STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	**4/25/01**	Bill No:	**AB 243**
Tax:	**Sales and Use**	Author:	**Runner**
Board Position:	**Neutral**	Related Bills:	

BILL SUMMARY

This bill would provide a partial sales and use tax exemption for sales of aircraft jet fuel sold to an aircraft jet fuel user at any airport that is located within an enterprise zone.

ANALYSIS

Current Law

Under existing law, Section 6385 of the Revenue and Taxation Code provides a sales tax exemption for that portion of fuel and petroleum products sold to a water common carrier that remains on board after the water common carrier reaches its first out-of-state destination. This section additionally provides a sales tax exemption for tangible personal property, other than fuel and petroleum products, sold to air, water, and rail common carriers when that property is shipped to a point outside this state under specified conditions.

With respect to air common carriers, Section 6357.5 provides an exemption for the sale or purchase of fuel and petroleum products sold to air common carriers when the fuel and petroleum products are for immediate consumption or shipment in the conduct of the air carrier's business on an international flight. Therefore, if an air common carrier's final destination were France, for example, current law would exempt the entire sale of fuel purchased in California, even if that carrier had stops in Los Angeles and New York before reaching its final destination. On the other hand, if the air carrier's final destination were somewhere in the United States, current law would impose tax on the entire sale of the fuel in California.

Current law also provides a sales and use tax exemption for sales of motor vehicle fuel (gasoline) used in propelling aircraft, when the motor vehicle fuel is subject to the motor vehicle fuel tax ($0.18 per gallon excise tax). This exemption does not apply to sales of aircraft jet fuel.

Proposed Law

This bill would add Section 6389 to the Revenue and Taxation Code to provide a state sales and use tax exemption for sales of aircraft jet fuel, as defined by Section 7387, sold to an aircraft jet fuel user, as defined by Section 7389, including any person using an aircraft as a common carrier of property or persons, at any airport that is located within an enterprise zone designated pursuant to Section 7073 of the Government Code.

The proposed exemption would not apply to the Bradley-Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or the taxes imposed under Section 6051.2 or 6201.2, or under Section 35 of Article XIII of the California Constitution.

The provisions of the bill would become operative on the first day of the calendar quarter commencing more than 90 days after the bill is enacted.

In General

Enterprise zones have been established in California to stimulate development in economically depressed areas. The Enterprise Zone Act provides the five following business related income tax incentives:

- Credit for sales and use tax paid on certain machinery.
- Credit for hiring qualified employees.
- Business expense deduction for the cost of certain machinery.
- Net operating loss carryover.
- Net interest deduction for lenders.

Additionally, employees may claim a tax credit to reduce the amount of their income tax on wages earned in an enterprise zone.

Enterprise zone tax incentives apply only to investments and business activities that are undertaken after an enterprise zone has received final designation.

Background

Until July 15, 1991, sales of fuel and petroleum products to air, water, and rail common carriers were exempt from sales tax when used in the conduct of the carriers' common carrier activities after the first out-of-state destination. The rationale for this exemption was that it made California ports and airports more competitive, and it established consistency in the Sales and Use Tax Law for interstate and foreign commerce sales by exempting that portion of the fuel which was actually transported outside this state prior to any use. However, because of the budget crisis in 1991, this exemption was repealed by AB 2181 (Stats. 1991, Ch. 85) and SB 179 (Stats. 1991, Ch. 88).

In 1992, however, AB 2396 (Ch. 905) restored this exemption for fuel and petroleum products, but only with respect to water common carriers, and only until January 1, 1998. The sponsors of that measure, Pacific Merchant Shipping Association, successfully argued before the Legislature that the July 1991 repeal of the exemption had been directly responsible for a decline in the number of ships which bunker in California ports, and that reinstating the exemption would increase bunker activity in California. The sunset date of January 1, 1998 was extended until January 1, 2003 by AB 366 (Stats. 1997, Ch. 615).

Two bills to restore the exemption for air and rail common carriers were introduced in the 1996 Legislative Session. Assembly Bill 3375 (Olberg) would have restored the exemption for rail common carriers. Assembly Bill 566 (Kaloogian) would have restored the exemption for air common carriers. According to a Department of Finance analysis of AB 566, "Governor Wilson has proposed a different form of tax relief for the aircraft industry. Under the Governor's proposal, a sales tax exemption would be extended to property that becomes a component part of an exempt aircraft as a result of maintenance, repair, overhaul, or improvement of the aircraft in compliance with FAA requirements." The Governor's proposal was actually enacted in the 1996 Legislative Session by SB 38 (Lockyer, et al., Stats. 1996, Ch. 954) which, among other things, included the sales tax exemption for the component parts.

Assembly Bill 1800 (Machado), introduced during the 1998 Legislative Session, would have provided an exemption for sales of fuel and petroleum products to air common carriers when used in the conduct of the carriers' common carrier activities after the first out-of-state destination. The bill failed to pass the Assembly Appropriations Committee. The Board was neutral on Assembly Bill 1800.

COMMENTS

1. **Sponsor and Purpose**. The author is the sponsor of this bill. The purpose is to create incentive for air common carriers to schedule additional flights to under-utilized regional airports, which will help alleviate some of the congestion at the over-utilized central airports.

2. **Summary of April 25 amendments.** Recent amendments changed the proposed exemption from a full tax exemption (state and local tax) to a partial tax exemption (state tax only). Also, a technical amendment regarding the definition of an aircraft jet fuel user was included.

3. **Definition of aircraft jet fuel user – suggested technical amendment.** The proposed exemption would apply to sales of aircraft jet fuel to an aircraft jet fuel user as defined by Section 7389, including any person using an aircraft as a common carrier of property or persons. Since Section 7389 specifically excludes common carriers from the definition of aircraft jet fuel user, the language providing the exemption to an aircraft jet fuel user, *including* a common carrier, would be incorrect since common carriers are specifically *excluded* from the definition. The bill should be amended to replace "including" with "in addition to."

4. **Definition of aircraft jet fuel.** The proposed exemption would apply to sales of aircraft jet fuel as defined by Section 7387. Section 7387 defines "aircraft jet fuel" to mean any inflammable liquid which is used or sold for use in propelling aircraft operated by the jet or turbine type of engine.

5. **Types of fuel used by common carriers.** Generally, there are two types of fuels used by aircraft (including helicopters). The first, aviation gasoline, is generally used in propeller type aircraft. Sales of aviation gasoline are exempt from the sales tax when the fuel is subject to the motor vehicle fuel tax. The second type of fuel, aircraft jet fuel, is used in jet or turbine type aircraft. Sales of aircraft jet fuel are generally subject to sales or use tax. Generally, the types of aircraft that frequent a regional airport consist of smaller aircraft powered by aviation gasoline rather than aircraft jet fuel.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

6. **Administration of proposed exemption.** The proposed exemption would only apply to sales of aircraft jet fuel at any airport that is located within an enterprise zone. Verifying which airports are located within enterprise zones should not be problematic for the Board.

7. **Partial tax exemptions are difficult to administer.** Due to the method used to report partial tax exemptions, any return containing a claimed partial tax exemption must be processed manually for the proper allocation of local taxes. Current law provides for two partial tax exemptions. The current partial tax exemptions apply to sales of manufacturing equipment and teleproduction equipment. The number of returns affected by the current partial tax exemptions are relatively minor. However, this bill would result in an increase in the number of returns filed containing a partial tax exemption.

COST ESTIMATE

Some additional administrative workload would be realized as a result of notifying affected retailers and responding to inquiries. Due to the partial tax exemption, additional resources will be needed to process returns in order to ensure the proper allocation and payment of local and district taxes. A detailed cost estimate of the workload impact is pending.

REVENUE ESTIMATE

According to the Department of Trade and Commerce, there are 19 airports that are located in Enterprise Zones in California.

A survey of all 19 airports revealed that jet fuel is sold at 15 of these airports. The total sales of jet fuel at these 15 airports are estimated to be $110.8 million.

The revenue loss from exempting from the state sales and use tax jet fuel sold at any airport located within an enterprise zone would be $5.5 million annually (110.8 million x 5% state sales tax rate).

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