

US-DIST-CT, [74-1 USTC ¶16,135], U. S. District Court, East. Dist. Ark., West. Div., **Petit Jean Air Service, Inc., Plaintiff v. The United States of America, Defendant , Transportation of persons (air) tax: Lessee operation: Refunds: Consent.--**, (Feb. 07, 1974)

[74-1 USTC ¶16,135] **Petit Jean Air Service, Inc., Plaintiff v. The United States of America, Defendant**  
U. S. District Court, East. Dist. Ark., West. Div., LR-71-C-216, 2/7/74

[Code Secs. 4261 and 6415]

**Transportation of persons (air) tax: Lessee operation: Refunds: Consent.--**Since the leasing of an aircraft by an individual was a nontaxable activity, revenue derived by the taxpayer was not payment for the transportation of persons, and was not taxable. However, with respect to other users of the aircraft, the revenue did constitute payment for transportation. In regard to the excise taxes collected on these payments for transportation, the taxpayer's refund suit was denied. The taxpayer failed to show that it had repaid the taxes collected to the aircraft users or that it had obtained their consents to bring a refund suit. BACK REFERENCES: ETR ¶2366.56 and ETR ¶5498.01.

### **Memorandum Opinion**

HENLEY, District Judge:

This is an action brought by Petit Jean Air Service, Inc., a dissolved Arkansas corporation, against the United States to secure a refund of federal excise taxes collected under the provisions of section 4261 of the Internal Revenue Code, 26 U. S. C. A., section 4261, and related statutes. The suit period includes most of 1964 and all of calendar years 1965 through 1971. Timely claims for refunds have been filed and denied.

The cause has been submitted on the pleadings, as amended, a stipulation of facts with exhibits thereto, an affidavit with exhibits executed by the late Winthrop Rockefeller, former Governor of Arkansas, the deposition of Craig M. Smith, former Administrative Assistant to Mr. Rockefeller, and memorandum briefs.

The principal issue in the case is whether revenues derived by plaintiff during the suit period for the use of certain jet aircraft by Mr. Rockefeller and others constituted "payments for transportation" which were taxable under section 4261. The record also presents an alternative and subordinate issue that will be stated in due course.

The litigation arises out of the well known fact that Governor Rockefeller had many and varied business and personal interests all over the United States, and that in the furtherance of those interests he was an extensive traveler by air.

In early 1964 Mr. Rockefeller, who had not then elected Governor of Arkansas, was the owner of a Sabreliner executive jet aircraft which was used by him, by relatives of his, by business associates, and by others. Such use of the aircraft inevitably exposed Mr. Rockefeller to very substantial personal liability in the event of accident to the craft while in flight, and he was understandably and legitimately interested in insulating himself insofar as possible from such personal liability.

With that end in view, he caused plaintiff corporation to be organized in February 1964 with himself as sole stockholder. Craig M. Smith was the president of the corporation. The other officers were George Eremea, Mr. Rockefeller's chief pilot, and Tom Downie and Marion Burton, who were attorneys residing in Little Rock, Arkansas.

The aircraft was leased to the corporation for a term of ten years. Under the terms of the lease, plaintiff was to pay to Mr. Rockefeller the sum of \$120,000 per year for the use of the plane for a period of five years, and \$80,000 per year for the remainder of the term of the lease. Those rentals were calculated so that over the period of the lease the lessor would be able to recover the cost of the plane.

The lease remained in effect until sometime in 1966 when the plane was purchased from Mr. Rockefeller by the corporation. It was contemplated that the corporation would sell that particular plane and would use the proceeds

of the sale to apply on the purchase price of a newer and larger Falcon jet. That plan was carried out. The acquisition of the new plane required funds in addition to those derived from the sale of the Sabreliner, and Mr. Rockefeller advanced the necessary money to the corporation which in consideration of the advance issued additional stock in his favor. According to the deposition of Mr. Smith, the original Falcon jet was disposed of in 1968 or 1969, while Mr. Rockefeller was Governor, and another one was acquired. That transaction called for another advance from Mr. Rockefeller, and the advance was made and still more stock in the corporation was issued in Mr. Rockefeller's name and delivered to him.

The primary function of the corporation was to operate and maintain the jet aircraft, but it performed certain other functions as well. One of the subsidiary functions of the corporation was to operate the Petit Jean, Airport, a small airport located on Petit Jean Mountain in Conway County, Arkansas, adjacent to Mr. Rockefeller's private estate, Winrock Farms. The jet aircraft, and certain other aircraft owned or controlled by Mr. Rockefeller were based at the airport just mentioned and all of the planes were serviced and maintained by the corporation.

The airport was located on property belonging to the State of Arkansas, and the corporation had a contract with the State relating to the airport. The corporation did somewhat more business than maintain and operate "Rockefeller" aircraft. It provided take-off and landing facilities for anyone who desired to use the airport, and it sold aircraft fuel. The airport had no control tower or radar equipment, but it did have two-way radio equipment which made possible communications with flying planes.

The corporation employed the pilots who operated the jets and also had two or three other employees. The corporation had the authority to hire and fire employees, including pilots, except that no pilot could be employed without "meeting" Mr. Rockefeller; that is to say, no pilot could be employed by the corporation without being approved by Mr. Rockefeller. The corporation undertook to have on the payroll at all times three qualified jet pilots, and the jets were always staffed with two pilots in the course of flights on which Mr. Rockefeller or members of his immediate family were aboard.

The corporation was not organized with profit in view. It was hoped, however, that by charging rental fees for the use of the jets, the corporation could make operating expenses and cover depreciation costs.

If that object was to be accomplished, and it was not accomplished except with respect to two years of the life of the corporation, it was necessary to keep the jets flying and to derive revenue from the flights. That revenue came from hourly rental fees charged by the corporation to users of the aircraft, including Mr. Rockefeller and members of his family.

During the suit period the jets were extensively used. Naturally, Mr. Rockefeller was the principal user. Substantial use of the planes was made by Winrock Farms, a partnership in which Mr. Rockefeller was the principal partner. The jets were also used from time to time by Mr. Rockefeller's brothers, Nelson and Laurance Rockefeller. Some use of them was made by the National Conference of Christians and Jews and by Colonial Williamsburg, both of which were charities in which Mr. Rockefeller was interested. There was some use by Petit Jean Attractions, Inc., a corporation wholly owned by Mr. Rockefeller. And the jets were used by a number of other persons and entities who and which may not improperly be called "outsiders."

All users of the jets paid same fees. The hourly charge from January 1966 through January 1968 was \$800; for February 1968 the rate was \$850; the rate was \$900 an hour from March 1968 through June 1970 when it was lowered to \$595.

Exhibit A to the affidavit of Mr. Rockefeller identifies the users of the jets during the period with which the Court is concerned, and reflects how much each user paid for his or its use. It appears that during the early years of the planes' use there were comparatively few "outside users." The number of such users increased substantially during 1969 and 1970; there was a decline in "outsider" use during 1971. The following table shows total revenues of plaintiff derived from uses of the jets, and the amounts paid by Mr. Rockefeller personally during each year of the suit period.

Total	Rockefeller
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Year	Revenue	Payment
1964 . . . .	\$145,364.50	\$118,328.75
1965 . . . .	286,100.00	215,450.00
1966 . . . .	236,625.75	210,340.00
1967 . . . .	355,940.00	334,660.50
1968 . . . .	293,155.60	209,923.00
1969 . . . .	894,918.40	539,726.40
1970 . . . .	409,355.33	314,466.60
1971 . . . .	162,934.20	146,741.50

Exhibit C to the Rockefeller affidavit shows that the corporation sustained substantial operating losses during each year of its existence, except 1966 and 1967. In 1966 there was a profit of \$13,202.53, but the corporate revenues for that year included a \$25,000 prize award on account of the jet's having set a trans-Atlantic speed record. The profit in 1967 was only \$6,377.96. Losses ranged from a low of \$6,906.00 in 1965 to a high of \$155,302.00 in 1971.

Since he was plaintiff's only stockholder, Mr. Rockefeller was in control of the affairs of the corporation, and in that sense he had control at all times of the use of the jets and of other aircraft belonging to the corporation. According to Mr. Smith, Mr. Rockefeller was much attached to the jets and referred to them as "his" planes. If an "outsider" desired to make use of one of the jets, he would be permitted to do so if he was financially responsible, if his use did not interfere with Mr. Rockefeller's plans, and if Mr. Rockefeller wanted the applicant to have the use of the plane.

For a number of years the corporation did not collect transportation taxes from users of the plane. However, in the spring of 1969 an Internal Revenue Agent audited the affairs of plaintiff and took the position that the fees charged users of the jets were payments for transportation and taxable under section 4261. Plaintiff requested a formal Ruling from the Internal Revenue Service, and the determination of the Internal Revenue Agent was upheld. That Ruling has been published as Rev. Rul. 70-325, 1970-1 Cum. Bull. 231.

As of September 30, 1969, plaintiff filed delinquent and paid transportation taxes shown by the returns to be due. Thereafter, plaintiff began to collect the tax from users of the aircraft, including Mr. Rockefeller, and duly remitted the collections to the Government.

In the fall of 1971 due to continuing losses arising out of the operation of the jet then owned by the corporation and tightened federal regulations dealing with the operation of the aircraft, it was decided that operation of the plane then owned by plaintiff would be discontinued, and that the corporation would be dissolved. The dissolution took place on November 1, 1971, three days after the filing of this suit.<sup>1</sup>

I. Section 4261 of the Internal Revenue Code imposes an excise tax on "the amount paid within the United States for taxable transportation (as defined in section 4262) of any person by air. . . ." Insofar as here applicable, section 4262 defines transportation as being transportation that begins and ends in the United States or in the "225-mile zone" defined in the Act of July 25, 1956, P. L. 84-796, 70 Stat. 644.

The Court finds that all of the uses of the jets with which the Court is concerned constituted "transportation" as defined in section 4262, and that none of the exemptions appearing in the relevant statutes is available to the plaintiff.

As heretofore indicated, the basis question in the case is whether the payments made to plaintiff by the several users of the jets were payments for transportation within the meaning of section 4261. The plaintiff contends that they were not; the Government contends that they were.

An alternative contention of the Government is that in any event plaintiff has no standing to recover refunds with respect to taxes collected from users of the planes, except Mr. Rockefeller, after September 1969 because plaintiff has neither repaid the sums collected to the users nor has it obtained their consent to plaintiff obtaining the refunds

as provided by section 6415 of the Code.

II. With respect to the basis question above stated, the position of plaintiff is that the users of the jets “leased” them from plaintiff, and that payments made to the lessor by the lessee of an aircraft are not taxable under section 4261.

It appears from IRS Rulings cited by counsel for plaintiff that the Service does not consider payments for the use of an aircraft to be taxable payments for transportation where the contract between the owner and user amounts to a bona fide and actual lease of the plane. Counsel for Government does not appear to challenge that proposition. The position of the Government is that the jets were not “leased” to the users, and that the payments made by the users, including Mr. Rockefeller, were amounts paid for taxable transportation by air and were covered by section 4261.

As to the use of the plans by Mr. Rockefeller himself, counsel for the Government appears to be of the opinion that counsel for plaintiff is seeking to have the Court disregard the corporate entity of plaintiff and to view the situation as though Mr. Rockefeller had simply been flying in his own plane and bearing the expenses of his flights. The Court agrees with counsel for the Government that such an argument would be unsound. See: *National Carbide Corporation v. Commissioner of Internal Revenue*, 1949, [49-1 USTC ¶9223] 336 U. S. 422; *Moline Properties v. Commissioner of Internal Revenue*, 1943, [43-1 USTC ¶9464] 319 U. S. 436; *Northern Natural Gas Co. v. Commissioner of Internal Revenue*, 8 Cir., 1966, [66-2 USTC ¶9508] 362 F. 2d 781; *Omaha Public Power District v. O’Malley*, 8 Cir., 1956 [56-1 USTC ¶9503] 232 F. 2d 805; *Omaha Public Power District v. O’Malley*, 8 Cir., 1954, [54-2 USTC ¶49,071] 216 F. 2d 764.

It is clear, however, from a letter to the Court from counsel for plaintiff submitted in lieu of a reply brief that plaintiff is not making the argument that the Government postulates. In that letter counsel says:

“1. The issue in *not*, as the Government states, whether the plaintiff’s corporate existence should be disregarded. The issue is whether Mr. Rockefeller, his relatives his friends, and his business associates have rented an airplane (not taxable) or paid for air transportation (taxable).”

The basic question appears to be one of first impression as far as the courts are concerned, and the Court agrees with the Government that cases decided with reference to efforts of the IRS in years prior to the passage of the Internal Revenue Act of 1951 to impose the tax on characters of sports fishing boats are not applicable to this case. See: *Smith v. United States*, N. D. Fla., 1953, [53-1 USTC ¶9332] 110 F. Supp. 892; *Abbott v. United States*, Ct. Cl., 1959, [59-2 USTC ¶15,249] F. Supp. 917.

III. As to the characterization of the payments made for the use of the jets, the burden is on the plaintiff to show that the payments were in consideration of leases or rentals of the aircraft and were not merely payments for transportation.

The Court finds and concludes that the plaintiff had discharged its burden with respect to the payments made by Mr. Rockefeller and Winrock Farms, but has failed to discharge it with respect to other users of the aircraft.

The question before the Court is somewhat obscured by the semantical consideration that any person who is transported, otherwise than gratis, in a conveyance from one place to another is “paying for transportation” whether he is driving his own automobile or flying his own plane, or whether he is renting or leasing the conveyance in which he is transported, or whether he is simply a fare paying passenger on a conveyance owned and operated by some other person or entity.

The contracts for the use of the jets with which the Court is concerned were oral, and there is no reason to believe that the parties used any particular verbal formula to express their agreements. Such being the case it is the duty of the Court to determine the actual intent of the parties to the respective contracts as manifested objectively. If the parties intended a given agreement for the use of one of the jets to constitute a lease, and if the transaction was characterized by the objective attributes of a lease, notably the right to possess, use, and control the aircraft during the life of the agreement, the inference is justified that the agreement was in fact one of lease or bailment, and that the user’s payment for such use was not mere payment for transportation taxable under section 4261. On the other

hand, if the parties did not actually intend for the plane to be leased to the user and if the transaction did not have the attributes that have been mentioned, then it would appear that the user was simply paying for transportation.

In characterizing the contracts with which the Court is concerned regard must be had to a number of factors including the relationship between the contracting parties and the nature and value of the aircraft.

As far as Mr. Rockefeller's uses of the jets are concerned, his position as sole owner of the stock in plaintiff corporation, while not in itself of controlling importance, is certainly relevant as bearing on the willingness of the corporation to lease the planes to him, on his willingness to lease the planes from the corporation, and on his right to possession and control of the planes during the lease periods.

With respect to right of control, Mr. Rockefeller would not have had any right, and presumably would not have had any desire, to control the pilot and co-pilot in actual flight so as to endanger the plane and the lives of those on it, or to substitute his judgment for that of crew members in areas necessarily reserved to their skill and discretion. But, apart from those limitations it would appear to the Court that during a given period of his use Mr. Rockefeller's right of control with respect to the plane and its crew would have been essentially absolute. It would have been, and doubtless was, within his power to prescribe destinations, routes, and times of departure, and he also would have had the right, subject to the discretion of the pilot and co-pilot, to exercise at least some control over the actual flying of the aircraft.

In the circumstances the Court is willing to infer and now finds that the contracts between plaintiff and Mr. Rockefeller were actual and bona fide contracts of lease, and that his payments for the use of the plane were not taxable under section 4261.

The Court also draws the same inference and makes the same finding with respect to payments made by Winrock Farms; the Court considers that contracts between plaintiff and Winrock Farms were essentially contracts between plaintiff and Mr. Rockefeller.

As to the other users of the plane, including Mr. Rockefeller's brothers, the Court is not persuaded by a preponderance of the evidence that their payments were other than simple payments for transportation in the planes, and the Court holds that their payments were taxable.

IV. The Government's contention based on section 6415 of the Code can be disposed of with little discussion.

Section 6415(a) provides that credit or refund of any overpayment of tax imposed by section 4261 may be allowed to the person who collected the tax and paid it into the Treasury if such person establishes either that he has repaid the tax to the person from whom he collected it or that such person has consented to the allowance of such credit or refund.

Since plaintiff did not collect the transportation tax from users prior to the end of September 1969, the applicability to the case of section 6415 is limited to the last quarter of 1969 and to 1970 and 1971.

Mr. Rockefeller died in the spring of 1973, and in June of that year one of his executors executed a consent to plaintiff obtaining refunds of the taxes collected from Mr. Rockefeller. However, the record does not establish with respect to other users, including Winrock Farms, that plaintiff has either repaid to such other users the taxes collected from them or that plaintiff has obtained their consent that plaintiff collect the refunds. Therefore, as far as the other users are concerned, plaintiff would not in any event be entitled to refunds with respect to the taxes collected from such users.

A judgment will be entered in favor of the plaintiff with respect to all uses of the plane charged to Mr. Rockefeller personally and with respect to all uses charged to Winrock Farms prior to the time at which plaintiff began to collect the transportation tax from that partnership. In all other respects plaintiff's complaint, as amended, will be dismissed. The Court expresses no opinion as to whether plaintiff can now comply with section 6415 as far as Winrock Farms is concerned.

Counsel should have no difficulty in framing an appropriate judgment, and when that has been done, it should be

submitted to the Court for signature and entry.

### **Order**

For good cause shown it is Ordered that the Court's Memorandum Opinion filed in this cause on February 4, 1974, be, and the same hereby is, amended as follows:

The second sentence of the last paragraph on page 3 of the opinion is amended so as to read: "Substantial use of the planes was made by Winrock Farms, a sole proprietorship owned by Mr. Rockefeller."

The fourth and fifth paragraphs of Section IV of the opinion are amended so as to read:

"Mr. Rockefeller died in the spring of 1973, and in June of that year one of his executors executed a consent to plaintiff obtaining refunds of the taxes collected from Mr. Rockefeller and from Winrock Farms. However, the record does not establish with respect to other users that plaintiff has either repaid to such other users the taxes collected from them or that plaintiff has obtained their consent that plaintiff collect the refunds. Therefore, as far as the other users are concerned, plaintiff would not in any event be entitled to refunds with respect to the taxes collected from such users.

"A judgment will be entered in favor of the plaintiff with respect to all uses of the plane charged to Mr. Rockefeller and to Winrock Farms. In all other respects plaintiff's complaint, as amended, will be dismissed."

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<sup>1</sup> No contention is made that the dissolution of the corporation affected the maintenance of this action in the corporate name.