

Whether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. See 2 Ill. Adm. Code 1200.110(a)(4). (This is a GIL.)

September 3, 2008

Dear Xxxxx:

This letter is in response to your letter dated May 10, 2007, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

This Request for a Private Letter Ruling (the 'Request') relating to Illinois Retailers' Occupation Tax and Illinois Use Tax is submitted pursuant to 2 Ill. Adm. Code 1200.110 on behalf of our client, CLIENT a STATE limited liability company (hereinafter referred to as the 'Owner') with offices located at ADDRESS, Illinois. Attached hereto is an executed form IL-2848 appointing the undersigned and this law firm to represent Owner in connection with this Request.

STATEMENT OF MATERIAL FACTS

On April 23, 2007 Owner purchased a newly manufactured aircraft (the 'Aircraft'). Owner took delivery of the Aircraft from the manufacturer in CITY/STATE. Promptly following Owner's receipt of the aircraft, it was flown to CITY, Illinois. During Owner's ownership of the Aircraft, Owner anticipates that the Aircraft will be hangared and maintained primarily at Airport.

In conjunction with Owner's acquisition of the Aircraft and prior to the Aircraft's entry into Illinois, Owner simultaneously dry leased the Aircraft to two separate entities. In one of these leases, Owner dry leased the Aircraft (the 'Charter Lease') to ABC, an Illinois corporation (the 'Charter Lessee'), which is an interstate carrier that holds a certificate issued by the Federal Aviation Administration ('FAA') under Part 119 of the Federal

Aviation Regulations (the 'FAR') authorizing it to conduct charter operations pursuant to FAR Part 135. The Charter Lease has a term of twelve months and was effective as of the date and time of Owner's acquisition of the Aircraft. The Charter Lease is a 'triple net lease' such that Charter Lessee and any other lessees of the Aircraft, are, in the aggregate, responsible for all Aircraft operating costs.

Charter Lessee is currently in the process of adding the Aircraft to Charter Lessee's FAA Operating Certificate and will have this process completed as promptly as possible. Thereafter, Charter Lessee will use the Aircraft as rolling stock to transport persons and property for hire in interstate commerce under Part 135 of the FAR. In connection therewith, Charter Lessee will offer the use of the Aircraft in charter to Charter Lessee's customers, which will include individuals and entities affiliated with Owner. Charter Lessee's customers will pay Charter Lessee for their use of the Aircraft at rates as determined by Charter Lessee. In turn, Charter Lessee will pay Owner, monthly in arrears, rent under the Charter Lease based on the number of hours that Charter Lessee uses the Aircraft. The amount to be paid to Owner by Charter Lessee under the Charter Lease is set at a fair market value rate.

Charter Lessee has the right to terminate the Charter Lease for cause (as defined in the Charter Lease) prior to the end of its term. However, if this were to occur, the Aircraft would either be removed from Illinois prior to any such termination or a new lease with a new charter lessee (that is an interstate carrier that holds a Part 119 certificate) would be entered into prior to or concurrent with the Charter Lease termination and would contain substantially the same terms as those of the Charter Lease described above.

In addition to the Charter Lease, Owner dry leased the Aircraft (the 'Private Lease') to an entity that is related to Owner through common ownership (the 'Private Lessee'). Private Lessee operates the Aircraft under the Private Lease pursuant to FAR Part 91 and pays Owner, in advance, monthly rent for Private Lessee's use of the Aircraft. As with the Charter Lease, the Private Lease is a 'triple net lease' such that Private Lessee is responsible (together with any other lessees of the Aircraft) for all Aircraft operating costs. Furthermore, the rent charged to Private Lessee under the Charter Lease is a fair market value rate based on the amount of Private Lessee's use thereof.

Owner anticipates that Charter Lessee will utilize the Aircraft for interstate charter flights for a total of 25% of the Aircraft's total hours flown during any particular twelve-month period. Owner also anticipates that Private Lessee will use the remaining 75% of the Aircraft's hours flown during such annual period. Charter Lessee may charge slightly differing rates to its customers provided, however, that in no event shall the lowest fare be lower than 80% of the highest charter rate charged by Charter Lessee for the Aircraft. Furthermore, during the Charter Lease term Charter Lessee shall charter the Aircraft solely or predominantly to entities or individuals that are related through common ownership to the Owner.

No later than 30 days after April 23, 2007 (the date the Aircraft was first brought into Illinois) Owner timely filed with the Illinois Department of Revenue (the 'Department') a completed Form RUT-25 (Use Tax Transaction Return) together with a completed Form RUT-7, Rolling Stock Certification.

TAX PERIOD AT ISSUE/REQUIRED STATEMENTS

The tax period at issue is the current calendar year, 2007, in which Owner purchased the Aircraft, and any subsequent tax period(s) during which Owner owns the Aircraft. No audit or litigation is pending with the Department of Revenue relating to Owner. To the best knowledge of Owner and this firm, the Department of Revenue has not previously ruled on the same or a similar issue for Owner or any predecessor of Owner and Owner has not previously submitted the same or a similar issue to the Department of Revenue.

STATEMENT OF AUTHORITIES AND ANALYSIS

Illinois has a sales tax, referred to as the Retailers' Occupation Tax ('ROT'), which is levied on receipts from the sale of tangible personal property within Illinois, and a complementary Use Tax ('UT'), which is levied on the use of tangible personal property in Illinois.¹ *Ill. Rev. Stat., ch. 35, par. 120/2, 120/2-10; Ill. Rev. Stat., ch. 35, par. 105/3, 105/3-10*. While the ultimate rate of tax varies according to the local jurisdiction, the statewide minimum is 6.25% of the purchase price paid for the property.

Illinois law also contains certain exemptions from the ROT and UT. One of these exemptions is referred to as the Rolling Stock Exemption ('RSE'). The RSE normally applies to sales of rolling stock, such as an aircraft, to an interstate carrier for use in transporting persons or property for hire in interstate commerce. *Ill. Rev. Stat., ch. 35, par. 105/3-55(b); 86 Ill. Admin. Code § 130.120(1); 86 Ill. Admin. Code § 130.340; 86 Ill. Admin. Code § 150.310*.

In addition, the purchase of an aircraft for lease by the purchaser thereof to an interstate carrier for use in interstate commerce is similarly exempt under the RSE from the ROT and UT, provided certain procedures are followed. For the RSE to apply to Owner's purchase of the Aircraft and subsequent lease thereof to Charter Lessee, (1) the Charter Lease must have a term of at least one year, (2) Charter Lessee must be an interstate carrier and intend to use the Aircraft for hire, and (3) Charter Lessee must use the Aircraft in interstate commerce for hire on a 'regular and frequent' basis. *National School Bus Service, Inc. v. Department of Revenue*, 302 Ill. App. 3rd 820 (1st Dist. 1998).

There is no clear guidance under Illinois law or regulations on the percentage of charter use that is necessary for 'regular and frequent' use of an aircraft in interstate commerce. In *Department of Revenue v. ABC, LLC d/b/a XYZ, Inc.*, Ill. Admin. Hearing Decision UT 06-4 (April 11, 2006), the Department reviewed a taxpayer protest of a Notice of Tax Liability and decided that the taxpayer's aircraft was exempt from use tax on the basis that it was being used as rolling stock in interstate commerce for hire. The taxpayer's aircraft, a 1981 Beechcraft King Air B200, as purchased on September 22, 2000. After repairing the aircraft's exterior, refurbishment of the interior and an engine overhaul, the taxpayer entered into an Aircraft Lease Agreement with COMPANY for the purpose of operating the aircraft in charter service.

In April 2002, the Department began an audit concerning the purchase of the aircraft from the date of purchase through March 31, 2002. During the audit period, the taxpayer produced evidence that the charter operator was a carrier-for-hire and that the

¹ Illinois also levies an Aircraft Use Tax ('AUT') on the use of aircraft within the state when such aircraft is purchased in a transaction qualifying as a casual or occasional sale. *35 ILCS 157/10-15*. In this instance, however, because the Aircraft was purchased from its manufacturer, the AUT does not apply. Instead, because the purchase transaction occurred outside Illinois and Private Lessee flew the Aircraft to Illinois pursuant to the Private Lease, the terms of the UT apply to this transaction.

taxpayer's purchase of the aircraft was therefore exempt from the UT under the RSE. From June 28, 2001 to March 31, 2002, the aircraft was chartered for twenty-five interstate flights, totaling 96.8 hours. The aircraft was also used for a significant number of intrastate charter flights during that time.

The Department affirmed in its ruling that the term 'rolling stock' includes aircraft. The Department further reaffirmed the three-prong test described above used to determine whether an aircraft qualifies for the RSE:

If the taxpayer is a lessor...the taxpayer must establish that (1) the aircraft is under a lease of one year or longer; (2) the aircraft was used by an interstate carrier for hire and (3) the aircraft in question moved in interstate commerce.

Id. In clarifying the third prong of this test, the Department declared that the aircraft's 'interstate use [must have been] regular and frequent or more than merely incidental.'
Id.

Applying the law to the facts of that case, the Department ruled that the payer leased the aircraft to an interstate carrier for hire and that the aircraft 'moved in interstate commerce' even though the Department disqualified ten of the interstate flights chartered during that period. In sum, the Department found that use of the aircraft in interstate commerce 14 times during a 9-month period was sufficient to qualify for the RSE in spite of the fact that the aircraft was not used at all during the first nine months of taxpayer's ownership of the aircraft.

In order to qualify for the RSE, the purchaser is also responsible for filing the appropriate Departmental forms required to claim that the purchase of an aircraft and subsequent lease thereof to an interstate carrier for regular and frequent use in interstate commerce qualifies for the RSE. The purchaser must file either a Form RUT-25 (Use Tax Transaction Return) or a Form RUT-75(Aircraft/Watercraft Use Tax Transaction Return), depending on the lessor's status as a dealer or casual seller, respectively, together with a Form RUT-7 (Rolling Stock Certification), each due no later than 30 days after the date the aircraft is brought into Illinois.

In this case, as described in the summary of facts above, Owner structured its ownership and lease of the Aircraft so that it complies with the requirements for the application of the RSE. Furthermore, Owner shall timely file with the Department a Form RUT-25 and Form RUT-7 to ensure the application of the RSE to its purchase of the Aircraft.

However, there are several sub-issues relating to this matter that are not addressed in applicable Illinois law or regulations and that have not been analyzed by the Department or the courts to date. There appears to be no guidance regarding whether the interstate carrier must charge one particular charter rate for a particular aircraft to all of its charter customers or whether the interstate carrier may charge disparate rates. There also appears to be no guidance regarding the application of the RSE to a transaction if an interstate carrier lessee charts an aircraft to only one customer during the term of a charter lease, or whether the charter customer may consist of only one customer who is a party related (through common ownership) to the aircraft owner.

Furthermore, there is no clear guidance under Illinois law or regulations on the percentage of charter use of an aircraft that is necessary to meet the requirement under the RSE that there be 'regular and frequent' use of the Aircraft in interstate commerce. See, *Department of Revenue v. ABC, LLC d/b/a XYZ, Inc.* (UT-06-4, April 11, 2006) wherein the Department ruled that a total of 14 interstate flights during a 9-month period was sufficient to qualify for the RSE.

RULING REQUESTED

Based on the foregoing, we ask that the Department of Revenue provide Owner with the following ruling:

That the Rolling Stock Exemption from Illinois Retailers' Occupation Tax and Use Tax will apply to the Owner's purchase of the Aircraft.

In connection with the issuance of such ruling, we ask that the Department of Revenue also clarify the following on Owner's behalf:

1. That the fact that the Charter Lessee will charter the Aircraft in interstate commerce for hire primarily or solely to an affiliate or affiliates of the Owner and its/their employees and to individuals who are members of the Owner or its affiliate(s) will not adversely effect the application of the RSE to the Owner's Aircraft purchase;
2. That the use of disparate charter rates for the charter of the Aircraft by Charter Lessee will not adversely effect the application of the RSE to the Owner's Aircraft purchase; and
3. That the envisioned use of the Aircraft by Charter Lessee for 25% of the Aircraft's total annual flight hours will be sufficient for the application of the RSE to the Owner's Aircraft purchase or, if that is not the case, the percentage of usage by Charter Lessee that is necessary for the RSE to apply.

In the event you have any questions or need further information, please contact me. Thank you.

DEPARTMENT'S RESPONSE:

The Department's regulation "Public Information, Rulemaking and Organization" provides that "[w]hether to issue a private letter ruling in response to a letter ruling request is within the discretion of the Department. The Department will respond to all requests for private letter rulings either by issuance of a ruling or by a letter explaining that the request for ruling will not be honored." 2 Ill. Adm. Code 1200.110(a)(4). After reviewing the nature of your inquiry, it is the Department's position that we must decline to issue a Private Letter Ruling.

A determination whether specific tangible personal property qualifies for the rolling stock exemption is very fact specific and fact intensive and will often depend upon the specific contractual obligations between the seller and purchaser or the lessor and lessee of the tangible personal property. The person reviewing the request may not possess or have access to all the relevant information necessary to issue a ruling that subsequently will be binding on the Department. The best method for determining whether specific tangible personal property qualifies for the rolling stock

exemption is for an auditor to review all of the facts and circumstances surrounding the acquisition and use of the specific tangible personal property.

Several of the questions in the request are not limited to the Company's factual situation and seek the Department's position on issues that may have broader implications relating to the Department's administration, implementation and enforcement of the rolling stock exemption. These issues are best addressed in the context of an agency rulemaking under the Illinois Administrative Procedures Act rather than in the context of a letter ruling.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Richard S. Wolters
Associate Counsel

RSW:msk