



STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082
916-323-3097 • FAX 916-323-3387
www.boe.ca.gov

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November 3, 2011

Re: *Legal Opinion – Aircraft Property Tax Issues*
Assignment No.: 11-072

Dear Mr. :

This is in response to your April 22, 2011 letter to the Board of Equalization's Legal Department wherein you requested our opinion on numerous questions pertaining to the assessment of aircraft. Please see the below analysis for answers to your questions.

Facts

Your letter contains three hypothetical situations regarding the assessment of aircraft for property tax purposes. After each hypothetical, you pose a number of questions which we address below. The first hypothetical situation addresses the business inventory exemption; the second and third hypothetical situations address the question of situs.

SITUATION 1¹

An aircraft owner places an aircraft for sale with a broker in the state of Washington in July of 2009 and signs a listing agreement giving him exclusive rights to sell his aircraft for, say, \$16,000,000, a 2% fee of the gross selling price will be charged at closing of escrow; and, the broker bears responsibility for all advertising and marketing costs; the aircraft is housed in a repair/storage facility owned by a third party who is acting on behalf of the owner to keep the aircraft in good maintenance and according to FAA regulations. The repair facility's staff is authorized to show and demo the aircraft to all prospective buyers. Logs are kept that show the aircraft has only been flown for demo and maintenance. Between the listing date and the lien date, only five hours have been flown for maintenance. Logs kept by the maintenance facility show each flight and none are for personal or business use of the owners. The corporate aviation company that has the listing has advertised in Amstat, Net Jet, and Plane Mover. Due to the down market in corporate jets, the aircraft does not sell until July of 2010 for almost \$10,000,000 less than the original asking price. The intent to sell is evidenced by many drops in selling prices before the aircraft is sold.

¹ For the purposes of this letter your hypothetical situations have been renumbered.

SITUATION 2

An aircraft was purchased on 12/17/2007 and delivered to the buyer, and LLC, in Salem, Oregon on 1/25/08. On 2/6/08 the aircraft was relocated to Reno, Nevada, where a managing partner lives. The aircraft was subsequently used partly in personal business by the owner and partly in charter, Part 135 usage, during the 2008 calendar year, but the home base, tax situs, remained in Reno, NV, but no Nevada personal property taxes were assessed or paid on the aircraft. Even though the aircraft was never on the ground for more than a few days at a time on Los Angeles, and the aircraft was not there on the lien date, 2009, it was assessed by Los Angeles County for the 2009 tax year and the value was apportioned based on the ground time listed in the aircraft's logs.

After the purchase, the aircraft underwent some repairs and modification, thus the lag in delivery form the purchase date. Here are the locations and ground days for the aircraft:

CALIFORINA

DAYS IN VAN NUYS	67
DAYS IN OTHER L.A. COUNTY	1
<u>TOTAL L.A.</u>	68
ONTARIO	9
MONTEREY	57
OTHER CA LOCATIONS	22
<u>TOTAL CALIFORNIA</u>	<u>156</u>

OUTSIDE CALIFORINA

OREGON	2
NEVADA	122
OTHER STATES AND INTERNATIONAL	61
<u>TOTAL OTHER</u>	<u>185</u>
TOTAL DAYS PER LOGS IN 2008	341
DAYS NOT FLOWN IN 2008	24
TOTAL DAYS IN 2008	365

Even though the aircraft was never in Los Angeles for 60 days at a time, the minimum number of days said needed to establish a tax situs in California, the owner did not have a residence in California, nor does he have any other income generated from California sources, the county apportioned the aircraft values of \$6,000,000 45.7%, 156 days divided by 341 days to Los Angeles, and said 54.3%, 183 Days divided by 341 days, was exempt.

SITUATION 3

An aircraft is based in Los Angeles and the owner is domiciled in California, however the aircraft is taken back east every year for around two or three months, where it is used in charter service. The owner has a home in New York and operates the charter service from a New York airport, where a hanger is rented each year.

In 2009 the aircraft operated out of New York for 67 days, but the ground days during this period were: 51 ground days in New York, 6 ground days in Montana, 4 ground days in New Jersey, 5 ground days in California, and one ground day in Ohio. The aircraft always returned to New York after the various flights. During the rest of the year, the aircraft was flown to New York at various times from California, where it returned between flights, and an additional 30 ground days in New York were accumulated. The owner did not pay any property tax in New York as personal property is not assessed there.

Law & Analysis

I. Business Inventory Exemption

The assessor has the duty to prepare the local assessment roll and to assess all property subject to general property taxation at its full value. (Rev. & Tax. Code, § 401; see §§ 110, 110.1, 110.5, 405, 601; see also Cal. Const., art. XIII, § 1, art. XIII A, § 1, 2.)

The business inventory exemption is set forth in Revenue and Taxation Code,² sections 219 and 129, and Property Tax Rule³ 133. Section 219 provides that: "For the 1980-81 fiscal year and fiscal years thereafter, business inventories are exempt from taxation and the assessor shall not assess business inventories." Section 129, states, in relevant part:

'Business inventories' shall include goods intended for sale or lease in the ordinary course of business and shall include raw materials and work in progress with respect to such goods.

Rule 133 states, in relevant part:

(a) Scope of Exemption.

- (1) 'Business inventories' that are eligible for a partial exemption from taxation under section 129 of the Revenue and Taxation Code include all tangible personal property, whether raw materials, work in process or finished goods, which will become a part of or are themselves items of personalty held for sale or lease in the ordinary course of business . . .

Section 129 provides that business inventories include "goods intended for sale or lease in the ordinary course of business" but do not include "any item held for lease which has been or is intended to be used by the lessor prior to or subsequent to the lease." Consigned goods that

² All section references are to the Revenue and Taxation Code unless otherwise specified.

³ Cal. Code Regs., tit. 18, § 133. All Rule references are sections to title 18 of the California Code of Regulations.

are held for sale may qualify for the business inventory exemption. (Letter to Assessors (LTA) 80/69, Question C4.)

Pursuant to section 5391, aircraft may qualify for the business inventory exemption: "Aircraft which are considered business inventories, within the meaning of Section 129 of the Revenue and Taxation Code, shall be included in the inventory exemption." The guidelines for the exemption of aircraft as business inventory are the same as for other properties, that is, to be eligible for the business inventory exemption the aircraft must be either held for sale or lease in the ordinary course of business on the lien date. Assessors' Handbook section 576 (AH 576) (February 2002), *Assessment of Vessels*, provides guidance for the application of the business inventory exemption to vessels held for consignment. While the definition of vessel specifically excludes aircraft (Rev. & Tax. Code, § 130), the business inventory exemption applies to both vessels and aircraft and thus the guidance in AH 576 can be instructive in the case of consigned aircraft. AH 576, pages 39-40, states:

PROPERTY HELD FOR LEASE OR CONSIGNMENT

Business inventory includes property held for lease or consignment by lessors, sublessors, and consignors. Exemptions allowed, however, are not based solely upon the status of a vessel on the lien date and the assessor should not judge the validity of the business inventory exemption based on that fact alone, but instead look to the true intent of the owner. Individual facts such as a vessel's actual use before and after the lien date, the length of a consignment or lease, and the location of the vessel tend to indicate the owner's intent, but are not singularly controlling . . .

To qualify for the business inventory exemption, the owner or lessor must have the intent to actually have the property available for lease or under consignment in accordance with the regular and usual practice and method of the business of the lessor or consignor. The vessel owners are not required to be in the business of selling or leasing vessels, only that the property is so held. The business inventory exemption is available to owners who have validly put their vessel up for consignment to a consignor . . . The key to qualifying for the business inventory exemption is that the vessel must be held for sale, lease, or consignment in the ordinary course of business of the seller, lessor, or consignor.

Situation 1

An aircraft owner places an aircraft for sale with a broker in the state of Washington. The aircraft is housed in a repair/storage facility owned by a third party who is acting on behalf of the owner to keep the aircraft in good maintenance and according to FAA regulations. You ask the following questions.

1. Does the listing with an out-of-state broker meet the criteria spelled out as a vendor or lessor of the property in his ordinary course of business when his course of business is to take listings from anywhere in the United States and sell or lease the aircraft?

As an initial matter, we note that the burden of proof is upon the taxpayer to establish that property for which an exemption is claimed falls within a specific constitutional or statutory exemption. (*Amdahl Corp. v. County of Santa Clara* (2004) 116 Cal. App. 4th 604, 614.) Thus, the burden is on the aircraft owner to establish to the assessor's satisfaction that aircraft was held for sale or lease in the ordinary course of business on the lien date and that all the other requirements of section 129 and Rule 133 were met.

For consigned aircraft to be eligible for the business inventory exemption, they must be held for sale or lease in the ordinary course of business on the lien date, in accordance with the regular and usual practice and method of the business of the consignor, and all the other requirements of section 129 and Rule 133 must be met. Assessors' Handbook section 577 (AH 577) (November 2003), *Assessment of General Aircraft*, provides at page 26:

In determining whether or not the business claiming the exemption is selling or leasing aircraft as part of their *ordinary course of business*, the business should have, but not limited to, the following:

- FAA dealer's license
- State of California seller's permit
- Local business license
- Location on an airport or airfield
- Listing or consignment agreements
- Statement that they have total care, custody, and control of consignment aircraft

The above documentation is evidence that a broker is in the business of selling, leasing, or consigning aircraft. You state that in your situation the broker's course of business is "to take listings from anywhere in the United States and sell or lease the aircraft." If such is the case, then the broker should be able to provide some, if not all, of the above documentation. Again, this is a fact-specific inquiry and the assessor should take all evidence into consideration in determining what business the broker is in and whether or not it is holding the aircraft in the ordinary course of business. The fact that the broker is located outside of California should not affect this inquiry.⁴

2. Do all of the following conditions have to be met for a vendor to qualify as vendor doing business in his ordinary course of business?

- FAA dealer's license
- State of California seller's permit
- Local business license
- Location on an airport or airfield
- Listing or consignment agreements
- Statement that they have total care, custody, and control of consignment aircraft

⁴ In your situation, you do not state whether the aircraft has established situs in California. We assume that it has since otherwise no California property tax would be due and the application of the business inventory exemption would be irrelevant.

As explained above, the documentation listed in AH 577 is evidence that a broker is in the business of selling, leasing, or consigning aircraft. However, it is not exhaustive and is meant only to guide the assessor's determination. There may be other persuasive evidence of the broker's ordinary course of business. The assessor should consider all evidence, not just the above-mentioned documentation, in determining whether or not the taxpayer has met the burden of showing that the property is held for sale or lease in the broker's ordinary course of business. In our opinion, it is possible that an assessor could find that property is held for sale or lease in the broker's ordinary course of business even though a broker could not provide all of the above documentation.

3. Does the aircraft have to be in the broker/vendor's physical possession, or can it be in the care, custody, and control of the third party, who is the agent for the owner or broker?

When determining whether a property placed on consignment qualifies for the business inventory exemption, the assessor must ascertain the true intent of the owner. Factors that reflect that intent include the property's actual use before and after the lien date, the length of a consignment or lease, and the location of the property. (AH 576, pp. 39-40.)

As explained in the supporting letter to Property Tax Annotation⁵ (Annotation) 205.0180, the location of the property is one factor to be considered in determining the owner's intent. If the property remains housed with the owner, it is possible that the owner could use the property for purposes not consistent with its sale or lease, rendering it ineligible for the exemption. (Rule 133, subd. (b).) In this case, the aircraft is located at the storage facility of a third party. Since the third party is acting on behalf of the owner, and is not an agent of the consignor, the owner has not given control of the aircraft to the consignor and there is still the possibility that the aircraft might be used for purposes other than its sale or lease. However, you also state that the logs kept by the third party show that only five hours have been flown for maintenance, and that the aircraft has not been flown for personal or business use.

While the foregoing facts are consistent with the aircraft being held exclusively for sale by the consignor, it is our opinion that more facts would be necessary to make a determination that the taxpayer has met its burden. For example, copies of the consignment agreement and the agreement between the owner and the third party would be helpful in determining the parties' rights with regard to the aircraft. Also, the location of the storage facility could have an effect on the analysis. Further, determining the intent of the owner is a subjective inquiry and there may be other facts not disclosed here that could affect the assessor's decision.

II. Situs

Pursuant to the California Constitution, article XIII, section 14, all property taxed by local government shall be assessed in the county, city, and district in which it is situated. General aircraft are assessable at the location where the aircraft is habitually situated. (AH 577, p. 21; Rule 205, subd. (b).) AH 577, pages 22-23, provides the following guidance when an aircraft establishes tax situs both in California and outside of California.

⁵ Property Tax Annotations are summaries of the conclusions reached in selected legal rulings of Board legal counsel published in the Board's Property Tax Law Guide and on the Board's website. See Cal. Code Regs., tit. 18, § 5700 for more information regarding annotations.

If an aircraft establishes tax situs both in California and outside California, apportionment is necessary between California and other jurisdictions under the rulings established in *Ice Capades, Inc. v. County of Los Angeles* and *GeoMetrics v. County of Santa Clara*. The interpretation of tax situs is that property must have "such contacts as confer jurisdiction to tax." Due process requires that the nature of the contacts sufficient to support a state's power to tax must provide the opportunities, benefits, or protection afforded by the state. For movable personal property such as aircraft, the amount and nature of the contact of property and its owner with a state necessary to establish tax situs is a factual determination. In general, relevant factors to be considered include the domicile of the aircraft owner, the aircraft's length of time in the state, the owner's intent to bring the aircraft into the county, and the owner's contact with the state. The court held that these were the determinative factors in *Ice Capades*. ¶ . . . ¶

When an aircraft owner is domiciled in California and the aircraft (1) has established a tax situs in California, (2) has established a tax situs in another state, states, or foreign country, (3) operates in other states or foreign countries but does not establish tax situs in those states or foreign countries, and (4) is predominantly located in California during the year, the county may assess portions of value reflecting the portion of the year that the aircraft is present in California and the portion of the year that the aircraft operates in the states or foreign countries where the aircraft has not established tax situs. ¶ . . . ¶

When an aircraft owner is domiciled in a state *other than* California and the aircraft (1) has established a tax situs in the owner's domiciliary state, (2) has established a tax situs in California, and (3) operates in another state, states, or foreign country, the county may assess portions of value reflecting only the portion of the year that the aircraft is present in California. In other words, the value is apportioned for only the time spent in California.

Situation 2

In situation 2, the aircraft is domiciled in Reno, Nevada, where it has established situs. The aircraft was in California airspace many times during the 2008 year, and spent 156 ground days in California (68 in Los Angeles County). You ask the following questions.

1. Are 68 days in Los Angeles County enough time to establish a taxable situs there in 2008?

First, we note that the question of whether the aircraft has established situs in California must be answered before we determine which county may tax the aircraft. As explained in *Ice Capades, Inc. v. County of Los Angeles* (1976) 56 Cal. App. 3d 745, 746 (*Ice Capades*) and *GeoMetrics v. County of Santa Clara* (1982) 127 Cal.App.3d 940, to establish situs, the property must have such contacts as to confer jurisdiction to tax. Due process requires that the nature of the contacts sufficient to support a state's power to tax must provide the opportunities, benefits, or protection afforded by the state. For movable personal property such as aircraft, the amount and nature of the contact of property and its owner with a state necessary to establish tax situs is a factual determination. In general, relevant factors to be considered include the domicile of the

aircraft owner, the aircraft's length of time in the state, the owner's intent to bring the aircraft into the county, and the owner's contact with the state.

In our opinion, the fact that the aircraft spent 156 ground days in California is a significant indication that the aircraft received the opportunities, benefits and protection of the state. Of course, the assessor may also consider other factors in making his determination (e.g., the owner's intent and the owner's contact with the state).

Assuming the assessor determines that the aircraft has situs in California, the decision of which county has the power to tax the aircraft is guided by Rule 205, subdivision (b). According to that Rule, once California tax situs has been established, the aircraft is "habitually situated" at the airport of the local jurisdiction where the aircraft spends its ground time. If the aircraft spends a substantial amount of time at multiple airports, it is habitually situated at the airport where it spends the most ground time. With regard to your specific situation, assuming that the aircraft has established situs in California, it is habitually situated in Los Angeles County for the year 2008, since the aircraft spent more ground days there than in any other county.

2. If a taxable situs in California has not been established does this contact with the county give them the right to add the time spent in other counties in California?

As explained above, the amount of time spent in all California counties is relevant to the threshold inquiry of whether or not taxable situs has been established in California. If the aircraft has not established situs in California, it is not necessary to determine in which county the aircraft is habitually situated; the aircraft is not taxable by Los Angeles County or any other California county.

3. What amount of short-term contacts in a year must an aircraft have before it can be assessed?

Again, whether an aircraft has established situs in California is a question of fact for the assessor to determine. The amount of time spent in California is only one factor to be considered. Therefore, there is no set number of short-term contacts that will determine the issue of situs.

4. Shouldn't short term days of one to two days to pick up passengers (often charter flight operators stay overnight or a weekend to pick up passengers the following day or Monday) be categorized as "transitory contact"?

In *Ice Capades*, the Court used the term "transitory contact" to describe the production of the taxpayer's show in a given jurisdiction. (*Ice Capades, Inc. v. County of Los Angeles, supra*, 56 Cal. App. 3d 745, 754.) The Court held that these contacts alone were insufficient to establish situs. In Assessors' Handbook section 504 (October 2002), *Assessment of Personal Property and Fixtures*, page 35, we advised that "transitory contact, such as may occur when a vessel or aircraft makes a round-the-world voyage, does not establish substantial presence." In our opinion, housing a plane in a jurisdiction for one or two days is more significant contact than that which might occur during a round-the-world voyage. As such, it is our opinion that the activity you describe is not likely transitory contact. Also, we note that in *Ice Capades*, each transitory contact was an isolated incident. That is, the court did not address the issue of whether

multiple instances of transitory contact in the same jurisdiction in the same year would be sufficient to establish situs.

5. Is there an overall percentage of time in a county, say 50%, like in [Property Tax Annotation 740.0002], that has to be met before a taxable situs is established? Would there be a minimum of 60 days in a year?

Annotation 740.0002 addressed one situation, among others, where aircraft had already established situs in California. In that case, pursuant to Rule 205, subdivision (b), we concluded that since the aircraft spent approximately 50 percent of its ground time in Orange County, that the aircraft was habitually situated in Orange County and thus had situs in that county.

Again, the inquiry of whether an aircraft has established situs in California is separate from the question of which county may impose personal property tax on the aircraft. In determining whether the aircraft has established situs in California, the amount of time spent in California is only one factor to be considered and there is no set number of ground days that will determine the issue of situs. If the aircraft has established situs in California, then it will be taxed in the county where it is habitually situated, i.e., has the most ground days. Whether 60 ground days is sufficient will depend on the amount of ground days spent in other counties.

6. If there is a taxable situs, shouldn't the numerator in the county's calculation have been 365, instead of 341?

Where, as here, an aircraft owner is domiciled in a state other than California and the aircraft (1) has established a tax situs in the owner's domiciliary state, (2) has established a tax situs in California, and (3) operates in another state, states, or foreign country, the county may assess portions of value reflecting only the portion of the year that the aircraft is present in California. (AH 577, p. 23) As explained in Annotation 740.0003, the time spent by the aircraft in the state in which the aircraft has acquired secondary taxable situs, California in this case, divided by 365 days provides the percentage of fair market value to be prorated to the state of secondary taxable situs.

Situation 3

In situation 3, the aircraft is based in Los Angeles and the owner is domiciled in California. In 2009, the aircraft is taken to New York for 67 days. The ground days during this period were: 51 ground days in New York, six ground days in Montana, four ground days in New Jersey, five ground days in California, and one ground day in Ohio. The aircraft always returned to New York after the various flights. During the rest of the year, the aircraft was flown to New York at various times from California, where it returned between flights, and an additional 30 ground days in New York were accumulated. You ask the following questions.

1. Were the ground days in New York sufficient to establish a tax situs there when the intent was to stay at least 60 days and there was a business reason in having the aircraft operated out of New York?

As explained above, for movable personal property such as aircraft, the amount and nature of the contact of the aircraft and its owner with a state necessary to establish tax situs is a factual determination. In general, relevant factors to be considered include the domicile of the

aircraft owner, the aircraft's length of time in the state, the owner's intent to bring the aircraft into the county, and the owner's contact with the state. In determining whether the aircraft has established situs outside of California, the amount of time spent in the other state is only one factor to be considered and there is no set number of ground days that will determine the issue of situs. While the facts that the aircraft operated out of New York for 67 days and spent 51 ground days there are consistent with establishing situs in New York, such a determination is best left for the county assessor after weighing all of the relevant factors.

2. Do the flights to other jurisdictions from New York detract from the total days in the east?

AH 577, page 22, provides that

When an aircraft owner is domiciled in California and the aircraft (1) has established a tax situs in California, (2) has established a tax situs in another state, states, or foreign country, (3) operates in other states or foreign countries but does not establish tax situs in those states or foreign countries, and (4) is predominantly located in California during the year, the county may assess portions of value reflecting the portion of the year that the aircraft is present in California and the portion of the year that the aircraft operates in the states or foreign countries where the aircraft has not established tax situs.

Therefore, if the aircraft has not established situs in the other jurisdictions, the ground time spent in those jurisdictions may be apportioned to California.

3. If 60 continuous ground days are not required for non-resident flights into Los Angeles to establish a tax situs, why would they be required to establish a tax situs in another state for an aircraft owned by a person who's domiciled is in California (if this is the case)?

As explained above, the amount and nature of the contact of property and its owner with a state necessary to establish tax situs is a factual determination. Several factors must be considered including the domicile of the aircraft owner, the aircraft's length of time in the state, the owner's intent to bring the aircraft into the county, and the owner's contact with the state. Length of time is alone not sufficient to make a determination. The assessor must also consider other factors including the nature of the time spent in the jurisdiction as well as the owner's contact with the state. Therefore, a specific amount of time may establish situs in one case and not in another.

The views expressed in this letter are only advisory in nature; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,

/s/ Daniel Paul

Daniel Paul
Tax Counsel

Mr.

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November 3, 2011

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cc: Honorable

County Assessor

Mr. David Gau MIC:63

Mr. Dean Kinnee MIC:64

Mr. Todd Gilman MIC:70