STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
AERO INSTRUMENTS & AVIONICS, INC.	:	DETERMINATION DTA NO. 811564
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period September 1, 1988 through August 31, 1991.	:	

Petitioner, Aero Instruments & Avionics, Inc., 7290 Nash Road, North Tonawanda, New York 14120-1508, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1988 through August 31, 1991.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on March 16, 1994 at 1:15 P.M., with all briefs filed by July 25, 1994. Petitioner appeared by Gary J. Gleba, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Vera R. Johnson, Esq., of counsel).

ISSUES

I. Whether petitioner's purchase and/or lease of machinery and equipment used to repair and maintain commercial aircraft is exempt from sales and use taxes pursuant to Tax Law § 1115(a)(21).

II. Whether petitioner has established that its failure to pay the tax due on the purchase of certain operations manuals and other miscellaneous expense items was due to reasonable cause and not willful neglect.

FINDINGS OF FACT

Petitioner, Aero Instruments & Avionics, Inc. ("Aero"), was engaged in the business of overhauling and repairing primarily commercial aircraft instruments and components during the period September 1, 1988 through August 31, 1991. The parts/instruments were sent to it for repair/testing, and Aero would then return the parts to the customer. Aero did no installation work.

In performing these services, Aero purchases or rents/leases various testing equipment, instruments and other items for use in the maintenance and repair of aircraft.

Aero does not own the aircraft but contracts for its repair and maintenance services primarily with commercial carriers.

The Division of Taxation ("Division") performed a field audit of Aero's books and records during the latter half of 1991 and the first half of 1992. The sales and purchase records were found to be adequate. Sales and asset acquisitions were examined in detail. Purchase records, although adequate, were tested pursuant to a duly executed audit election method agreement.

Aero maintained a sales tax accrual account which revealed that all recorded tax was properly reported. Likewise, Aero maintained a withholding tax accrual account which revealed that all recorded tax was properly reported.

The detailed audit of Aero's sales records indicated additional taxable sales of $2,523.72 and resulted in additional sales tax due of $190.78. This amount is not included in the notices in issue.

The detailed audit of asset acquisitions yielded $405,980.80 in purchases of assets on which $28,418.72 in additional tax was found due.

Finally, the Division performed a one-year test of expense purchases, utilizing the year 1990. The one-year test resulted in tax of $12,836.82. This was divided by the total expenses tested yielding an error rate which was applied to account totals for the entire audit period. Additional tax was determined to be $34,223.50.

Total additional tax determined to be due on audit was $62,833.00 and was assessed by two notices of determination and demands for payment of sales and use taxes due, to wit, notice numbers L-005712238-6 and L-005712239-5, both dated May 28, 1992.

Assessment number L-005712239-5 asserted additional tax of $10,602.58, together with penalty and interest. This tax arose from the test period audit of purchases which the Division believed were taxable beyond dispute because they were not related to repair and maintenance of commercial aircraft in any way. The workpapers indicated that the items in this category included those not related to instrument repairs, like manuals, air conditioner filters, building maintenance, gestetner toner, lighting fixtures, painting and patching work, erection system and dust caps, protective caps, shoeboxes and sweater boxes, towels, toilet tissue, kimwipes, printer, portable inkjet and paper, scanner, holiday cards, ribbons, window cleaning, exhaust parts, video card, diskettes, platform scale, hard drive and other miscellaneous computer equipment.

Assessment number L-005712238-6 asserted additional tax of $44,653.29 plus interest which was the sum of tax on purchases/expenses considered to be related to commercial aircraft ($23,620.92) and the tax determined to be due on assets related to commercial aircraft ($21,032.37). Items deemed taxable for the test period analysis included paint brushes, repair of deadweight testers, service bulletins, manuals, calibrated stopwatches, micrometer, level, dial caliper calibrator, torque wrench calibration, kellstrom digital protractor/calibrator, wire wheels, taps and an installation tool, instruction books and equipment rentals.

The latter part of the assessment attributable to tax on assets related to commercial aircraft included items such as testing equipment, digital pressure gauges, manometers, attentuators, oscilloscopes, tektronics accessories, wave analyzers, filters and an altos computer.

Not in issue, but worth noting for the record, was $7,386.35 in additional tax determined to be due on assets not related to commercial aircraft which Aero paid together with the penalty and interest imposed.

Penalties were assessed pursuant to Tax Law § 1145(a)(1)(i) and (vi) on assessment number L-005712239-5. These penalties were assessed on the purchases of items (primarily

manuals) which the Division determined were not related to the repair or maintenance of commercial aircraft and therefore the Division believed there to be no reason for Aero's failure to pay the tax.

Aero was the subject of a prior audit by the Division for the period 1974 to 1977, but no audit history now exists which would reveal the details of the audit and no witnesses had personal knowledge of the audit or recalled the specifics of the records kept concerning the audit.

Subsequent to the assessment, Aero requested a conciliation conference which was held on October 29, 1992. A Conciliation Order sustaining the statutory notices was issued on January 8, 1993.

SUMMARY OF THE PARTIES' POSITIONS

Aero contends that penalties asserted by the Division on assessment number L-005712239-5 should be abated because it believed in good faith that the operations manuals, which constituted the majority of untaxed items purchased, were exempt from tax.

Aero also argues that it is entitled to an exemption from sales and use taxes on its purchase and/or lease of equipment used to repair, test and maintain commercial aircraft.

The Division asserts that the purchases in question were not used in the repair or maintenance of commercial aircraft within the meaning and intent of Tax Law § 1115(a)(21). Further, the Division argues that manuals purchased by Aero were clearly subject to tax and petitioner's good faith belief that they were exempt does not constitute reasonable cause for the abatement of penalties.

CONCLUSIONS OF LAW

A. Tax Law § 1105(c) provides that sales tax shall be imposed on the receipts from every sale of the services of maintaining, servicing or repairing tangible personal property except those services rendered:

> "with respect to commercial aircraft, machinery or equipment and property used by or purchased for the use of such aircraft as such aircraft machinery or equipment, and property are specified in paragraph twenty-one of subdivision (a) of section eleven hundred fifteen" (Tax Law § 1105[c][3][v]).

Tax Law § 1115(a) provides for exemption from the sales tax imposed by Tax Law § 1105(a) on certain receipts, including:

> "(21) Commercial aircraft primarily engaged in intrastate, interstate or foreign commerce, machinery or equipment to be installed on such aircraft and property used by or purchased for the use of such aircraft for maintenance and repairs and flight simulators purchased by commercial airlines" (Tax Law § 1115[a][21]).

Although no regulations have been promulgated in this area, the Division issued a Technical Services Bureau memorandum, TSB-M-80(4)S, which stated that certain definitions, although provided in the sales tax regulations with respect to commercial vessels, were also applicable to commercial aircraft (see, 20 NYCRR 528.9[a][4]; 528.9[a][5]; 528.10[b]). The memorandum also provided:

> "Although the term 'commercial aircraft' has not been defined in the Tax Law, . . . aircraft used by an 'airline' as defined above, would constitute 'commercial aircraft' qualifying for sales tax exemption."

The memorandum closes with a list of purchases for qualifying exempt commercial aircraft, one of which is the purchase of equipment and machinery purchased or rented for use in the maintenance of qualifying exempt commercial aircraft. Those purchases were deemed exempt.

The aircraft parts upon which Aero performed repairs (meant to include testing and maintenance herein) were from "commercial aircraft" as that term was defined above. The question devolves to one of whether the services performed by Aero on the commercial aircraft parts, and specifically whether its purchase of equipment and machinery used in those repairs, should be exempt from tax.

Aero argues that the statutory language should be construed broadly to include services rendered or machinery or equipment purchased by it for use in its repair of parts of qualifying exempt commercial aircraft. Aero's position bears a heavy burden, however.

In Matter of Airlift International v. State Tax Commn. (52 AD2d 688, 382 NYS2d 572, 574) the court stated:

> "(1) In construing a taxing statute in order to determine what is included within its purview the rule is that the statute is to be strictly construed in favor of

> the taxpayer and against the taxing authority (Matter of Nehi Bottling Co. v. Gallman, 39 AD2d 256, 333 NYS2d 824, affd 34 NY2d 808, 359 NYS2d 44, 316 NE2d 331; Matter of American Locker Co. v. Gallman, 38 AD2d 105, 327 NYS2d 973, affd 32 NY2d 175, 344 NYS2d 358, 297 NE2d 96). In construing a taxing statute in order to determine the scope of a statutorily prescribed exemption, however, the rule is that the exemptions are to be strictly construed and that if any ambiguity or uncertainty exists it is to be resolved in favor of the sovereign and against exemption (Matter of Aldrich v. Murphy, 42 AD2d 385, 348 NYS2d 384)."

Further, in Matter of Moran Towing and Transportation Co. v. New York State Tax Commn. (72 NY2d 166, 531 NYS2d 885, 888), the court noted the familiar rules of construction:

> "that a statute creating a tax exemption must be construed against the taxpayer (Matter of Alamo Assocs. v. Commissioner of Fin. of City of N.Y., 71 NY2d 340, 343, 525 NYS2d 823, 520 NE2d 542; Matter of Grace v. New York State Tax Commn., 37 NY2d 193, 195-196, 371 NYS2d 715, 332 NE2d 886), that the taxpayer must establish that its interpretation of the statute is not only plausible, but also that it is the only reasonable construction (Matter of Blue Spruce Farms v. New York State Tax Commn., 99 AD2d 867, 472 NYS2d 744; affd for reasons stated below, 64 NY2d 682, 485 NYS2d 526, 474 NE2d 1194), and that the taxpayer must show that the Tax Commission's interpretation of the exemption's scope is irrational or clearly erroneous (Matter of Great Lakes Dredge & Dock Co. v. Department of Taxation & Fin., 39 NY2d 75, 79, 382 NYS2d 958, 346 NE2d 796, cert denied, 429 US 832, 97 S Ct 95, 50 L Ed2d 97, supra; Matter of Young v. Bragalini, 3 NY2d 602, 605-606, 170 NYS2d 805, 148 NE2d 143, rearg denied, 4 NY2d 879, 174 NYS2d 1027, 150 NE2d 704)."

Tax Law § 1115(a)(21) specifically states that receipts for "property used by or purchased for the use of such aircraft [commercial aircraft] for maintenance and repairs" will be exempt from the sales tax imposed pursuant to Tax Law § 1105(a). The statute does not indicate specifically who must "purchase" the property for use of the aircraft for maintenance and repairs. With no other guidance available for the interpretation of this phrase, it is proper to seek the guidance of the legislative history:

> "Undoubtedly, the primary consideration in the interpretation of all statutes is to discern and apply the will of the Legislature (see, Matter of Sutka v. Conners, 73 NY2d 395, 403, 541 NYS2d 191, 538 NE2d 1012; cf., Matter of Moran Towing & Transp. Co. v. New York State Tax Commn., 72 NY2d 166, 173, 531 NYS2d 885, 527 NE2d 763). If legislative intent is plain, clear and distinct from a literal reading of the statute, it will be enforced according to its terms. If, however, examination of the language leaves the statute's purpose and intent uncertain, resort must be had to other available aids" (Matter of American Communications Technology v. State of New York Tax Appeals Tribunal, 185 AD2d 79, 592 NYS2d 147, 148, affd 83 NY2d 773, 611 NYS2d 125).

If, after a reading of the statute, the meaning is not clear, courts must search for

legislative intent in the purpose of the enactment (McKinney's Cons Laws of NY, Book 1, Statutes § 92[b]).

A literal reading of Tax Law § 1115(a)(21) indicates that an exemption is granted on receipts for "property used by or purchased for the use of such aircraft for maintenance and repairs." Aero contends that this exemption applies to its purchase of equipment and machinery it uses to "repair" aircraft parts and components, while the Division construes the exemption to apply only to commercial airlines.

The subsection also provides for three other exemptions which specifically apply only to commercial airlines, i.e., receipts from the purchase of commercial aircraft, machinery or equipment to be installed on commercial aircraft and the purchase of flight simulators. Therefore, petitioner contends that one of four exemptions in subsection (21) should be read more broadly than the other three. This construction does not survive the scrutiny of a literal reading of the statute or a review of the legislative history.

As set forth in the memorandum referred to above, TSB-M-80(4)S, the term "commercial aircraft" refers to an aircraft "used by an 'airline'". Therefore, property used by "such aircraft" for maintenance and repairs refers to property owned by the airline and consumed by it. Property purchased for the use of such aircraft for maintenance and repair refers to property purchased by an airline for the maintenance and repairs of its aircraft. Certainly, Aero's purchase of property was for the use of its business which was the provision of repair service on aircraft parts sent to it by commercial airlines, not for the use of the commercial aircraft used by an airline.

Even assuming this construction was not sufficient to reach this conclusion, the legislative history leaves no doubt as to the legislative intent. The justification set forth in the "Memorandum in Support" clearly indicated the intended beneficiaries:

> "JUSTIFICATION: This bill would keep New York State competitive with the twelve other states which offer programs of tax incentives to airlines for maintenance purposes. Generally, the airlines tend to locate their maintenance facilities in those states which offer such programs. There will be a somewhat accelerated amount of major maintenance being performed during the next few years as the airlines bring their fleets into compliance with federal noise

regulations. It would, therefore, be desirable to make New York as attractive as those states with incentive programs in order to prevent relocation with the consequent loss of jobs and to encourage the establishment of new facilities within the state. The major airlines generally tend to locate their maintenance facilities in the 12 states that offer programs of tax incentives for the big carries [sic] for that purpose. New York, by enacting this bill, would become competitive with those 12 states and thereby encourage the carriers to perform their maintenance work in New York, strengthening the State's economy. This measure was born out of the same concern for improvement of our business climate that prompted out [sic] $750 million tax cut earlier this year. It also would help persuade other businesses and industries that the Legislature here is serious about continuing on a course intended to keep and attract business here. American Airlines, for example, now flies its planes to Tulsa, Oklahoma for service and repair to avoid paying the New York sales taxes. We should be able to do better for ourselves and for the airlines that [sic] that. We have the finest labor force in the nation here and our people should have the opportunity to do these jobs for the airlines" (Mem in Support, Bill Jacket, L 1978, ch 773; emphasis added).

Even the Division of the Budget, which was fearful of the revenue ramifications of a broad application of the exemption, noted that the exemption was meant to be a tax incentive to airlines, specifically Pan American, which had threatened to leave New York without such relief (see, Budget Report on Bills, Bill Jacket, L 1978, ch 773). In fact, the agency memoranda and airline industry letters clearly reflect an interpretation of the statutory language consistent with what has been determined herein. Particularly revealing was the letter of the former Commissioner of the Department of Taxation and Finance, James H. Tully, Jr., who said:

"Under existing law, with regard to aircraft, only food sold to an airline for in-flight consumption and fuel sold to an airline are exempt from sales and use taxes. The purchase of aircraft and other related tangible personal property and certain related services are subject to sales and use taxes. However, where the installation, maintenance, servicing or repairing services are performed by the airline's own employees, there is no tax on such services under the existing law because the statute provides that wages and other compensation paid to employees are not taxable receipts under the provision imposing sales taxes on services (see section 1105(c), last paragraph (unnumbered)).

* * *

"The sponsors of the bill state in their memorandum that the aim of the bill is to encourage airlines to locate their aircraft maintenance facilities in New York and to retain existing maintenance facilities here. I understand that Pan American Airways and American Airlines are particularly interested in the passage of this bill.

"I understand that the large airlines perform the maintenance work on their own planes by using their own employees. Therefore, under existing law, they would not have to pay a tax on the service of installing items on their planes and upon the services of maintaining, servicing or repairing their planes. However,

> under existing law, they would have to pay a tax when any parts are installed on the planes and any parts and supplies are used in maintenance, service or repair of the planes. If an airline performed a maintenance or repair job for another airline, under existing law, it would have to collect a tax on the total charge for the service including the amount charged for the parts or supplies" (Letter to the Honorable Hugh L. Carey, Bill Jacket, L 1978, ch 773).

Hence, there seems to be little doubt from the legislative history that the exemption was meant for commercial airlines and that the statutory language of Tax Law § 1115(a)(21) must be read to consistently apply the exemptions provided therein to only commercial airlines.

Since the case can be determined from a reading of the statute and the legislative history, the analogies drawn by the parties to the cases of Todd Shipyards Corp. v. State Tax Commn. (52 AD2d 126, 383 NYS2d 93) and Matter of Brewer Dry Dock Company (State Tax Commn., May 6, 1983) need not be addressed, except to note that the decisions in those matters are consistent with the conclusion reached herein.

B. Petitioner was assessed penalties under Tax Law § 1145(a)(1)(i) and (vi) on assessment number L-005712239-5, which resulted from its failure to pay sales tax on certain manuals it purchased. Petitioner believes that it had reasonable cause for not paying the tax because such purchases had not been determined to be taxable until 1980 and therefore were not assessed in an audit of Aero's records by the Division in 1977.

However, as of the issuance of the Technical Services Bureau memorandum on May 15, 1980 (TSB-M-80[4]S), there was no question that manuals, guides and advertising materials were taxable. Aero, however, believes its good faith reliance on the results of its prior audit constitutes reasonable cause for the abatement of penalties under Tax Law § 1145(a)(1)(iii) and (vi).

Also, Aero's representative raised the possibility that its accountants during the audit period did not advise them competently. However, this point was not developed subsequent to such representative's closing argument at hearing.

Petitioner's two arguments seem to rely upon 20 NYCRR 536.5(c)(5) for its definition of reasonable cause which states, in pertinent part, as follows:

> "Any other cause for delinquency which would appear to a person of

> ordinary prudence and intelligence as a reasonable cause for delay and which clearly indicates an absence of willful neglect may be determined to be reasonable cause. Ignorance of the law, however, will not be considered as a basis for reasonable cause."

Although petitioner raises its reliance upon its accountants only weakly, it will be dealt with first. It is well established that reliance on a tax advisor does not necessarily constitute reasonable cause for the remission of penalties (see, Matter of Auerbach v. State Tax Commn., 142 AD2d 390, 536 NYS2d 557; Matter of LT & B Realty v. State Tax Commn., 141 AD2d 185, 535 NYS2d 121). In order to establish reasonable cause, the reliance itself must be reasonable (Matter of BAP Appliance Corp., Tax Appeals Tribunal, June 29, 1989). In evaluating whether the reliance was reasonable, the taxpayer is required to show that he acted with ordinary business care and prudence in attempting to ascertain his tax liability (Matter of A & V Crown, Tax Appeals Tribunal, May 24, 1990). Petitioner must also demonstrate that the advice came from a competent tax advisor (id.). In this instance, the record does not contain any evidence that would establish that it was reasonable for petitioner to rely on its accountants. Therefore, petitioner has not shown that its failure to pay the tax was due to reasonable cause.

Further, Aero's contention that it reasonably relied on a prior audit in 1977 when there had been an intervening major change in the law (Tax Law § 1115[a][21]) and an interpretation of that law by the Division in TSB-M-80(4)S is without merit and amounts to a defense of "ignorance of the law" which is specifically excepted from the definition set forth in 20 NYCRR 536.5(c)(5) as constituting reasonable cause.

Therefore, the penalties imposed on assessment number L-005712239-5 are sustained.

C. The petition of Aero Instruments & Avionics, Inc. is denied and the two notices of determination and demands for payment of sales and use taxes due, dated May 28, 1992, are sustained.

DATED: Troy, New York
January 19, 1995

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE