

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:) OTA Case No. 18053102
JET SOURCE, INC.)
) CDTFA Case IDs: 959564, 959568, 959571,
) 959575, 959578, 959581, 959588, 959591,
) 959593, 959595, 959596, 959598

OPINION

Representing the Parties:

For Appellant:	Janet L. Pass, Attorney at Law
For Respondent:	Stephen Smith, Tax Counsel IV Jason Parker, Chief of Headquarters Ops.

M. GEARY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Jet Source, Inc. (appellant) appeals an April 25, 2018 Decision issued by California Department of Tax and Fee Administration (respondent¹) denying appellant’s petition for redetermination of 12 Notices of Determination (NODs), which assessed a total of \$223,925.00 additional tax, plus applicable interest, for the 12 quarters commencing April 1, 2013, and ending March 31, 2016 (liability period), and also denying appellant’s claim for refund of \$164,067.95 for the 10 quarters commencing October 1, 2013, and ending March 31, 2016.

Office of Tax Appeals (OTA) Administrative Law Judges Michael F. Geary, Josh Aldrich, and Richard Tay held an electronic oral hearing for this matter on June 15, 2021.² At the conclusion of the hearing, the parties submitted the matter, and we closed the record.

¹ Sales and use taxes (and other business taxes and fees) were formerly administered by the State Board of Equalization (BOE). In 2017, the California Legislature transferred functions of the BOE relevant to this case to respondent. (Gov. Code, § 15570.22.) The effective date of the transfer of all but adjudicatory functions was July 1, 2017. (Adjudicatory functions were transferred to the Office of Tax Appeals effective January 1, 2018.) When this Opinion refers to events that occurred before July 1, 2017, “respondent” refers to BOE.

² Appellant requested an oral hearing in Cerritos. However, OTA temporarily suspended live hearings to comply with restrictions in effect to minimize the spread of COVID-19. The parties agreed to this electronic hearing process, which allows audio and video participation in real time using a web-based application.

ISSUE

Is appellant entitled to an adjustment to the amount of disallowed claimed credits for sales tax prepaid to fuel distributors?³

FACTUAL FINDINGS

1. Appellant is a California corporation and an aircraft jet fuel (jet fuel) wholesaler and dealer.
2. On August 1, 2011, appellant entered into a 10-year hangar lease (lease) with Tango Air Inc., dba Schubach Aviation (Schubach). The lease provided that Schubach would purchase jet fuel “in conjunction with” appellant, that the jet fuel would be stored at appellant’s facility, and that Schubach would pay appellant a pumping fee.⁴
3. Appellant purchased jet fuel from Epic Aviation, LLC (Epic). Epic issued invoices to appellant. The Epic invoices showed the price per gallon paid by appellant, as well as the itemized amounts of prepaid sales tax and other taxes, fees, and surcharges.
4. Appellant sold jet fuel, as a jet fuel dealer, to jet fuel users. Appellant also either sold jet fuel, as a jet fuel wholesaler, to Schubach, or appellant provided jet fuel to Schubach pursuant to their agreement to jointly purchase the fuel. Schubach, a jet fuel dealer, resold the jet fuel at retail to its customers.
5. Appellant billed Schubach per calendar month for jet fuel withdrawn by Schubach from appellant’s fuel storage facility. The amount appellant charged Schubach for jet fuel was exactly equal to the amount Epic charged appellant for the jet fuel, including prepaid sales tax and other taxes, fees, and surcharges.
6. Appellant issued invoices to Schubach for all jet fuel purchases. Appellant’s invoices to Schubach stated the total number of gallons sold and the total price charged. Appellant’s invoices did not itemize the various components of the price Epic charged to appellant. However, to support the amounts charged for jet fuel sold to Schubach, appellant also gave Schubach copies of Epic’s invoices to appellant.

³ Generally, and as relevant here, a jet fuel dealer is any person who sells to a jet fuel user, either by delivering jet fuel in this state into the fuel tanks of aircraft or by delivering it into a storage facility from which the fuel is withdrawn for use in aircraft (R&TC, § 7388), and a jet fuel wholesaler is a person who deals in jet fuel who is not a jet fuel dealer (R&TC, § 6480(d)).

⁴ The pumping fee was \$0.25 per gallon if Schubach purchased over 60,000 gallons of jet fuel per calendar month and \$0.35 per gallon if Schubach did not meet that threshold.

7. At all relevant times, fuel wholesalers were required to obtain from respondent a permit with an “SG” prefix in addition to a regular sales tax permit. Schedule A of the SG return is used to report taxable removals, entries, or sales of fuel, and Schedule B of the SG return is used to report sales taxes prepaid to other wholesalers or suppliers. Appellant did not have the required “SG” account during the liability period. Consequently, appellant could not report on Schedule A the prepaid sales tax it owed on its sales of jet fuel to Schubach, or claim the credits for the prepaid sales tax to Epic on Schedule B.
8. For the liability period, appellant claimed (on Schedule G of its sales and use tax returns) a deduction of \$554,047 for prepaid sales tax, which amount included \$223,925 attributable to sales to Schubach.⁵
9. Respondent determined that appellant’s claimed deduction for prepaid sales tax relating to sales to its retail customers should be allowed, but that appellant’s claimed deductions for prepaid sales tax relating to appellant’s sales to Schubach should be disallowed. By letter dated May 4, 2016, respondent informed appellant regarding this determination.
10. On May 26, 2016, respondent issued to appellant 12 NODs for a total of \$223,925 tax, plus accrued interest, for the 12 quarters constituting the liability period.
11. On June 23, 2016, appellant filed a petition for redetermination, disputing the entire liability.
12. On June 27, 2017, respondent levied \$164,067.95 from appellant’s bank account and applied this amount to the subject tax liabilities.
13. Appellant filed a claim for refund for \$164,067.95, asserting that that bank levy was issued in error.
14. By email sent February 23, 2018, respondent conceded that the bank levy was issued in error.
15. Respondent issued its April 25, 2018 Decision granting the claim for refund but denying the petition for redetermination. This appeal followed.

⁵ Schubach also claimed deductions for prepaid sales tax on Schedule G of its sales and use tax returns for its purchases of jet fuel from appellant, identifying Epic as the wholesaler for these transactions, and respondent allowed the deductions. Appellant’s arguments are intertwined with the assertion that respondent wrongfully allowed Schubach the benefit of the prepaid sales tax credit. Schubach’s liability is not before us, and we need make no finding regarding it.

DISCUSSION

A wholesaler of jet fuel is required to collect a prepayment of the retail sales tax from the person to whom the jet fuel is sold and to give the buyer evidence of the collection of the prepaid amounts. (R&TC, § 6480.1(b)(1).) Such prepayment constitutes a debt owed by the wholesaler to respondent until sales tax is paid to respondent by the jet fuel dealer who makes the retail sale of that jet fuel (for which the prepayment was made), or until use tax is paid to respondent by a subsequent (in the delivery chain) jet fuel wholesaler or retailer who consumes that jet fuel prior to resale. (R&TC, § 6480.1(a).) The amount of a prepayment by a dealer who makes the retail sale of the jet fuel and reports sales tax due measured by the retail sale price of the fuel, or by a subsequent wholesaler or retailer who consumes the jet fuel before resale and reports use tax due measured by its cost, constitutes a credit against the use tax or sales tax due, in the period in which the consumption or retail sale occurs.⁶ (R&TC, § 6480.1(d).) These procedures essentially provide the state with some security for the payment of sales or use tax with the burden of the prepayment being passed from the initial supplier, through the chain of wholesalers, and ultimately to the dealer who makes the retail sale of the jet fuel and reports tax due on that sale, or to the wholesaler or retailer who consumes the jet fuel prior to resale and reports tax due on that use. There is no provision in the Sales and Use Tax Law that allows a wholesaler to claim a credit for jet fuel sales tax prepayments unless the wholesaler reports use tax due on its consumption of the jet fuel before resale.

Appellant contends that it was entitled to take a credit for tax prepaid to Epic when appellant filed its sales and use tax returns reporting its sales to Schubach. Appellant's argument is based on appellant's factual assertion that it prepaid sales tax to Epic but did not collect prepaid sales tax from Schubach. Appellant argues that, although the price it charged to Schubach was exactly the same as the price paid to Epic, there is no mention of sales tax in either the hangar contract or the invoices appellant issued to Schubach. Citing R&TC section 6012 and Civil Code section 1656.1, appellant asserts that just as a taxpayer must establish that sales tax has been included in reported gross receipts to be entitled to deduct the included tax, respondent should not be allowed to infer that Schubach prepaid sales tax to appellant based solely on the fact that appellant's acquisition cost and its sales price were the same. It argues that the evidence

⁶ In the case of a retailer, additional sales tax would typically be due because the prepayment is measured by the retailer's cost and does not include its markup.

must show that Schubach prepaid sales tax by establishing one or more of the conditions specified in Civil Code section 1656.1: (1) that the sales agreement expressly provided for the addition of prepaid sales tax; (2) that sales tax reimbursement is shown on the proof of sale, in this case the invoice issued to Schubach; (3) that appellant had posted in its premises in a location visible to Schubach a notice to the effect that prepaid sales tax will be added to the sales price; or (4) that the inclusion or addition of prepaid sales tax was indicated on a price tag or in an advertisement or other printed material directed to Schubach. Appellant contends that the absence of any of these conditions here compels the conclusion that Schubach did not prepay sales tax on its purchases of fuel, and thus appellant, who did prepay sales tax, was the one entitled to claim the prepayment credit. Finally, in reply to respondent's argument that appellant cannot claim a prepaid sales tax credit because it was not a retailer who reported sales tax due on the sale of the fuel to Schubach or a consumer of the jet fuel who reported use tax on such consumption, appellant argues that the statute also allows a seller to claim the credit when the sale is exempt, apparently suggesting that this is what occurred here.

We first address appellant's final point. Although R&TC section 6480.1 does state that "motor vehicle fuel sold by a supplier or wholesaler to a qualified purchaser who, pursuant to a contract with the State of California or its instrumentalities, resells that fuel to the State of California or its instrumentalities shall be exempt from the prepayment requirements," that provision has no application to our facts. We conclude that, as relevant here, section 6480.1 clearly limits the credit for prepaid sales tax to the retailer who reports sales tax due on the sale of the fuel or to a wholesaler or retailer who consumes the fuel before reselling it and reports use tax on such consumption. Appellant is neither. On this basis alone, we find that appellant was not entitled to claim the deductions or credits for prepaid sales tax. Although this finding is dispositive, below we will address appellant's other arguments.

The parties agree that appellant was acting as a jet fuel wholesaler when it made the sales to Schubach and that those sales were for resale. R&TC section 6480.1(d) does not give jet fuel wholesalers the option of collecting prepaid sales tax. It states that the wholesaler "shall collect" it. Collection is mandatory. On this basis, we find unpersuasive appellant's argument that it chose to not collect prepaid sales tax from Schubach.

Regarding appellant's argument that the evidence must show that Schubach prepaid sales tax by establishing one or more of the conditions specified in Civil Code section 1656.1, we note

first that 1656.1 does not apply to these facts. Section 1656.1 specifically refers to sales tax reimbursement. The collection of sales tax reimbursement by a retailer is optional and depends on the terms of the agreement of sale. As explained above, a wholesaler's collection of prepaid sales tax on sales of jet fuel is mandatory. Second, and as previously noted, we are not concerned here with the question of whether respondent's allowance of prepaid tax credits to Schubach was correct. The issue is whether respondent's disallowance of appellant's claim to a deduction for prepaid sales tax was incorrect. Finally, appellant's assertion that respondent presumed Schubach's payment of prepaid sales tax is not supported by the evidence, which shows that by agreement between appellant and Schubach, appellant fulfilled its mandatory duty to collect prepaid sales tax from Schubach. Appellant identified the components of the price charged to Schubach by sending Schubach the corresponding Epic invoice(s) to show how the total price, which was the only amount referred to on appellant's invoices, was calculated. That is persuasive evidence that appellant, with Schubach's agreement, collected prepaid sales tax from Schubach.

Our conclusion that Schubach prepaid appellant for sales tax would be the same if we interpret the lease language governing fuel purchases to indicate that appellant made fuel purchases jointly with Schubach to the extent Schubach later withdrew the fuel. The evidence shows that the parties negotiated lease terms that included their agreement that appellant and Schubach would jointly purchase jet fuel from Epic. The printed form of the lease stated that Schubach would purchase its fuel "direct from Supplier."⁷ However, the parties changed the terms to state that Schubach would purchase fuel "in conjunction with" appellant. We do not accept appellant's representation that the new language meant only that appellant would sell fuel to Schubach. The parties to the lease easily could have written that language into the lease if that was their intent. The language chosen by the contracting parties and the subsequent billing practices employed by appellant indicate that the parties to the lease agreed appellant would be buying jet fuel on Schubach's behalf, paying the cost, and subsequently recovering the cost, including prepaid sales tax, from Schubach. As already stated, above, the evidence shows that appellant collected prepaid sales tax from Schubach.

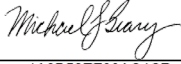
⁷ It does not appear that "Supplier" is defined in the lease.

HOLDING

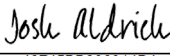
Adjustments to the amount of disallowed claimed credits for sales tax prepaid by appellant in connection with purchases of jet fuel resold to Schubach, a jet fuel dealer, are not warranted.

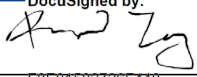
DISPOSITION

Respondent’s action is sustained.

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Michael F. Geary
Administrative Law Judge

We concur:

DocuSigned by:

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Josh Aldrich
Administrative Law Judge

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Richard Tay
Administrative Law Judge

Date Issued: 8/17/2021