



# New IRS audit campaign prepares to take flight



The Internal Revenue Service (IRS) Large Business and International (LB&I) Division's announcement of a new audit campaign related to personal use of business aircraft has put a spotlight on the myriad tax issues associated with owning or leasing aircraft used for both business and personal travel. Navigating complex tax rules and maintaining records creates challenges for owners and employers as well as individuals who use the aircraft for personal travel.

## IRS audits of business aircraft

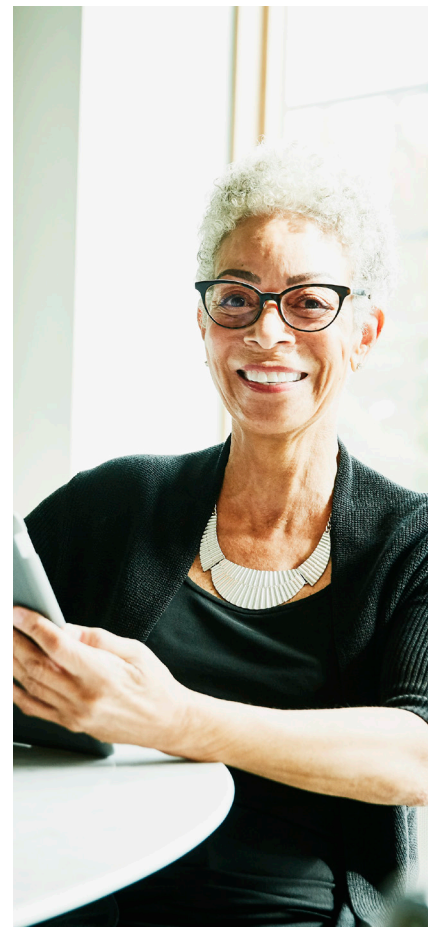
- The KPMG Tax Controversy & Dispute Resolution practice has decades of experience assisting clients through the audit process, including reviewing and responding to IRS inquiries in this area.
- It appears that initial audits in this campaign will start at an entity level but may lead to individual income and employment tax audits.

## Potential compliance issues



### Imputed income for personal flights

- US tax rules require that income be imputed in connection with personal use of a business aircraft by individuals who provide services to the organization.
- Complex rules exist to determine the value that must be included in compensation and whether the value of the flight will be taxable to the employee and/or other passengers, generally requiring use of either the Fair Market Value (Charter Rate) Method or the Standard Industry Fair Level (SIFL) Method flight, with certain exceptions.
- Companies should have a policy in place to address these issues and facilitate adequate recordkeeping.





## Depreciation

- Business assets generally may be depreciated; however, calculating depreciation for aircraft can be complex and depend on a number of factors.
- Availability of bonus depreciation or accelerated depreciation is subject to complex rules and depends upon factors such as level of qualified business use and domestic versus international travel.



## Deduction disallowance and limitations

- A business typically may deduct reasonable expenses of maintaining an asset, such as a corporate jet, utilized for a business purpose; however, the use of a company aircraft must be allocated between business use and personal use.
- Personal use may impact the business's eligibility to deduct costs related to personal travel, even if treated as taxable compensation to the employee. In addition, expenses related to air travel that are determined to be for "business entertainment" are also not deductible to the extent not included in the employee's income.



## Federal excise tax

- Excise tax is imposed on amounts paid for domestic and international air transportation of persons and domestic air transportation of property.
- While the tax generally applies to amounts paid to scheduled airlines and companies that provide charter aircraft, it may also apply with respect to amounts paid to operators of "noncommercial" aircraft.

## Other considerations

While less likely to present exposure on audit, there are many other considerations around owning, leasing, and usage of business aircraft that could significantly impact current and future tax implications for employers and individuals, such as:



## Preacquisition considerations

- Ownership versus leasing
- Timing of acquisition and impact on qualified business use/available depreciation methods
- Implications of anticipated international travel
- Potential state tax implications of ownership
- Use of a leasing entity and implications for depreciation deductions as well as liability for SIFL considerations and deduction limitations





## State and local indirect tax considerations

- Sales and use tax considerations vary state to state.
- Aircraft transactions, such as ownership transfers, leases, and fractional ownership, can give rise to unintended indirect tax consequences without proper planning and documentation.
- Owners should identify, evaluate, and document relevant exemptions (such as resale, fly-away, occasional sale, commercial airlines, use in interstate commerce, agricultural use, government use, etc.).
- Property tax considerations can be complex, including with respect to assessed value, location, transaction timing, and the availability of exemptions or abatements for certain types of aircraft or uses.



## Charitable use

- Charitable deductions may be available but limited to the variable costs of charitable flights.
- Charitable use of aircraft may also result in associated record-keeping and reporting requirements.



## Business-oriented security concerns

- The tax treatment of personal travel may differ when the employer-provided aircraft is used in response to a bona fide business-oriented security concern related to the employee.
- Whether these special rules may apply generally requires a separate third-party analysis.



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