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August 5, 2004

TO INTERESTED PARTIES:

PROPERTY TAX RULE 138,
EXEMPTION FOR AIRCRAFT BEING REPAIRED, OVERHAULED,
MODIFIED OR SERVICED

In Letter To Assessors 2004/032, we advised interested parties that the Board had received a petition from the California Assessors' Association (CAA) to amend Property Tax Rule 138, *Exemption for Aircraft Being Repaired, Overhauled, Modified or Serviced*. Interested parties were invited to provide comments on the CAA petition. Enclosed is a matrix summarizing the comments received.

An interested parties meeting will be held on September 9, 2004 to discuss the proposed amendments to Rule 138. The meeting will begin at 9:30 a.m. at the Board's headquarters in Sacramento, 450 N Street, Room 122. The petition to amend Rule 138 is scheduled for the December 14, 2004 Property Tax Committee meeting.

All documents regarding this project will be posted to the Board's Web site at <http://www.boe.ca.gov/proptaxes/ptr138.htm>. If you plan to attend the interested parties meeting on September 9, 2004, please advise Mr. James Anderson at james.anderson@boe.ca.gov or (916) 323-5688.

Sincerely,

/s/ Dean R. Kinnee

Dean R. Kinnee, Chief
Assessment Policy and Standards Division

DRK:sk
Enclosure

**PROPERTY TAX RULE 138,
EXEMPTION FOR AIRCRAFT BEING REPAIRED, OVERHAULED,
MODIFIED OR SERVICED**

On September 25, 2003, the California Assessors' Association (CAA) petitioned the Board to consider the following amendments to Property Tax Rule 138:

(b) **QUALIFYING CERTIFICATED AIRCRAFT.** Aircraft that qualify for exemption include certificated aircraft that have been taken out of revenue service by an air carrier:

(1) for the purpose of being repaired, overhauled, modified, or serviced; and,

(2) with an executed contract or a specific written plan for the purposes described in subsection (b)(1).

~~Aircraft in California solely for the purposes described in subsection (b)(1) include any incidental and attendant storage.~~ Aircraft in California primarily for the purpose of storage may require incidental maintenance or servicing related to storage. Such aircraft do not qualify for the exemption.

Following are comments received in response to the CAA petition.

NO.	SOURCE	COMMENTS
1	Dick Fisher, Yolo County Assessor; CAA Property Tax Rules Committee	<p>The objection to the current version of Rule 138 is that it provides a tax exemption the extent of which is not authorized by statute. The CAA's proposed amendment would correct this by bringing Rule 138 into constitutional and statutory harmony.</p> <p>The rule is flawed because it conflicts with the proper scope of the aircraft maintenance exemption. When enacted, the purpose of the exemption was to support the market for the CA aircraft maintenance industry, and the exemption was limited solely to aircraft actually undergoing work. As subsequently reinterpreted by the BOE, the language of Section 220 limiting an exemption to actual maintenance activities is amended to include incidental and attendant storage.</p> <p>Naturally, the terms "incidental and attendant" mean "adjunct" and "connected with." Commercial aircraft could be parked in the Mojave Desert for years, and under the Board's interpretation, an annual oil change would qualify the craft for exemption under the current rule. This interpretation, however, does not square with the plain terms of the statute that an exemption be provided <u>solely</u> to aircraft undergoing work, and in no event to commercial aircraft that would otherwise be typically operated in CA.</p> <p>The rule provides that aircraft that are taken out of revenue service are no longer deemed to be operated interstate within CA. <i>In effect, the rule provides that all aircraft that are taken out of revenue service are exempt from taxation.</i> This interpretation, however, completely reverses the plain meaning of Section 220 which limits the exemption to (1) commercial aircraft in the state solely for the purpose of maintenance, <u>and</u> (2) of these only commercial aircraft that are otherwise not normally based or operated in the state.</p>

NO.	SOURCE	COMMENTS
2	Rick Auerbach, Los Angeles County Assessor	<p>I support the requested CAA amendments, however, there are other inconsistencies between the rule and Section 220 which must be addressed.</p> <p>First, although Section 220 clearly states in its last sentence, "This exemption does not apply to aircraft normally based in California, or operated intrastate or interstate in and into California," it is contradicted by the rule in subsection (c) which defines the aircraft being repaired, overhauled, modified or serviced as not being operated interstate into CA. This definition renders the above-quoted sentence meaningless and certainly could not have been what was intended by the Legislature in enacting Section 220.</p> <p>Also, the rule in subsection (d) mistakenly exempts aircraft normally flown within or into CA and are being repaired, overhauled, etc., <i>outside</i> this state. I have to believe this is a drafting error in the rule, as I believe we all understand it was the intent of the Legislature in enacting Section 220 to encourage aircraft maintenance facilities in CA, not other states.</p> <p>For these reasons, and the fact that Section 220 is clear and needs no interpretation, I strongly urge your vote to repeal Rule 138.</p>
3	Teresa Isakson, American Airlines	<p>American Airlines has spent the past three years aggressively working to contain all costs that we can control and to be the most efficient airline we can be. Therefore, we review all costs in all aspects of our company, including costs involved in maintaining our aircraft. An increase in property taxes at one potential maintenance site would be a negative for that site in determining where we maintain our aircraft.</p> <p>We are moving away from maintaining aircraft in CA.</p>
4	Keith Fuqua, UPS	<p>We avoid storing aircraft in CA because of the tax uncertainty.</p> <p>We avoid CA because this issue never dies.</p>

NO.	SOURCE	COMMENTS
5	John M. White, Southern California Aviation (SCA)	<p>This specific rule is critical not only to our ongoing business as it relates to the maintenance, modification, sale and/or leasing of commercial aircraft out of our FAA repair station located at the former Air Force Base in Victorville, CA, but also to other facilities that perform the same type of work throughout CA. SCA has been in business since 1998. Since then we have employed as much as 250 employees at the former Air Force Base and are their largest tenant, paying well over a million dollars a year to the local airport authority creating revenue and opportunity for them to pursue other property improvements in order to attract additional tenants.</p> <p>Due to SCA's presence at the former base, it has attracted other business. One significant company that has established itself at the airport is GE Engine Test. They built a 10 million dollar hangar facility. This is a significant property improvement that is subject to the appropriate property tax. It has been determined, through approved accounting practices, that SCA contributes seven million dollars annually to the local economy, mostly taxable, due to the fact it's generated through hotel, restaurants, rental car and gas receipts, just to mention a few. Taxing the airlines and/or owners on non-performing assets would be detrimental to all. One needs to remember, not like real property, these assets can fly away at anytime, taking jobs and incremental tax revenue with them.</p> <p>The proposed language by the CAA is simply wrong. All aircraft that are located at our facility are under FAA approved maintenance programs no matter if they are currently being worked on or are waiting to be. Other aircraft are being offered for sale or lease by companies or airlines that own them. Other aircraft are no longer aircraft in a sense, as they are marked for, or being torn down, and become a piece part inventory. These aircraft are de-registered and have no current Certificate of Airworthiness issued to them by the FAA, and the aircraft data plate is removed, effectively making them a non-aircraft. The activities described above qualify the aircraft for exemption under RTC 220 Rule 138.</p> <p>We are disappointed that the assessors continue to challenge the validity of Rule 138 as it currently stands. They threaten to eliminate jobs and create a new economic downturn in aviation in CA and will give those opportunities and jobs to our neighbors to the east. The state and the people of the State of CA simply lose if there is a change in Rule 138.</p>

NO.	SOURCE	COMMENTS
6	Bob W. Ziegelaar, AVTEL Services, Inc.	<p>AVTEL is a CA based aeronautical company specializing in the maintenance, repair, overhaul, modification and temporary storage of aircraft belonging to owners and operators located in CA, other locations within the US, or other countries around the world. The company built its reputation in a highly competitive international business environment by taking advantage of California's High Desert climate and the readily available pool of local aeronautical labor talent.</p> <p>It should not require much elaboration to point out that the economic conditions within the aviation industry, particularly within the maintenance segment of the sector, can be termed as "dismal." It gives us no pleasure to inform you that AVTEL is only just managing to survive the malaise within the sector. Without the demand for the storage and related maintenance of commercial aircraft, AVTEL could not have survived in CA. <i>In other words, AVTEL is highly dependent on the overall demand for maintenance services, whether they are for active or inactive aircraft, as dictated by market conditions.</i></p> <p>If the Board should add to the owners' and operators' difficulties by excluding stored aircraft from the existing exemption for "aircraft not in economic use," the inevitable consequence would be the relocation of such aircraft to states where similar property taxes are not levied. With the departure of the aircraft, hundreds, if not thousands, of employment opportunities would again be lost to CA, often in areas that can least afford such losses.</p> <p>AVTEL is fully aware that no government authority is ever impressed by threats of relocation or a cessation of business activities. Therefore, we can only hope that an honest prediction on AVTEL's part that it will have no choice but to cease operations in CA will help convince the Board to refrain from enacting the contemplated change. <i>In AVTEL's case alone, at least 130 employees would be furloughed as a direct result of the implementation of the contemplated property tax change.</i></p> <p>Of equal and critical importance is the loss of related activities that CA and its aircraft service providers would experience. When the bulk of an owners'/operator's stored fleet is relocated, it stands to reason that any other maintenance services required will also flow to the new locations. So the loss of storage customers will create a secondary and potentially even greater hardship for California's operators.</p> <p>AVTEL strongly urges the Board to refrain from considering any change in its approach to the "maintenance" exemption from property taxes currently in place for aircraft, as the contemplated change would have extremely detrimental economic consequences for CA, its aircraft service providers and statewide aeronautical employment.</p>