TAXPAYER INFORMATION RULING LR12-002

April 5, 2012

This taxpayer information ruling is in response to your June 3, 2011 taxpayer information ruling request as supplemented by the July 27, 2011 and September 19, 2011 correspondence, in which you, ("Representative"), request that the Arizona Department of Revenue ("Department"), on behalf of your unnamed client ("Client") issue a ruling on the application of Arizona's transaction privilege and use tax to Client's sales of helicopter tours, . . . ("recreational vehicle tours"), and picnic food.

Statement of Facts:

The following facts are excerpted from your June 3, 2011 letter:

1. Client's business is that of providing helicopter tours and [recreational vehicle]/helicopter combination tours of certain scenic areas in the State of Arizona. The [recreational vehicle]/helicopter combination tour may include a picnic. Client purchases [recreational vehicle] tours from [Tour Company] and picnic food from [Café] which charges Client state and local transaction privilege tax on the cost of the tours and food. Client passes through the cost to its customers and does not mark-up the cost of the tour or food or receive a commission from [Tour Company].[1]
2. Client's tours are priced as a fixed, lump sum per person or couple plus a 15% fuel surcharge. Tours do not operate on a set schedule, and they are usually booked directly through Client who is paid by the customer. Tours may also be arranged through area hotels, resorts, or tour brokers. Guests pay the hotel, resort or tour broker for the cost of the tour, and the Client invoices the hotel, resort or tour broker for approximately 90% of the retail price of the tour. The difference between amounts paid by guests and the amount invoiced by Client is a commission to the hotel, resort or tour broker. The hotel, resort or tour broker may or may not mark-up the cost of the tour, and they do not give Client a resale certificate.

The following facts are excerpted from your July 27, 2011 letter:

[1] Representative, initially incorrectly said, Client purchases tours and picnic food from [Tour Company] which charges Client state and local transaction privilege tax on the cost of the tours and food. The error was corrected in the September 19, 2011 correspondence.

1. Client operates helicopters – pilots and ground crew are all employees of Client. Some aircraft are owned by company and other aircraft are leased from third parties.
2. [Recreational vehicles] are owned and operated by [Tour Company], which is an independent company with no ties to Client.
3. . . . Client is a helicopter tour company. Client owns and leases aircraft and hires employees and ground crew for flights. [Recreational vehicle] tours are secured from independent third parties and included with helicopter tours as a combination package.
4. Client and [Tour Company] work together to provide combination packages. Client works closely with [Tour Company] to arrange and schedule tours.
5. [Tour Company] and Client entered into an oral agreement which allows Client to sell [Tour Company's] tours to Client's customers.
6. Client is not contractually restricted from working with other helicopter or [recreational vehicle] tour vendors.
7. Client is a helicopter tour company that owns and leases aircraft. Additional services are purchased from other vendors and bundled into packages. Client charges its client for full packages and pays [Tour Company] and other vendors at agreed upon rates.
8. Client charges customers directly for tours and pays [Tour Company] agreed upon prices for tours sold.
9. Customers can walk into facility and buy tours or buy tours via phone or internet.
10. Hotels, resorts, or tour brokers book tours with Client via phone or internet.
11. Client does not currently charge customers, including hotels, resorts or tour brokers, transaction privilege tax on the tour sales.
12. Client's helicopter tours are flown 1500 feet or less AGL ("Above Ground Level").

The following facts are excerpted from your September 19, 2011 letter:

1. Combo Package includes: (1) helicopter tour provided by Client, using Client's aircraft and employees; (2) [recreational vehicle] tours purchased from another tour company – includes only [recreational vehicle] & driver; and (3) picnic lunch – purchased by Client from local purveyor, [Café].
2. Client purchases picnic lunches directly from local vendors.
3. Client buys the provided food for the picnic and pays in full. [Tour Company] does not pay for any of this food. Client purchases this picnic basket for two

from a local restaurant called [Café]. This purchase includes tax per owner of café.

4. Client does not provide picnic food to its customers while its customers are on the helicopter tour.
5. Client purchases the food and provides it to the customers. [Tour Company] has nothing to do with this process other than taking the food with them on the [recreational vehicle] tour to give to the customers.
6. Client separately states the charge for the helicopter tour from the [recreational vehicle] tour.
7. Client separately states the charge for the helicopter tour from the picnic food on the invoice.
8. On Client's invoice to customer, Client does not charge its customer a lump sum for the helicopter tour, [recreational vehicle] tour, and/or picnic food on the invoice. All charges are stated separately. Food is listed on its own line (no tax charged), [recreational vehicle] amount on its own line (no tax charged) and tours are separate on their own line. Tax we charge for our tours which is 15% is also separate on its own line.

Issue(s):

Based on the arguments presented in your request, Client raises the following issues:

1. Whether Client's helicopter tours are subject to Arizona's transaction privilege tax or whether a federal aviation statute on state taxation, 49 U.S.C. § 40116 (also known as the Anti-Head Tax Act ("AHTA")), preempts Arizona's transaction privilege tax on the gross proceeds of sales or gross income derived from Client's business of helicopter tours?
2. Whether [recreational vehicle] tours are taxable amusements per A.R.S. § 42-5073(D) of the amusement classification?
3. Whether Client can deduct the actual amount it pays [Tour Company] for providing the [recreational vehicle] tours and not remit additional tax to the State of Arizona?
4. Whether Client can deduct its cost of the picnic food it purchased from a local café to provide to its customers and not remit additional tax to the State of Arizona?

Your Position(s):

1. Client's helicopter tour activities are exempt from Arizona's transaction privilege tax under the transporting classification by virtue of the federal preemption created in 49 U.S.C. § 40116(b)(4). Per A.R.S. § 42-5062(A)(2), the transporting classification does not include the business of transporting for hire persons traveling in air commerce by aircraft if taxation of the business is preempted by federal law.

2. [Recreational vehicle] tours are taxable amusements per A.R.S. § 42-5073(D) of the amusement classification.
3. Client may pass-through the cost of the [recreational vehicle] tours, plus the transaction privilege tax charged by their vendor, to its customers. Pass-through transactions involving destination services are allowed by businesses operating a transient lodging facility, per *Arizona Transaction Privilege Tax Ruling* 06-1, 09/14/2006. It would be unlawful to treat taxpayers dissimilarly regarding identical transactions.
4. Client purchases [recreational vehicle] tours and picnic baskets from independent third parties and pays sales [*sic*] tax on the purchases. Client wants to pass-through TPT as allowed in *Arizona Transaction Privilege Tax Ruling* 06-1, 09/14/2006. It would be unlawful to treat taxpayers dissimilarly regarding identical transactions.

Applicable Statutory Provisions:

Arizona Revised Statutes § 42-5001(4) defines "[g]ross income" to mean the gross receipts of a taxpayer derived from trade, business, commerce or sales and the value proceeding or accruing from the sale of tangible personal property or service, or both, and without any deduction on account of losses.

* * *

A.R.S. § 42-5001(5) defines “[g]ross proceeds of sales" to mean the value proceeding or accruing from the sale of tangible personal property without any deduction on account of the cost of property sold, expense of any kind or losses, but cash discounts allowed and taken on sales are not included as gross income.

* * *

A.R.S. § 42-5008 levies a transaction privilege tax measured by the amount or volume of business transacted by persons on account of their business activities.

* * *

A.R.S. § 42-5073 imposes the transaction privilege tax on the business of operating or conducting theaters, movies, operas, shows of any type or nature, exhibitions, concerts, carnivals, circuses, amusement parks, menageries, fairs, races, contests, games, billiard or pool parlors, bowling alleys, public dances, dance halls, boxing and wrestling matches, skating rinks, tennis courts, except as provided in subsection B of this section, video games, pinball machines, sports events or any other business charging admission or user fees for exhibition, amusement or entertainment, including the operation or sponsorship of events by a tourism and sports authority under title 5, chapter 8. For purposes of this section, admission or user fees include, but are not limited to, any revenues derived from any form of contractual agreement for rights to or use of premium or special seating facilities or arrangements.

* * *

A.R.S. § 42-5073 imposes the transaction privilege tax under the amusement classification. A.R.S. § 42-5073(B)(5) states that the tax base for the amusement classification is the

gross proceeds of sales or gross income derived from the business, except that the following shall be deducted from the tax base:

> The gross proceeds of sales or gross income derived from:
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> . . .
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> (b) Business activity that is arranged by the person who is subject to tax under this section and that is not taxable to the person conducting the activity due to an exclusion, exemption or deduction under this section or § 42-5062, but the gross proceeds of sales or gross income to be deducted shall not exceed the consideration paid to the person conducting the activity.
>
> (c) Business activity that is arranged by a person who is subject to tax under this section and that is taxable to another person under this section who conducts the activity, but the gross proceeds of sales or gross income to be deducted shall not exceed the consideration paid to the person conducting the activity.

* * *

A.R.S. § 42-5073(D) states, until December 31, 1988, the revenues from hayrides and other animal-drawn amusement rides, from horseback riding and riding instruction and from recreational tours using motor vehicles designed to operate on and off public highways are exempt from the tax imposed by this section. Beginning January 1, 1989, the gross proceeds or gross income from hayrides and other animal-drawn amusement rides, from horseback riding and from recreational tours using motor vehicles designed to operate on and off public highways are subject to taxation under this section. Tax liabilities, penalties and interest paid for taxable periods before January 1, 1989 shall not be refunded unless the taxpayer requesting the refund provides proof satisfactory to the department that the taxes will be returned to the customer.

* * *

49 U.S.C. § 40116 states, in pertinent:[2]

(a) Definition.--In this section, "State" includes the District of Columbia, a territory or possession of the United States, and a political authority of at least 2 States.

(b) Prohibitions.--Except as provided in subsection (c) of this section and section 40117 of this title, a State, a political subdivision of a State, and any person that has purchased or leased an airport under section 47134 of this title, may not levy or collect a tax, fee, head charge, or other charge on--

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[2] Section 1513 was renumbered and became § 40116 in the 1994 recodification of the U.S. Code.

(1) an individual traveling in air commerce;

(2) the transportation of an individual traveling in air commerce;

(3) the sale of air transportation; or

(4) the gross receipts from that air commerce or transportation.

(c) Aircraft taking off or landing in State. -- A State or political subdivision of a State may levy or collect a tax on or related to a flight of a commercial aircraft or an activity or service on the aircraft only if the aircraft takes off or lands in the State or political subdivision as part of the flight.

* * *

49 U.S.C. § 40102(a)(3) defines “air commerce” to mean foreign air commerce, interstate air commerce, the transportation of mail by aircraft, the operation of aircraft within the limits of a Federal airway, or the operation of aircraft that directly affects, or may endanger safety in, foreign or interstate air commerce.

* * *

49 U.S.C. § 40102(a)(5) defines “air transportation” to mean foreign air transportation, interstate air transportation, or the transportation of mail by aircraft.

* * *

49 U.S.C. § 40102(a)(6) defines “aircraft” to mean any contrivance invented, used, or designed to navigate, or fly in, the air.

* * *

49 U.S.C. § 40102(a)(20) defines “Federal airway” to mean a part of the navigable airspace that the Administrator designates as a Federal airway."

* * *

14 CFR § 1.1 defines "helicopter" as a rotorcraft that, for its horizontal motion, depends principally on its engine-driven rotors.

Discussion:

The Amusement Classification

Arizona’s transaction privilege tax is a tax on the privilege of conducting business in the State of Arizona and is imposed upon the seller or lessor, who may pass the burden of the tax on to the purchaser or lessee but is the party that remains ultimately liable to Arizona for the tax. The tax is imposed under sixteen tax classifications, with exclusions and deductions separately provided for under each classification. The amusement classification, found at Arizona Revised Statutes § 42-5063, imposes transaction privilege tax on the business of operating or conducting theaters, movies, operas, shows of any type or nature, exhibitions, concerts, carnivals, circuses, amusement parks, menageries, fairs, races, contests, games, billiard or pool parlors, bowling alleys, public dances, dance halls, boxing and wrestling matches, skating rinks, tennis courts, except as provided in

subsection B of this section, video games, pinball machines, sports events or any other business charging admission or user fees for exhibition, amusement or entertainment, including the operation or sponsorship of events by a tourism and sports authority under title 5, chapter 8. For purposes of this section, admission or user fees include, but are not limited to, any revenues derived from any form of contractual agreement for rights to or use of premium or special seating facilities or arrangements.

I.
Helicopter Tours

Federal Preemption - 49 U.S.C. § 40116

In the matter of *State of Arizona v. Cochise Airlines*, the Court of Appeals of Arizona held "... that when Congress prohibited a tax upon the carriage of persons in air commerce, it preempted the Arizona transaction privilege tax insofar as it relates to the transportation of persons."[3]

The Anti-Head Tax Act prohibits a State or a political subdivision of a State from levying or collecting a:

> . . . tax, fee, head charge, or other charge on – an individual traveling in air commerce; . . . or the gross receipts derived from that air commerce or transportation. 49 U.S.C. § 40116(b)(1), (4).

Whether Client's helicopter tours are exempt from Arizona's transaction privilege tax by virtue of the federal preemption created in 49 U.S.C. § 40116(b)(1) turns on whether Client's helicopter tour passengers are "traveling" and whether Client's helicopters operate "in air commerce."

Whether Client's Helicopter Tour Passengers are "Traveling"

A passenger-carrying, piloted helicopter tour operator carries individuals who are "traveling" under the Anti-Head Tax Act. The Anti-Head Tax Act fails to provide a definition of "traveling" or "travel." Turning to the plain meaning of "traveling," pursuant to the American Heritage Dictionary, "traveling" is defined as "to go from one place to another, as by car, train, plane, or ship; take a trip; journey: to travel for pleasure."[4]

One could argue that Client's passengers are not "traveling" within the meaning of the Anti-Head Tax Act because Client's passengers are not traveling from one place to another as the helicopter tours takeoff and land from the same location. However, on January 29,

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[3] *State of Arizona v. Cochise Airlines*, 128 Ariz. 432, 626 P.2d 596, 602 (1980).
[4] The American Heritage Dictionary (4th ed. 2006).

2010, the United States Department of Transportation ("DOT"), who is charged with administering the Anti-Head Tax Act, addressed this argument in an advisory opinion and deemed it unpersuasive. Specifically, in the January 29, 2010 advisory opinion from the U.S. Department of Transportation General Counsel *Re: Question on Taxation of Hot Air Balloon Flights* in which the General Counsel explains whether passengers in free balloon "travel," the DOT explains:

> It may be contended that hot air balloon passengers in untethered, piloted balloons do not "travel" within the meaning of the AHTA, based on an argument that the dominant purpose of a hot air balloon ride is not to go from one specific place to another specific place, but rather to provide entertainment, such as that provided by sightseeing companies. However, the AHTA nowhere mentions the purpose of a flight. Nor does it limit the definition of "travel" by specifying that one can only "travel" from one specific place to another. We decline to interpret the word "travel" as including any such limitations not found in the statute. [5]

Passengers in a piloted helicopter tour are "traveling" under the Anti-Head Tax Act.[6]

Whether Client's Helicopter Tours Operate in Air Commerce

Client's helicopter tours operate in "air commerce." For purposes of 49 U.S.C. § 40116, "air commerce" includes not only "foreign or interstate air commerce," but also "the operation of aircraft that directly affects, or may endanger safety in, foreign or interstate air commerce."[7] Here, for a helicopter to satisfy the statutory definition of "air commerce" as defined in 49 U.S.C. § 40116, the following two elements must be satisfied: (i) helicopter must satisfy the statutory definition of "aircraft" as defined in 49 U.S.C. § 40102(a)(6) and (ii) the operation of the helicopter must directly affect, or may endanger safety in, foreign or interstate air commerce.

First, a helicopter is an "aircraft" under the definition in the federal aviation statutes because a helicopter is a "contrivance invented, used, or designed to navigate, or fly in, the air."[8] In particular, the definition of "heliport" found in the Code of Federal Regulations ("CFR") lends support to the fact that helicopters are "used, or designed to navigate, or fly

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[5] Department of Transportation. *RE: Question on Taxation of Hot Air Balloon Flights*. January 29, 2010.
[6] The Wisconsin Department of Revenue revised its longstanding position set forth in sec. Tax 11.84(2)(c), Wis. Adm. Code (May 2010 Register), as the result of a recent advisory opinion by the U.S. Department of Transportation General Counsel. http://www.revenue.wi.gov/taxpro/news/101213a.html.
[7] 49 U.S.C. § 40102(a)(3).
[8] 49 U.S.C. § 40102(a)(6).

in, the air."[9] Specifically, "heliport" means an area of land, water, or structure used or intended to be used for the landing and takeoff of helicopters.[10]

Second, the operation of a helicopter may "directly affect or endanger safety in interstate commerce." As seen in *Hill v. National Transportation Safety Board,* the court demonstrated that the FAA may regulate flight activities that have the "potential" to endanger safety in interstate or overseas air commerce.[11] As a result, the statutory definition of "air commerce" as defined in 49 U.S.C. § 40102(a)(3) is satisfied and Client's helicopters operate in "air commerce."[12]

49 U.S.C. § 40116(b) & (c) – Statutory Analysis

Determining whether a tax successfully passes the Anti-Head Tax Act begins with 49 U.S.C. § 40116(b). 49 U.S.C. § 40116(b) prohibits four categories of taxes: taxes on "(1) an individual traveling in air commerce; (2) the transportation of an individual traveling in air commerce; (3) the sale of air transportation; [and] (4) the gross receipts from that air commerce or transportation."[13] The ban, however, operates "[e]xcept as provided in subsection (c)," which states that a municipality "may levy or collect a tax on or related to a flight of a commercial aircraft or an activity or service on the aircraft only if the aircraft takes off or lands in the [taxing locale]."[14]

The Arizona transaction privilege tax does not apply to Client's helicopter tours because Client's helicopter tours are within the meaning of air commerce and preempted by 49 U.S.C. § 40116(b).

II.
[Recreational Vehicle] Tours

Taxation under the Amusement Classification

Income derived from [recreational vehicle] tours is specifically subject to tax pursuant to A.R.S. § 42-5073(D). In pertinent part, A.R.S. § 42-5073(D) specifies that "[b]eginning January 1, 1989, the gross proceeds or gross income from hayrides and other animal-drawn amusement rides, from horseback riding and from recreational tours using motor vehicles designed to operate on and off public highways are subject to taxation under this section."[15] Client is properly classified under the amusement classification.

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[9] 14 CFR §1.1.
[10] 14 CFR §1.1.
[11] *Hill v. National Transp. Safety Bd.*, 886 F.2d 1275, 1279-1280 (10th Cir. 1989).
[12] 49 U.S.C. § 40102(a)(3).
[13] 49 U.S.C. § 40116(b).
[14] 49 U.S.C. § 40116(b).
[15] A.R.S. § 42-5073(D).

A.R.S. § 42-5073(B)

A.R.S. § 42-5073 imposes the transaction privilege tax under the amusement classification. A.R.S. § 42-5073(B)(5) states that the tax base for the amusement classification is the gross proceeds of sales or gross income derived from the business, except that the following shall be deducted from the tax base:

> The gross proceeds of sales or gross income derived from:
>
> . . .
>
> (c) Business activity that is arranged by a person who is subject to tax under this section and that is taxable to another person under this section who conducts the activity, but the gross proceeds of sales or gross income to be deducted shall not exceed the consideration paid to the person conducting the activity.

Taxation of Client's cost of purchasing the [Tour Company's] [recreational vehicle] tours - A.R.S. § 42-5073(B)(5)(c)

Pursuant to A.R.S. § 42-5073(B)(5)(c), Client's gross proceeds of sales or gross income derived from arranging an amusement activity in the form of [recreational vehicle] tours are deductible under the amusement classification.[16] A.R.S. § 42-5073(B)(5)(c) requires the business activity in question to be "arranged by a person who is subject to tax under [the amusement classification] and that is taxable to another person under this section who conducts the activity . . ." Here, the activity in question is [Tour Company's] [recreational vehicle] tours. A.R.S. § 42-5073(B)(5)(c) is satisfied because Client, who arranges the [recreational vehicle] tours, is subject to tax under the amusement classification and the [recreational vehicle] tours are taxable to the person under this section who conducts the activity, namely [Tour Company]. As a result, Client can deduct the actual amount it pays [Tour Company] for providing the [recreational vehicle] tours under A.R.S. § 42-5073(B)(5)(c).

III.
Picnic Foods

Taxation of Client's cost of purchasing the picnic food – A.R.S. § 42-5073(B)(5)(a)

Again, A.R.S. § 42-5073 imposes the transaction privilege tax under the amusement classification. A.R.S. § 42-5073(B)(5) states that the tax base for the amusement

[16] A.R.S. § 42-5073(B)(5)(c).

classification is the gross proceeds of sales or gross income derived from the business, except that the following shall be deducted from the tax base:

> The gross proceeds of sales or gross income derived from:
>
> (a) Business activity that is properly included in any other business classification under this article and that is taxable to the person engaged in that classification, but the gross proceeds of sales or gross income to be deducted shall not exceed the consideration paid to the person conducting the activity.
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> . . .

A.R.S. § 42-5073(B)(5)(a) of the amusement classification requires the activity to be a "business activity that is properly included in any other business classification under this article and that is taxable to the person engaged in that classification . . ." Here, the activity in question is the sale of picnic food. A.R.S. § 42-5073(B)(5)(a) is satisfied because the sale of picnic food is properly included under A.R.S. § 42-5074 of the restaurant classification and is taxable to the seller of the picnic who is subject to tax under the restaurant classification. As a result, Client can deduct the cost of purchasing the picnic food that it purchases for its customers under A.R.S. § 42-5073(B)(5)(a).

Ruling:

Based on the facts and documentation provided, the Department rules as follows:

1. ***Federal preemption - 49 U.S.C. § 40116:*** Arizona's transaction privilege tax does not apply to Client's helicopter tours because Client's helicopter tours are within the meaning of air commerce and preempted by 49 U.S.C. § 40116(b).

2. ***Taxability of [recreational vehicle] tours:*** [Recreational vehicle] tours are subject to Arizona's transaction privilege tax pursuant to A.R.S. § 42-5073(D) of the amusement classification because the gross proceeds of sales or gross income derived from recreational tours using motor vehicles designed to operate on and off public highways are subject to taxation under the amusement classification.

3. ***Taxation of Client's cost of purchasing [Tour Company's] [recreational vehicle] tours:*** Client can deduct the actual amount it pays [Tour Company] for providing the [recreational vehicle] tours under A.R.S. § 42-5073(B)(5)(c) because Client, who arranges the [recreational vehicle] tours, is subject to tax under the amusement classification and the [recreational vehicle] tours are taxable to the person under this section who conducts the activity, namely [Tour Company].

4. ***Taxation of gross proceeds from picnic food:*** Client can deduct its cost of purchasing the picnic food that it provides to its customers under A.R.S. § 42-5073(B)(5)(a) because the sale of picnic food is properly included under A.R.S. § 42-5074 of the restaurant classification and is taxable to the seller of the picnic who is subject to tax under the restaurant classification.

The conclusions in this taxpayer information ruling do not extend beyond the facts presented in your correspondences dated June 3, 2011, July 27, 2011, and September 19, 2011.

This response is a taxpayer information ruling (TIR) and the determination herein is based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the Department's making of an accurate determination, this taxpayer information ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law, or notification of a different Department position.

If the Department is provided with required taxpayer identifying information and taxpayer representative authorization before the proposed publication date (for a published TIR) or date specified by the Department (for an unpublished TIR), the TIR will be binding on the Department with respect to the taxpayer that requested the ruling. In addition, the ruling will apply only to transactions that occur or tax liabilities that accrue from and after the date the taxpayer receives the ruling. The ruling may not be relied upon, cited, or introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the taxpayer information ruling. If the required information is not provided by the specified date, the taxpayer information ruling is non-binding for the purpose of abating interest, penalty or tax.