SC98409

IN THE SUPREME COURT OF MISSOURI

DIRECTOR OF REVENUE,

Appellant,

v.

APLUX LLC AND PAUL AND ANN LUX ASSOCIATES L.P.,

Respondent.

From the Administrative Hearing Commission
The Honorable Sreenivasa Rao Dandamudi

APPELLANT'S REPLY BRIEF

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TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Regulations

Other Authorities

TABLE OF CONTENTS

ISSUES

(1) What constitutes a taxable use by a purchaser and owner of an aircraft for use tax purposes; and

(2) Whether an entity must transfer more than a mere non-exclusive license in order to qualify for the use tax exemption for resale purposes.

ARGUMENT

I. The Aircraft do not fall under any statutory exemption to use tax

"This Court strictly construes tax exemptions against the taxpayer." *DI Supply*, 601 S.W.3d at 196. "Any doubt regarding the applicability of an exemption is resolved in favor of taxation." *Id*. at 196-197.

"Out-of-state purchases are subject to a use tax for the privilege of storing, using or consuming within the state tangible personal property." *DI Supply*, 601 S.W.3d at 197. One exemption is property that is purchased solely for resale. *Id*. "Section 144.615(6) specifically exempts [t]angible personal property held by processors, retailers, importers, manufacturers, wholesalers, or jobbers solely for resale in the regular course of business from use tax." *Id*. at 197-198. As discussed in Appellant's brief, the Administrative Hearing AHC expressly stated that it was not making any findings on whether APLUX's purchase of the two airplanes at issue here qualified for an exemption under § 144.615(6). (App. Br. at 42) (citing L.F. 00056).[1]

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[1] Respondent argues that the undefined terms in § 144.615(6) are so broad that the statute applies to almost any company. (Resp. Br. at 34). Respondent claims that "APLUX is an importer as it imports aircraft from other states into Missouri" and thus the purchase of the Aircraft and their subsequent "sale" to Luxco qualify as a sale for resale under § 144.615(6) rendering both planes exempt from use tax. (Resp. Br. at 34-35). An importer is defined in the dictionary as "one that imports; esp: one whose business is the importation and sale of goods from a foreign country." Webster's Third New International Dictionary (3rd Ed. 1993). An importer therefore, is someone who brings

The AHC erred in finding that APLUX was entitled to a use tax exemption on two purchased aircraft because the purchase did not qualify for the resale exception under § 144.018.1(4). In order to qualify for this exception, the subsequent sale must have been "subject to tax but exempt under this chapter" meaning that the purported sale of the Aircraft from APLUX to Luxco must qualify for an exemption under Chapter 144. As discussed below, the purchase of the 2011 Socata TBM 850 (TBM) did not qualify for an exemption under Chapter 144, as the plane did in *Business Aviation*,[2] because it was not leased to a common carrier, and because its "lease" to Luxco was actually a limited license. The purchase of the 1999 Cessna 560XL (Excel) also did not qualify for an exemption under Chapter 144 because while it was leased to a common carrier, this lease was not exclusive as the lease was in *Business Aviation*, and the purchase should not be exempt from use tax when the taxpayer claiming the resale exemption reserves the right to use the airplane whenever it chooses.

The AHC found that APLUX's purchase of both airplanes qualified for a resale tax exemption as provided in § 144.018 generally and that APLUX properly collected and remitted sales taxes to the Director when it elected to

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something into one country from another. *See generally* 19 CFR § 101.1 Definitions. APLUX is not an importer simply because it purchased two airplanes out of state for alleged resale within Missouri.

[2] 579 S.W.3d at 216-218.

do so in accordance with 12 CSR 10-108.700(3). (L.F. 00068). Respondent argues that the AHC based its ruling on § 144.018.1(1), which exempts or excludes purchases of tangible personal property from tax made for the purpose of resale when the subsequent sale is subject to a tax in Missouri (or any other state). (Resp. Br. at 28).[3]

This Court should not affirm the AHC's decision on this basis because the "lease" of the Aircraft to Luxco was not the same as an outright sale; instead it was a limited license.

"License" is defined as: "authority or permission of one having no possessory rights in land to do something on that land which would otherwise be unlawful or a trespass—distinguished from lease." *Six Flags Theme Parks, Inc. v. Dir. of Revenue*, 102 S.W.3d 526, 533 (Mo. banc 2003) (quoting Webster's Third New International Dictionary 1304 (3rd ed. 1993)) (Wolff, J. concurring in part). This definition matches with other definitions of "license" drawn from real property. "A license is a privilege conferred either by writing or by oral permission to do one or more acts on the real estate without possessing any interest therein." *State v. Girardier*, 484 S.W.3d 356, 361 (Mo. App. E.D. 2015) (citing *Wright v. Edison,* 619 S.W.2d 797, 803 (Mo. App. E.D. 1981)). A license

[3] As discussed below, the AHC also found that the Excel purchase qualified for a use tax exemption under § 144.615(3) because Aero was a common carrier. (L.F. 00068). This finding was also incorrect and is an expansion of this Court's holding in *Business Aviation*. 579 S.W.3d at 216-218.

is "personal unassignable and ordinarily revocable. Such a privilege operates to authorize entry on premises for a certain purpose and for a protection to the licensee for acts done by him within the scope of the license." *Edison*, 619 S.W.2d at 803.

"In Missouri a lease is acknowledged as having a dual character: it is both a conveyance and a contract." *Premier Golf Missouri, LLC v. Staley Land Co., LLC*, 282 S.W.3d 866, 873 (Mo. App. W.D. 2009) (quotation omitted). A license conveys much less than a lease. Missouri courts and the statutes at issue provide that a "sale" can constitute a lease or rental, but not a license. *See* § 144.605(7) (Sale," any transfer, barter or exchange of the title or ownership of tangible personal property, or the right to use, store or consume the same, for a consideration paid or to be paid, *and any transaction whether called leases, rentals, bailments, loans, conditional sales or otherwise*, and notwithstanding that the title or possession of the property or both is retained for security.") (emphasis added); *See Bus. Aviation, LLC v. Dir. of Revenue*, 579 S.W.3d 212, 217 (Mo. banc 2019). To adopt Respondent's view would make every license a sale for resale.

Use tax law "is an all inclusive act which provides specifically for the exemptions to that particular tax…[and the Supreme Court] will not read into the use tax act exemptions which did not clearly appear therein." *Farm and Home Sav. Ass'n v. Spradling*, 538 S.W.2d 313, 319 (Mo. 1976).

Additionally, simply titling a document "lease" does not make it a "sale" under § 144.605(7). *See Kansas City Area Transp. Authority v. Ashley*, 485 S.W.2d 641, 644-645 (Mo. App. W.D. 1972) (examining the contents of the document to determine that a so-called "License Agreement" was in actuality a lease). Here, the lease was in actuality a limited license because the right to use the property at issue was revocable at the grantor's will. *Kan. City Area Transp. Auth.*, 485 S.W.2d at 644-645 ("The essential attribute of a bare license is the right of the grantor to freely revoke it at any time.").

In *Progress Instruments*, the AHC discussed how to distinguish between what was truly a lease and what was a management agreement. *See Progress Instrument, Inc. v. Director of Revenue*, Case No. 05-0861 RS at 15 (Mo. Admin. Hr'g Comm. June 21, 2006). While the AHC's decisions do not have precedential value,[4] it is important to note that the AHC found in this case that significant retention of control over an aircraft by the owner resulted in use tax being owed by the owner. (Holding that the taxpayer's (PI) management agreement with a common carrier (EBI) was not a lease because the taxpayer retained significant control over the aircraft and used it extensively.). The Aircraft Agreement had similar language to the lease agreements at issue here. *Id*. (App. Br. 19-21).

[4] *Central Hardware Co. v. Director of Revenue*, 877 S.W.2d 593, 596 (Mo. banc 1994).

In *Progress*, the AHC found that while the Aircraft Agreement gave a service company (EBI) "operational control" for FAR Part 135 flights, the taxpayer retained "operational control" for FAR Part 91 flights "and also retained control in other significant respects." *Id*. The AHC reasoned that: "The Supreme Court's opinion in *Six Flags I*, 102 S.W.3d at 530, noted an element of exclusivity of use by the lessee. That element is not present in this case. PI's extensive use of the airplane demonstrates that PI purchased the airplane primarily for its own use, and not primarily for the purpose of leasing it to EBI." *Id*. (citing *Six Flags*, 102 S.W.3d at 530).

Here, the "lease" transferred the right to use the Aircraft to Luxco but this right was limited because APLUX reserved priority of use for itself. This is a critical fact because in order to be analogous to a sale a lease must transfer more than just the non-exclusive right to use something. It must transfer rights incident to power and control over the tangible personal property and it must relay these rights exclusively. Otherwise it is a non-exclusive license and not a lease. Under the use tax definition of sale, a lessor may retain the title or possession of the property for security only. § 144.605(7). This statute does not permit a purchaser to maintain the right to use the tangible personal property. If the purported lessor retains rights incident to power and control then it is "using" the property and subject to paying use tax. *See Fall Creek Const. Co. v. Dir. of Revenue*, 109 S.W.3d 165, 170 (Mo. banc 2003) (Holding "Fall Creek

unambiguously purchased an undivided fractional ownership interest in two aircraft as evidenced by the purchase agreement. The mere fact that it entered into additional management agreements with Raytheon does not change the nature of Fall Creek's ownership interest."). While an incidental benefit will not defeat the use-tax exemption, here there was more than an incidental benefit to the purchaser. *See House of Lloyd, Inc. v. Dir. of Revenue*, 884 S.W.2d 271, 275 (Mo. banc 1994).[5]

The AHC found that the Aircraft were exempt from use tax because APLUX leased it to Luxco and paid tax on the revenue stream from Luxco to APLUX. *See* §§ 144.018.1(1) and 12 CSR 10-108.700. (L.F. 00054-00055). 12 CSR 10-108.700(3)(A)(3) states that a purchaser may lease an item and elect to pay sales tax on the lease income instead of use tax on the purchase price. (App. A60-A64.) This regulation defines "lease" as "any transfer of the right to possess or use tangible personal property for a term in exchange for

[5] Under the facts of this case, if the Aircraft were purchased within the state of Missouri, and fell under the sales tax definition of "sale at retail" and sales tax sale for resale exemption, this lease would not constitute a sale. *See DI Supply*, 601 S.W.3d at 201-202. While this Court held that the "sales tax and use tax resale exclusions derive from separate and distinct statutes requiring independent analysis," this Court should seek to harmonize their effects because the intent of the compensating use tax code is to ensure that taxpayers are treated equally whether they make their purchases in-state or out of state. *Farm and Home Sav. Ass'n*, 538 S.W.2d at 317 (Holding "the primary function of a use tax is to complement the sales tax…by creating equality of taxation of purchasers on use of property purchased outside the state which cannot be reached as sales because of the commerce clause of the federal constitution.").

consideration. This includes a rental." 12 CSR 10-108.700(2)(A). The regulation then goes on to include several examples, including one stating: "A taxpayer purchases three airplanes and provides the seller with a resale exemption certificate. Taxpayer then offers the airplanes for rental. Taxpayer must collect and remit tax on the rental payments for the airplanes." 12 CSR 10-108.700(4)(C) (App. A60-A64).

This regulation does not specifically permit the practice employed by Respondents here. This regulation was intended to illustrate a taxpayer's ability to choose whether to pay tax at the purchase of an item or pay on the lease stream when the item is leased to a different company. The regulation states that "taxpayer then offers the airplanes for rental." It does not say that Company A may purchase an airplane and then offer the airplane for rental to itself or to its parent company. Allowing this practice permits the end user to set their tax liability instead of having the tax liability flow from a negotiated agreement between two separate entities dealing at arms' length.

The evidence that the lease here was not negotiated at arms' length was detailed in Point II of Appellant's Brief. (App. Br. at 45-55). In brief summary, the pertinent facts showing the transaction was made for the purpose of tax evasion or deferral were: (1) the leases were between a parent company and a wholly-owned subsidiary with no independent means of purchasing the Airplanes or paying the taxes owed; (2) the leases were executed by the same

person acting on behalf of both parties; (3) the leases did not make a profit; and (4) the statement of the founding member of APLUX regarding its business purpose was "APLUX isn't a business. It's just two planes." (L.F. 00044-48, 00062-00063, Tr. 22).

II. The *Business Aviation* exemption should not be applied to the Excel

In *Business Aviation*, this Court found that a purchase and subsequent exclusive lease of an airplane to a common carrier qualified for an exemption from use tax applying an exemption that is specific to sales and leases of airplanes to common carriers. *See* 579 S.W.3d at 214 ("[S]ection 144.030.2(20) provides an exemption for sales of aircraft to common carriers.") (citing §§ 144.018.1(4), 144.615(3), and 144.030.2(20)). Here, the AHC found that the purchase of the Excel qualified for a use-tax exemption under § 144.615(3) because it was leased to Aero and Aero was a common carrier and cited *Business Aviation* for support. (L.F. 00068). But the AHC noted that because there were two lessees involved, the case might be distinguishable from Business Aviation and other precedent. (L.F. 00068).

In *Business Aviation*, this Court determined that the lease at issue transferred the right to use the Airplane to a common carrier because the lease granted "the exclusive care, custody and control of the Aircraft during the term of [the Lease] and at all times during any Part 135 charter operations

conducted by [Burgess]" to Burgess, Burgess maintained exclusive custody and control of the airplane each time it was flown, and the airplane was stored at Burgess' hangar facility when it was not flown. *Id.* at 218.

To apply the same exemption here would expand *Business Aviation* beyond the specific exemption outlined in § 144.030.2(20) that is solely for common carriers. The purpose of this exemption was not to permit non-exempt entities to bootstrap a claim for exemption from use tax by entering into a "lease" with an exempt entity. If the lease was like the one at issue here, it would freely permit the non-exempt entity to use the item at any time for a non-exempt purpose. Under this practice, the exemption would permit wide-spread tax evasion.

Additionally, the TBM was never leased to a common carrier and thus does not fall within the specific exemption from use tax discussed by this Court in *Business Aviation*.

Respondent asserts that APLUX never "used" either Aircraft. (Resp. Br. at 31, LF 61, 66). As discussed in Appellant's brief, the Director disagrees. Respondent's argument, and the AHC's findings to this effect, rely on too narrow a definition of use and equate use with flying or exercising operational control. An owner is not limited to flying an Aircraft as the sole method by which one may exercise "any right or power over tangible personal property incident to the ownership and control of that property." § 144.605(13). For

example, an owner uses an Aircraft when the owner signs an agreement reserving for themselves priority of use of that Aircraft, or enters into a management agreement for the Aircraft on behalf of itself and all lessees, or directs another company on how the Aircraft shall be used. All of which occurred here.

Under the plain reading of the contracts, APLUX maintained a taxable use of the Aircraft by reserving priority of use for itself. Additionally, APLUX exercised rights incident to control and ownership over the Aircraft by entering into maintenance agreements with Aero, and through its agent Mr. Lux, by directing that the Excel not be taken on short-leg flights. (L.F. 00047-00048, Tr. 133-134). Also, the Lease did not grant the same rights to use and control that were granted under the lease in Business Aviation, as Respondent alleges. (Resp. Br. at 31). In *Business Aviation,* the lessee had uninterrupted possession and exclusive operational control. 579 S.W.3d at 218. Here, APLUX could interrupt Luxco or Aero's exercise of use at any time under the "lease" agreements.

This Court should reverse the AHC's finding that the lease of the Aircraft qualified for any exception under § 144.018 because the sale was not for resale in the normal course of business by two companies dealing at arms' length but was purchased through a pass-through entity solely for the purpose of avoiding paying use tax on the purchase price of the plane.

Respondent relies on § 144.018 for a general sale-for-resale exemption. As discussed by the Director in the Appellant's brief, subsection 4 of § 144.018 explains that the statute was enacted as a clarifying statute following the decisions in *Music City Centre Management, LLC v. Director of Revenue*, 295 S.W.3d 465, (Mo. banc 2009) and *ICC Management, Inc. v. Director of Revenue*, 290 S.W.3d 699 (Mo. banc 2009). It is not a new resale exemption that abrogates or replaces §§ 144.615 or 144.030. This Court cited both §§ 144.615(6) and 144.010.1(11) as the use-tax and sales-tax sale-for-resale exemptions in *DI Supply*, 601 S.W.3d at 197-198.

Respondent cites *Sipco* for support that "[s]ection 144.018 avoids taxing the same piece of tangible personal property twice." However *Sipco* was handed down in 1994, long before the effective date of § 144.018 (May 12, 2010). Section 144.018 is not superfluous because it addressed an issue in the case law as discussed in subsection 4. Giving effect to § 144.018.1 as a separate resale exemption renders §§ 144.615(6) and 144.010.1(11) superfluous. "This Court assumes that the legislature does not intend to perform a useless act." *E & B Granite, Inc. v. Dir. of Revenue*, 331 S.W.3d 314, 317 (Mo. banc 2011). Section 144.018 should be read *in pari materia* with the other sale for resale tax provisions found in §§ 144.010.1 and 144.615(6). *Roesing v. Dir. of Revenue*, 573 S.W.3d 634, 639 (Mo. banc 2019) ("Under the doctrine of *in pari materia*,

statutes relating to the same subject matter should be construed to achieve a harmonious interpretation.").

The AHC's finding is not supported by the Compensating Use Tax Law or the Department of Revenue's regulations. This Court should reverse the AHC's finding that APLUX qualified for an exemption from use tax.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the Administrative Hearing Commission.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

The attached brief complies with the limitations contained in Missouri Supreme Court Rule 84.06 and contains 3,045 words, excluding the cover, certification and appendix, as determined by Microsoft Word 2016 software; and that pursuant to Rule 103.08 the brief was served upon all other parties through the electronic filing system.

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