming that the airplane was excepted from sales and use tax because it was purchased for resale.

In support of its assertion, A.M. & J.B. submitted copies of two documents. The first is a "Charter Lease Agreement" (S.T. 13-16.) The lease became effective on January 1, 1994, and provides that CWI agreed to lease the Lear Jet from A.M. & J.B. for a period of twelve months, with automatic renewals of six-month terms. The lease provides that CWI is to pay to A.M. & J.B. a monthly rental of \$14,266.60. In addition, CWI is to pay A.M. & J.B. \$1,016.50 for each hour A.M. & J.B. uses the aircraft, \$1,712 for each hour the airplane is chartered by a member of the general public, and \$1,899.28 for each hour the jet is chartered by the Invacare Corporation.¹

¹ The record suggests that A.M. & J.B.'s shareholders have an ownership and managerial interest in Invacare.

Under the lease, CWI is responsible for all billing and collection. CWI is charged with maintaining the airplane. However, A.M. & J.B. is “solely responsible for all cost and expense associated with performance of maintenance of the Aircraft.” (S.T. 14.) In addition, maintenance can only be performed under the supervision of a crew chief “selected” by A.M. & J.B. Finally, A.M. & J.B. “or its representative shall have the right to approve or disapprove any charter of the aircraft.” (S.T. 15.)

Contemporaneous with the lease agreement, CWI and A.M. & J.B. entered into an “Aircraft Management & Operation Agreement.” (S.T. 19-29.) The management agreement, which by its terms “supersedes any and all other agreements” made between CWI and A.M. & J.B., provides that flight operations of the Lear Jet shall be under the exclusive control of CWI, which shall supply crew members for the aircraft. However, the agreement also provides that all crew members, including the crew chief, must be approved by A.M. & J.B. The agreement further provides that A.M. & J.B. shall be responsible for all costs pertaining to the operation of the aircraft. A review of the agreement and of invoices submitted by A.M. & J.B. indicates that such costs include: crew fees, management fees, marketing fees, hanger rental, insurance, crew training, flightcrew service, crew lodging, crew per-diem, crew transportation, and supplies, in addition to the maintenance fees. While A.M. & J.B. is responsible for these costs, the agreement provides that A.M. & J.B. will have all invoices sent to CWI for payment. Credit is to be given to CWI for such costs. While CWI is responsible for obtaining storage for the airplane at A.M. & J.B.’s expense, A.M. & J.B. retains the right to direct CWI to “reposition the aircraft at a location of [A.M. & J.B.’s] choice.” (S.T. 22.) The

agreement provides that A.M. & J.B. has the right to use the aircraft when crewed by CWI's employees. Risk of loss remains with A.M. & J.B., who is responsible for payment of the insurance. Finally, the management agreement provides that CWI is "authorized to act as agent for [A.M. & J.B.] for the limited purpose of performing those services" provided for in the management agreement. (S.T. 25.)

Upon review of the lease and management agreements, the Commissioner concluded that the arrangement between A.M. & J.B. and CWI does not constitute a true lease, and, therefore, the purchase of the airplane was not subject to an exception from sales and use tax:

"Although the petitioner attempts to characterize its agreement with CWI as a lease, such contention is not well taken. In reality, the agreement provides that the petitioner allows CWI to use its plane, and that the petitioner pays CWI to provide a management service to the petitioner. In addition to providing a management service, CWI provides charter services to third parties, and credits the petitioner a portion of the monies CWI receives when it charts the aircraft for any third party. In so doing, CWI acts on behalf of the petitioner by sharing with the petitioner a portion of the profit CWI makes when using the petitioner's aircraft in rendering charter services to third parties. The petitioner contends that 'this credit is the rental consideration received by (the petitioner).' The arrangement, however, is merely an allocation of charter revenue between the parties in an attempt to characterize the relationship between the parties as a lease.

"Additionally, certain other elements of the agreement indicate that it is not a true lease. The petitioner pays the operating expenses of CWI, and retains the right to approve or disapprove any charter to a third party. Furthermore, the petitioner received the management service at a discounted rate in comparison to the rates charged to the third parties. These factors are not elements of a true lease. The relationship between the petitioner and CWI demonstrates that the agreement is not a lease between the parties, and

therefore, the purchase of the aircraft is not eligible for the resale exception ***.

“The [agency clause in the management agreement], even with its restrictive language, indicates that the intent of the agreement is that CWI act as the petitioner’s agent by generating revenue for the petitioner.” (S.T. 1-4).

In its notice of appeal, A.M. & J.B. specifies that the Commissioner erred in not recognizing that the agreement between A.M. & J.B. and CWI constituted a lease. A.M. & J.B. asserts that it had as its intent the resale of the Lear Jet by lease.² The Commissioner responds that both agreements, taken together, support his determination.

In reviewing A.M. & J.B.’s specifications of error, we observe that the findings of the Tax Commissioner are presumptively valid. *Alcan Aluminum Corp. v. Limbach* (1989), 42 Ohio St.3d 121. Consequently, it is incumbent upon a taxpayer challenging a determination of the Commissioner to rebut the presumption and to establish by competent and probative evidence a clear right to the requested relief. *Belgrade Gardens v. Kosydar* (1974), 38 Ohio St.2d 135; *Midwest Transfer Co. v. Porterfield* (1968), 13 Ohio St.2d 138. In this regard, the taxpayer is assigned the burden of showing in what manner and to what extent the Commissioner’s determination is in error. *Federated Dept. Stores, Inc. v. Lindley* (1983), 5 Ohio St.3d 213. Additionally, all sales of tangible personal property within Ohio are presumed to be subject to tax until shown otherwise. We emphasize that exceptions and exemptions to taxation are to be

² A.M. & J.B. also specifies that the Commissioner’s determination results in a denial of equal protection of the laws under both the U.S. Constitution and the Ohio Constitution. However, as A.M. & J.B. did not brief this issue, we consider it to have been withdrawn. *Riss & Co. v. Bowers* (1961), 114 Ohio App. 429; *State ex rel. Brooks v. Trans World Airlines, Inc.* (1990), 53 Ohio St.3d 713; *Unacapher v. Baltimore & Ohio Rd. Co.* (1933), 127 Ohio St. 351.

strictly construed in favor of taxation, and the burden rests with the taxpayer to affirmatively establish its right thereto. *National Tube Co. v. Glander* (1945), 157 Ohio St. 407. See, also, *Frankelite Co. v. Lindley* (1986), 28 Ohio St.3d 29.

A.M. & J.B.'s specifications of error relate to the assessment of use tax. R.C. 5739.02 levies a sales tax upon all retail sales made in Ohio. A similar use tax is imposed by R.C. 5741.02. If a transaction is not subject to sales tax, it follows that the transaction, if made within Ohio, is also not subject to use tax. R.C. 5741.02(C). Since our analysis of the relevant sales and use tax provisions is essentially identical in the context of this appeal, we shall refer only to the applicable sales tax provisions, unless circumstances require otherwise.

A.M. & J.B. asserts its purchase of the aircraft is excepted from use tax under 5739.01(E):

“(E) ‘Retail sale’ and ‘sales at retail’ include all sales except those in which the purpose of the consumer is:

“(1) To resell the thing transferred or benefit of the service provided, by a person engaging in business, in the form in which the same is received by the person[.]”

We must determine whether this transaction is a sale under R.C. 5739.01(B), which provides that “sale” and “selling” include “all transactions by which title or possession, or both, of tangible personal property, is or is to be transferred, or a license to use or consume tangible personal property is or is to be granted.” R.C. 5739.01(B)(1). In *Fliteways v. Lindley* (1981), 65 Ohio St.2d 21, the Supreme Court considered a situation in which the taxpayer furnished airplanes, fuel, and pilots in its charter service.

This service would transport passengers and freight to various destinations. Some of the planes were also used in a flying school run by the taxpayers. While the taxpayer argued that its leasing of airplanes and purchases of fuel were excepted under the resale exception, the Court concluded that the exception was not available because the transactions did not constitute “sales.” Instead, the Court found that the taxpayer employed the airplanes and fuel in rendering personal services and did not resell them. The Court, however, did find that some of Fliteways’ purchases of airplanes were excepted where Fliteways had purchased the aircraft with the intent to ultimately resell them. Fliteways used these planes in its charter service but held them out for sale at all times. The Court determined that Fliteways’ use of those planes in its charter service until sale did not refute its intent to resell.

Recently, in *Laurel Transp., Inc. v. Zaino* (2001), 92 Ohio St.3d 220, the Court considered a situation very similar to the one before us. *Laurel* concerned a management agreement entered into by an airplane owner and CWI, the same company now before us. There, CWI provided management services, pilots, and crew services. CWI was to operate the aircraft. Laurel paid for insurance, and charged for the use of the aircraft, which was used by the shareholders of Laurel and a related company. We originally determined that Laurel leased the airplane to its users and thus granted the resell exception under R.C. 5739.01(E)(1). The Court reversed this Board’s determination, finding that no “sale” occurred:

“Laurel contends that its purchases should be excepted as sales for resale because it resells the aircraft, fuel, and maintenance by transferring possession to its customers. Here, Laurel's witness, Richard Horvitz, a vice- president and

customer of Laurel, testified that as a user of the aircraft, he could request the services of certain of Wings's pilots to the extent feasible with scheduling; subject to the pilot's control of safety, Horvitz made the decisions on where to go and when to leave. Horvitz further stated that the user could use his or her own pilot if the pilot was certified for the Citation III, had adequate experience, and was deemed worthy of Laurel's trust. However, no customer requested use of his or her own pilot, and using such a pilot would not have reduced the hourly fee.

“We find essentially no difference between this case and *Fliteways*. Here, and in *Fliteways*, the owners furnished an aircraft, fuel, and pilot to users for an hourly fee, albeit through contractual agreements with others. Laurel distinguishes *Fliteways* from this case because Laurel contracted with Wings to maintain the aircraft and to furnish fuel and pilots. We do not agree that this is a defining difference. Laurel chose the third party to furnish the pilots. While the users could determine when and where they wanted to travel, Laurel provided the transportation service that took them. Laurel controlled the aircraft by contracting with Wings to fly the aircraft.” *Id.* at 222.

Also germane is *Executive Express, Inc. v. Tracy* (Nov. 5, 1993), BTA No. 92-P-880, unreported. There, Executive Express purchased an airplane and entered into an agreement with a management company, which was to provide the airplane to Executive's charters. Executive Express argued that it leased the plane to the management company in that the company had control of the airplane. The Tax Commissioner disagreed and determined that Executive Express was providing charter services, in that there had been no transfer of title or possession. On appeal, we affirmed, finding that the Commissioner could find a charter service based upon the record before him. We reach the same conclusion here.

The management agreement between A.M. & J.B. and CWI indicates that A.M. & J.B. maintained control over the Lear Jet. A.M. & J.B. had final approval of the crew, the crew chief, and the pilots. A.M. & J.B. could disapprove any charter at its own discretion. A.M. & J.B. was responsible for all expenses, including crew costs, insurance, and hanger rental. A.M. & J.B. even controlled where the aircraft could be based. In addition, the management agreement clearly makes CWI an agent for A.M. & J.B. Finally, nearly all of the charters were for the use of A.M. & J.B.'s shareholders and for Invacare, the related corporation.

Based upon the forgoing, we find that there was sufficient evidence upon which the Commissioner could base a conclusion that the true intent of A.M. & J.B. was not to lease the airplane to CWI, despite the use of the term in the one agreement, but to operate a charter service. Such is not a "sale" within the meaning of R.C. 5739.01(B)(1) and 5739.01(E)(1). *Laurel, supra*. While A.M. & J.B. has argued that it had intended to resell the jet in much the same way as the taxpayer in *Fliteways*, and should be granted the exception despite the airplane's use, we do not find that *Fliteways* lends support to A.M. & J.B.'s position. In *Fliteways*, the taxpayer used its planes in its charter service while still holding the aircraft out for sale. While the chartering of the planes did not constitute a "sale" under R.C. 5739.01(B), the ongoing intent to ultimately resell the airplanes was established by the evidence. Unlike the situation in *Fliteways*, the record here does not evidence the intent to resell the plane. The record before us describes a charter service, which does not constitute a "sale."

In reaching this conclusion, we observe that the contentions raised by A.M. & J.B. involve a mixture of law and fact. The burden rests with A.M. & J.B. to demonstrate that the Commissioner's determination regarding the plane and A.M. & J.B.'s relationship with CWI was in error. *Alcan* and *Executive Express, supra*. The Commissioner had the opportunity to review the facts presented by A.M. & J.B. and determined that the purchase of the aircraft was a taxable transaction. Despite being offered a hearing to present evidence concerning the agreements and the use of the Lear Jet, A.M. & J.B. chose to waive its opportunity to present additional facts for our consideration. Upon review of the record now before us, we can find nothing that gives support to A.M. & J.B.'s specifications of error. Having declined its opportunity to further develop the factual record in this matter, we must conclude that A.M. & J.B. has failed to prove by competent and probative evidence that the final determination of the Tax Commissioner is in error. *Executive Express, supra*.

Based upon all of the foregoing, we conclude that the Commissioner's determination is supported by a preponderance of the evidence and is in accordance with law. Accordingly, the Board of Tax Appeals orders that the Tax Commissioner's final determination must be, and the same hereby is, affirmed.

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