

Issue Paper Number **08-001**



- Board Meeting
- Business Taxes Committee
- Customer Services and Administrative Efficiency Committee
- Legislative Committee
- Property Tax Committee
- Other

Forms to Implement Senate Bill 87, Fractionally Owned Aircraft

I. Issue

Which forms should the State Board of Equalization (Board) adopt to implement the provisions of Senate Bill 87¹ which established streamlined property tax administration procedures for county assessors to use in the assessment of fractionally owned aircraft?

II. Alternative 1 - Staff Recommendation

Staff recommends that the attached two forms be adopted by the Board to implement the provisions of Senate Bill 87 for the assessment of fractionally owned aircraft:

- Form BOE-570-FO-1, *Supplementary Schedule to the Business Property Statement – Aircraft Cost Report*, and instructions [Attachment A]
- Form BOE-570-FO-2, *Supplementary Schedule to the Business Property Statement – Aircraft Value Computation*, and instructions [Attachment B]

III. Other Alternative(s) Considered

The Board could adopt forms that limit the reporting requirements for managers of a fleet of aircraft in a Fractional Ownership Program [Attachment C].

¹ Urgency statute effective August 24, 2007; Ch. 180, Stats. 2007.

IV. Background

Government Code section 15606, subdivision (d), mandates that the Board shall prescribe and enforce the use of all forms for the assessment of property for taxation. One of the key assessment tools available to county assessors is the business property statement. Revenue and Taxation Code section 452 provides that "the board shall prescribe in detail the content of property statements, including the specific wording, to be used by all assessors...." The enactment of Senate Bill 87 created a need for supplementary property statements for fractionally owned aircraft.

V. Discussion

Fractional Ownership Programs are an emerging commercial aviation industry that has rapidly expanded in the last 10 years. *Fractionally owned aircraft*, as defined by the Federal Aviation Administration (FAA), are aircraft that are privately owned and operated pursuant to FAA regulations for operations in Fractional Ownership Programs. These are fleets of aircraft that are managed and maintained by an operating company, but ownership is distributed like a time-share. Participants in the programs have on demand, random access to aircraft in the program. Fractional ownership of aircraft is an overall concept using (1) shared ownership, (2) exchange of "dry leases" which allows the exchange of aircraft between owners in the programs, and (3) the use of an aircraft management company. The management company handles all operating requirements of the aircraft, including availability, maintenance, billings, shareowner usage, training, and flight crews.

Prior to the enactment of Senate Bill 87, there were no special assessment provisions for fractionally owned aircraft used in Fractional Ownership Programs that were using California airports. Previously, the Revenue and Taxation Code contained separate provisions of law related to the taxation of aircraft depending upon one of two types of traditional ownership and use: (1) general aircraft and (2) certificated aircraft. Typically, certificated aircraft are commercial aircraft operated by air carriers for passenger and freight service, while general aircraft are typically privately owned aircraft. General aircraft are assessed on an aircraft-by-aircraft basis and an assessment is made only in a single county where the aircraft is habitually situated. Certificated aircraft are assessed based on a fleet basis and assessments are made for each county in which the aircraft in the fleet land.

Senate Bill 87 provides:

- That a fleet of fractionally owned aircraft operated in a Fractional Ownership Program obtains situs in California when an aircraft within the fleet lands in California. With respect to ensuring that the fleet are taxed in a manner that will reflect their actual presence in California, the bill provides a value allocated formula based upon the presence of aircraft in California.
- Implementation of a centralized administrative system by outlining the process for selecting the lead county for each Fractional Ownership Program, notifying the manager of the responsible lead county to which it would file its information, and detailing the duties of the lead county.
- That the manager in control of a fleet of fractionally owned aircraft file a single property statement with a designated lead county. Flight data included in the statement would be required to be segregated by airport.
- That the lead county will calculate the unallocated fleet value of aircraft operated in the Fractional Ownership Program for each make, model, and series. This information will then be transmitted to the other counties.

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- That the aircraft within the fleet will be valued the same as general aircraft. That is, current market value using commercially available aircraft price guides approved by the Board.
- That each county will determine their allocated portion for the total fleet value based on the flight data for that particular county. The formula will be based upon the number of landings in and departures from a county in proportion to landings and departures worldwide. Each county assessor is responsible for assessing and enrolling the taxable value of the aircraft that has situs in his or her county.
- That the fleet be assessed to the manager in control of the fleet
- That the lead county will head up an audit team of up to three counties. The audit will be made on behalf of all California counties that would otherwise be required to perform a mandatory audit under Revenue and Taxation Code section 469.
- That airport operators, upon an assessor's request, will provide information related to the aircraft that uses the airport facilities.
- That the Board will prescribe the contents of the property statement required to report fractionally owned aircraft to the lead counties.

At the November 15, 2007 Board meeting, after consultation with the California Assessors' Association Aircraft Subcommittee, staff asked the Board to adopt two supplementary property statement forms to implement the provisions of the fractionally owned aircraft reporting provisions of Senate Bill 87. Due to comments received from industry on the day of the meeting, staff was directed to meet with interested parties to ensure that the property statement forms and instructions were (1) understandable to the managers of the Fractional Ownership Programs who will be required to file the property statements; and (2) sufficiently detailed to provide county assessors with information to assess the aircraft.

On January 8, 2008, an interested parties meeting was held at the Board's headquarters in Sacramento. The major Fractional Ownership Programs operating aircraft in California were represented at the meeting: NetJets, Inc., Flight Options, LLC, Bombardier Aerospace Corporation (Flexjet), and CitationShares. Additionally, the designated lead counties for these Fractional Ownership Programs were also represented at the meeting: Los Angeles County, San Mateo County, Orange County, and Santa Clara County.

VI. Alternative 1 - Staff Recommendation

Staff recommends that the attached two forms be adopted by the Board to implement the provisions of Senate Bill 87 for the assessment of fractionally owned aircraft:

- Form BOE-570-FO-1, *Supplementary Schedule to the Business Property Statement – Aircraft Cost Report*, and instructions [Attachment A]
- Form BOE-570-FO-2, *Supplementary Schedule to the Business Property Statement – Aircraft Value Computation*, and instructions [Attachment B]

A. Description of Alternative 1

Form BOE-570-FO-1 [Attachment A] and form BOE-570-FO-2 [Attachment B] reflect the forms' content and language crafted at the January 8, 2008 interested parties meeting. The forms were revised from the November 2007 versions to accommodate requests made by industry representatives.

B. Pros of Alternative 1

Adoption of form BOE-570-FO-1 [Attachment A] and form BOE-570-FO-2 [Attachment B] will accomplish the mandates of Senate Bill 87 that the Board prescribe the contents of the property statements required to report fractionally owned aircraft to designated lead counties. Additionally, the proposed supplementary property statement forms will provide county assessors with information necessary to assess fractionally owned aircraft. The proposed forms reflect the language that industry representatives requested at the January 8, 2008 interested parties meeting to clarify what information the managers of the Fractional Ownership Programs are required to report to the lead county.

C. Cons of Alternative 1

Adoption of the proposed supplementary property statements will facilitate the implementation of legislation that is opposed by industry.

D. Statutory or Regulatory Change for Alternative 1

None

E. Operational Impact of Alternative 1

None

F. Administrative Impact of Alternative 1

1. Cost Impact

Development of Board-prescribed property tax assessment forms is a routine statutory duty of the Property and Special Taxes Department and the cost will be absorbed by existing staff.

2. Revenue Impact

None

G. Taxpayer/Customer Impact of Alternative 1

None

H. Critical Time Frames of Alternative 1

Adoption of supplementary property statements at the Board's January 31, 2008 meeting will assist industry and counties to comply with the statutory reporting deadline of 5:00 p.m. on April 1.

VII. Other Alternatives

A. Description of Alternative 2

Industry requests that forms BOE-570-FO-1 and BOE-570-FO-2 be limited to requesting only information regarding fractionally owned aircraft. They oppose providing information regarding "other" aircraft within a Fractional Ownership Program. [See Attachment C.]

Industry representative who participated in January 8, 2008 interested parties meeting provided the following comments in a letter dated January 11, 2008:

"By this letter, NetJets, Inc., Flight Options, LLC, Bombardier Aerospace Corporation (Flexjet), and CitationShares ("the fractional industry participations") object to the above-reference proposed forms, which we understand will be considered by the Board at a meeting to be held on or about 31 January 2008.

The fractional industry participants believe that the forms are predicated on a fundamentally flawed statute. We understand that the Board's task at this stage is to assist the counties in implementing the statute the best it can. We also appreciate the opportunity provided by your staff to participate in the interested parties meeting on 8 January 2008, and believe that such discussions are essential in order to develop a common understanding of the manner in which the fractional industry participants operate—an understanding that was, we submit, sorely lacking when Senate Bill ("SB") 87 was enacted. As a result of the discussions at the 8 January meeting, we believe that the proposed forms have been improved as compared to prior drafts. Nevertheless, we believe that the statute and the forms are still seriously flawed. Unless and until the defects in the underlying statute are rectified or otherwise resolved, industry participants need clear guidance with respect to the property statements they are compelled to file with the lead county assessor's office.

Our principal concern regards the intended scope of SB 87 and, consequently, the operation of the proposed forms in support of retroactive and ongoing property tax assessments to the managers of fractionally owned aircraft when, in fact, any taxable property interests in the aircraft are held by the fractional owners. SB 87 adopts a novel, unworkable, and unlawful approach to the assessment of personal property tax to a manager in control of a fleet.

Beyond the overarching flaws in the assessment methodology enacted by SB 87, the statute also has a specific defect which renders the forms inherently confusing in terms of the property to which they purport to apply. The statute directs that "[n]otwithstanding any other law, **fractionally owned aircraft** that has situs in this state shall be assessed on a fleetwide basis to the manager in control of the fleet." Rev. & Tax. Code § 1161(a) (emphasis added). The statute defines "fractionally owned aircraft" as "those aircraft registered with the Federal Aviation Administration as fractionally owned aircraft." Rev. & Tax. Code § 1160(a)(4). As we explained at the interested parties meeting, no aircraft meet this statutory definition. Registration of aircraft with the Federal Aviation Administration (FAA) is governed by 49 U.S.C. §§ 44101-44104 and implementing regulations found at 14 C.F.R. Part 47, and is accomplished through submission of an Aircraft Registration Application, AC Form 8050-1, to the FAA Registry. Upon acceptance of an application, the FAA issues a Certificate of Aircraft Registration, AC Form 8050-3. (I enclose example copies of the Application and Certification with this letter.) Nowhere in these statutes and regulations, or in the Registration Application or Certificate of Registration, is there any reference to fractional ownership. Accordingly, there are no "aircraft registered with the Federal Aviation Administration as fractionally owned aircraft."

The proposed forms compound this confusion by referring not just to "fractionally owned" aircraft, but also to aircraft that are not fractionally owned but managed in some way that is connected to

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fractionally owned aircraft. For example, the title of both forms states: "Use only for aircraft *managed within* a Fractional Ownership Program." The instructions for completing Column "A" of form BOE-570-FO-1 refer to aircraft "*managed by* a Fractional Ownership Program." In addition, the instructions for Column "A" require identification of "ownership type for each aircraft managed by a Fractional Ownership Program" as *either* "fractionally owned" or "other aircraft managed in a Fractional Ownership Program," which apparently implies that aircraft can be "managed in a Fractional Ownership Program" without being "fractionally owned."

SB 87, however, does not use these terms. Under the statute, only "fractionally owned aircraft" are assessed. *See* Rev. & Tax. Code § 1161(a) ("**F**ractionally owned aircraft that has situs in this state shall be assessed on a fleetwide basis to the manager in control of the fleet..."). *See also* Rev. & Tax. Code § 1161(c) ("A fleet of **fractionally owned aircraft** shall be assessed on an allocated basis."); *id.* § 1162(b)(3) ("[T]he lead county assessor's office...shall do all of the following:...Calculate...an unallocated value of all **fractionally owned aircraft** for each manager in control of a fleet of **fractionally owned aircraft**..."). Moreover the statute explicitly equates "fractionally owned aircraft" with "aircraft operated in fractional ownership programs"; both are defined to mean "aircraft registered with the Federal Aviation Administration as fractionally owned aircraft." Rev. & Tax. Code § 1160(a)(4). The form's use of the undefined term "aircraft managed in a Fractional Ownership Program" to suggest a broader class of aircraft than those that are "fractionally owned" creates confusion and is contrary to the statute.

We therefore object to the use of the phrase "aircraft managed within [by] [in] a Fractional Ownership Program" in both forms, to the inclusion of Column "A" in form BOE-570-FO-1, and to the request to identify aircraft other than those that are "fractionally owned" as that term is defined by statute."

B. Pros of Alternative 2

Revision of the proposed forms to require that the manager of a Fractional Ownership Program only report "fractionally owned aircraft" will conform with the limited provisions of Senate Bill 87.

C. Cons of Alternative 2

Deletion of the requirement for the manager of a Fractional Ownership Program to report "aircraft managed within a Fractional Ownership Program" may increase the likelihood of double assessments.

In a well-established line of cases, the United States Supreme Court has held that personal property involved in interstate travel or commerce, such as an aircraft, may be subject to taxation by any state in which the property maintains a substantial presence. Aircraft that use California's airports have long been subject to property taxation. Generally, the appropriate assessee has been relatively easy for county assessors to establish. However, with the advent and increased popularity of fractionally owned aircraft, the determination of an assessee for property taxation purposes has been difficult, if not impossible, for county assessors. The Legislature recognized these issues and enacted Senate Bill 87.

Currently, county assessors receive information regarding fractionally owned aircraft from airport managers and from the FAA website. At the January 8 interested parties meeting, industry representatives confirmed that there are many aircraft "managed in a Fractional Ownership Program" that are not actually fractionally owned. When these aircraft land at a California airport, they are identified as part of the "Fractional Ownership Program." By requesting information on the proposed forms that will identify "fractionally owned aircraft" and "other aircraft within the Fractional Ownership Program," this will provide the lead county assessor's office with essential information to

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ensure that aircraft are not assessed under the Senate Bill 87 provisions that are already being assessed to another assessee.

County assessors have the right to request information they believe is necessary to perform their statutory duties. Revenue and Taxation Code section 442 mandates that "every person owning, claiming, possessing, controlling or managing property shall furnish any required information or records to the assessor for examination at any time."

D. Statutory or Regulatory Change for Alternative 2

None

E. Operational Impact of Alternative 2

None

F. Administrative Impact of Alternative 2

1. Cost Impact

Development of Board-prescribed property tax assessment forms is a routine statutory duty of the Property and Special Taxes Department and the cost will be absorbed by existing staff.

2. Revenue Impact

None

G. Taxpayer/Customer Impact of Alternative 2

None

H. Critical Time Frames of Alternative 2

Adoption of supplementary property statements at the Board's January 31, 2008 meeting will assist industry and counties to comply with the statutory reporting deadline of 5:00 p.m. on April 1.

Preparer/Reviewer Information

Prepared by: Property and Special Taxes Department, County-Assessed Properties Division

Current as of: January 16, 2008

INSTRUCTIONS FOR COMPLETING FORM BOE-570-FO-1

Using a separate sheet for each aircraft type as described in California Code of Regulations, Title 18, section 202, list name of management company and the lien date. Fill in the columns in the following manner:

- Column A.** Identify ownership type for each aircraft managed by a Fractional Ownership Program. Enter by using the following codes: "O" for fractionally owned or "M" for all other aircraft managed in a Fractional Ownership Program.
- Column B.** Enter the Aircraft's Federal Aviation Administration (FAA) number.
- Column C.** Enter the manufacturer's aircraft serial number.
- Column D.** Enter the make (manufacturer's name), model, and series number of each aircraft.
- Column E.** Enter the manufacture year of the aircraft.
- Column F.** Enter the date the aircraft is delivered to the manager of the Fractional Ownership Program or delegatee.
- Column G.** Enter the original acquisition cost for that individual aircraft reported in accordance with generally accepted accounting principles, so long as that produces net acquisition cost. Also include any transportation costs, capitalized interest, and any capital additions or modifications not included in the original acquisition cost that are incurred as part of this transaction.
- Column H.** Segregate the cost of the improvements to aircraft, including transportation costs, capital additions, and modifications not included in Column G.
- Column I.** Segregate the cost not included in Column G.
- Column J.** *(Assessor's Use Only)*
- Column K.** *(Assessor's Use Only)*

INSTRUCTIONS FOR COMPLETING FORM BOE-570-FO-2

Complete general information listing name of management company, county in which the airport is located, airport name, and previous calendar year nonscheduled flight activity. Fill in the columns in the following manner:

- Column A.** List aircraft by make, model, and series from BOE-570-FO-1.
- Column B.** Enter the total arrivals and departures of this type of aircraft at this airport only for the prior calendar year.
- Column C.** Enter the total arrivals and departures of this type of aircraft system wide for the prior calendar year.
- Column D.** Calculate the total factor by dividing the number of arrivals and departures of all aircraft at this airport in Column B by the total number of arrivals and departures in Column C.
- Column E.** The taxable value of the operator's entire fleet of each type of aircraft will be determined by the Assessor reported on BOE-570-FO-1 and entered into this column.
- Column F.** The Assessor will multiply the total factor in Column D by the taxable value in Column E and enter the result here.
- Column G.** *(Assessor's Use Only)*

INSTRUCTIONS FOR COMPLETING FORM BOE-570-FO-1

Using a separate sheet for each aircraft type as described in California Code of Regulations, Title 18, section 202, list name of management company and the lien date. Fill in the columns in the following manner:

Column A. ~~Identify ownership type for each aircraft managed by a Fractional Ownership Program. Enter by using the following codes: "O" for fractionally owned or "M" for all other aircraft managed in a Fractional Ownership Program.~~

Column B. Enter the Aircraft's Federal Aviation Administration (FAA) number.

Column C. Enter the manufacturer's aircraft serial number.

Column D. Enter the make (manufacturer's name), model, and series number of each aircraft.

Column E. Enter the manufacture year of the aircraft.

Column F. Enter the date the aircraft is delivered to the manager of the Fractional Ownership Program or delegatee.

Column G. Enter the original acquisition cost for that individual aircraft reported in accordance with generally accepted accounting principles, so long as that produces net acquisition cost. Also include any transportation costs, capitalized interest, and any capital additions or modifications not included in the original acquisition cost that are incurred as part of this transaction.

Column H. Segregate the cost of the improvements to aircraft, including transportation costs, capital additions, and modifications not included in Column G.

Column I. Segregate the cost not included in Column G.

Column J. *(Assessor's Use Only)*

Column K. *(Assessor's Use Only)*