

Excise Taxes On Management Services—The Path Forward

BY: JACQUELINE E. ROSSER

In 2012 the IRS issued the now well-known Chief Counsel Advice Memorandum (CCA), which concluded that amounts paid by aircraft owners for management services, particularly when the owner doesn't directly employ the pilots, are subject to the commercial Federal Excise Tax of 7.5% on the amounts paid. The CCA described the tax due on the management fee, as well as other amounts paid to the management company by the owner, for things like maintenance, insurance and hangar fees. The CCA's interpretations ran counter to virtually everyone in the industry's understanding of the FET and when it does or doesn't apply.

It was predictable what came next—audits of air charter operators providing management services began to reflect the findings of the CCA, and dozens of operators faced significant assessments for alleged

uncollected taxes on management services. Operators under audit faced IRS findings that reached into the million-dollar range. Fortunately, a significant number of operators successfully appealed audit findings.

Since the issuance of the CCA, NATA has worked hard to represent member interests by establishing and building relationships within the IRS and the Treasury Department, including retaining specialized counsel to help navigate this process. In the fall of 2013, the IRS formally acknowledged the need for new, clear FET guidance for industry by taking two significant steps. First, they agreed to a suspension of audit assessments on the issue of taxability of aircraft management services. Second, they added the development of new FET guidance to their Priority Guidance List (PGL).

Priority Guidance

The inclusion of FET guidance on the PGL is significant because it means the issue is important enough to the IRS to ensure resources are dedicated to the project. This has resulted in an on-going dialogue between the government and NATA as we educate them on the uniqueness and nuances of aircraft management services, especially when an owner's aircraft is also used by a certificate holder for Part 135 air charter.

A benefit of the current course of action is that whatever type of guidance the IRS ultimately issues, it will first be published in draft form. This means that everyone will have an opportunity to provide comments in response to the IRS proposal, and ideally shape it into something that is easily understood by industry and doesn't

Continued on page 56

Beginning in 2014 NATA engaged a consultant who has special expertise working with the Department of Treasury and the IRS. Several members have generously supported the extraordinary effort to engage these agencies on behalf of all NATA members. NATA offers them heartfelt thanks for their leadership.



Bakersfield
Jet Center by
Loyd's Aviation

Jet Aviation

Keystone
Aviation

LJ Aviation

Pentastar
Aviation

Priester Aviation

Excise Taxes on Management Services—The Path Forward

Continued from page 55

inappropriately impose commercial taxes on private aircraft operations.

While NATA is engaged, meeting with the right people at the IRS and Treasury Department, and working toward revised guidance, those of you in need of the answers the

audit assessments for uncollected taxes on amounts paid for aircraft management services. FET audits (i.e. audits of your quarterly Form 720 filings) are on-going and will continue, although they do seem to have slowed somewhat since the

The most important thing you can do is review new guidance and provide comments in response.

guidance is intended to provide are justifiably frustrated by the pace these in-depth efforts require.

This is where the suspension of audit assessments does provide some assistance. It's important to understand what the suspension does and how to avail yourself of it.

Assessment Suspension

Importantly, this is *not* a suspension of audits. It is a suspension of

suspension was announced. Auditors can and will review your compliance with other excise tax elements; such as proper collection of segment fees, review of fuel tax credits, eligibility for claimed exemptions, compliance with the Canada/Mexico 225-mile rule, etc. Findings related to these issues will continue as before. Only if there is aircraft management service involved and the IRS auditor determines you have a tax liability

related to that activity does the suspension come into play. If this happens, you must formally disagree with the examination's findings to have the assessment suspended.

The suspension of assessments will continue until the IRS finalizes new guidance on this issue. Once that occurs, the ultimate disposition of those suspended audit findings will be influenced by the guidance and other factors.

While the suspension is a welcome option for those undergoing an audit, many operators are trying to figure out how or if they should change the way they do business to head off audit problems.

Changing Your Business

There are two key questions charter operators regularly ask—do I need to change my management agreements with owners? And, do I continue to employ the pilots who fly for the aircraft owner? Neither question has a straightforward answer.

Legislation Introduced On FET Issue

As this edition of *ABJ* went to print, members of the Ohio congressional delegation introduced bipartisan legislation in the House and Senate that, if enacted, will prohibit the IRS from imposing commercial excise taxes on aircraft management services.

In late July, Congressman Pat Tiberi (R-OH) introduced a bill (H.R. 5382) that would require the IRS to exempt from the commercial transportation excise taxes amounts aircraft owners pay for management

services. Companion legislation was introduced in the Senate (S. 2775) by Senators Sherrod Brown (D-OH) and Rob Portman (R-OH).

The bills are an important signal to the Administration from Congress that commercial taxes should not apply to aviation management services. NATA is in contact with key members of the House and Senate to provide them with additional information on the issue.

Your best bet is to engage an attorney, consultant, accountant or other qualified professional that has knowledge of both aviation regulations and excise taxes. This person should take a complete look at your agreements and how your business actually runs in order to conduct a knowledgeable risk assessment and help you plan a strategy to balance your business needs, owner's desires, the FAA regulations, and the IRS requirements.

Remember, the first premise is always the legal operation of the aircraft. Having your operational control system well documented and properly executed is essential. Everyone who lived through the operational control special emphasis inspections a few years ago learned that lesson.

From there, evaluating the various pros and cons of pilot employment, fleet insurance policies and even whether you should have one

agreement covering both management services and charter services for third parties (or if you need two) are all nuanced and often client-specific decisions.

Talk with your owners (or their "people" as it may be) to make sure they are hearing from you about the situation and the latest developments. They hired you for your aviation expertise, so make sure you give them your informed perspective. Discuss any changes you want to make and listen to their concerns about the implication of those changes.

The one thing I don't recommend you do is initiate wholesale changes to your business based upon the latest information from the rumor mill or to act on third-hand (or worse) reports that come your way without verifying their accuracy.

Participate

I mentioned earlier that the IRS will publish the new guidance in draft form. Once that happens, you can expect your inbox to light up with alerts and information about the draft document. The most important thing you can do is be ready to review it and provide comments in response. Air charter operators have the obligation to collect and remit taxes, but it is the obligation of the IRS to provide you with unambiguous guidance on how to properly execute your responsibilities. By providing thoughtful, detailed and constructive comments during the review period you can help ensure that occurs. **A**

Jacqueline Rosser provides aviation consulting services specializing in on-demand charter operations through her company *Jacqueline Rosser Consulting, LLC.* jrosser@outlook.com



Irving Aviation
709.651.5000