



## Airlines for America®

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December 11, 2017

Honorable Diane Harkey, Chairwoman  
California State Board of Equalization  
via email: [diane.harkey@boe.ca.gov](mailto:diane.harkey@boe.ca.gov)

Dear Chairwoman Harkey:

On behalf of Airlines for America (A4A),<sup>1</sup> I offer our comments regarding the Board of Equalization's adoption of the 2018 assessment year aircraft representative period for certificated aircraft. These comments respond to the BOE staff recommendations contained in Issue Paper Number 17-005, which recommends that the Board adopt the week of January 14, 2018, as the representative period for the 2018 tax year and announce its intent to use a week in October 2018 as the representative period for 2019 and transition to a 365-day method for 2020.

First, we want to thank the staff for its work and recommendations. It is clear that they heard our concerns at the November 27 interested parties meeting and took them into account when drafting the issue paper. Even though we do not agree with every specific recommendation, we view the issue paper as a good starting point, and the airlines are willing to engage the staff, the Board members and other interested parties to achieve the best result for all sides in this process.

### **2018 Tax Year**

Moving to the specific recommendations, we urge the Board to adopt the staff's recommendation to use the week of January 14 as the representative period for 2018. As the issue paper notes, the Board has for decades chosen a week very close to the lien date as the representative period.

When the lien date was March 1, the representative period usually included the lien date. In almost 40 years, however, the representative period never deviated from the lien date by more than 30 days. When the lien date moved from March 1 to January 1 in 1997, the representative period moved with it. In the period since 1997, the representative period again has always been within 30 days of the lien date.

There is a simple reason why a representative period close to the lien date has been chosen for over a half-century, and that reason is stated in the Board's own Handbook:

*The purpose of a representative period is to obtain air carrier operational data, for as brief a time span as possible that can reasonably be expected to reflect the average activity of the carrier for the ensuing tax year. . . .*

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<sup>1</sup> A4A members include: Alaska Airlines, Inc., American Airlines, Inc., Atlas Air, Inc., Federal Express Corp., Hawaiian Airlines, JetBlue Airways Corp., Southwest Airlines Co., United Continental Holdings, Inc., and UPS Airlines; Air Canada is an associate member.

The desirable representative period is one that is short enough not to be too burdensome, *yet long enough and current enough to be reasonably representative of the near future.* (AH 570 “Assessment of Commercial Aircraft,” p. 6, emphasis added.)

The importance of this cannot be overstated. The representative period is chosen to gather operational data to best reflect the airline’s taxable presence in California for the *ensuing tax year*, not the prior tax year. In the instant case, this means accurately measuring the presence of a fleet of commercial aircraft owned by an airline on January 1, 2018, in California for the period of July 1, 2018, through June 30, 2019. Putting the representative period close to the lien date then closely matches the property being valued (the fleet of aircraft as it exists on January 1) to the measurement of how much of *that fleet’s* time is spent in California.

Conversely, the further one separates the representative period from the lien date, the less relevance the operational data gathered during that period will have to the relative amount of time the fleet *in existence on the following lien date* will likely spend in California *for the ensuing tax year.*

As it stands today, we believe that no case, let alone a compelling case, has been made for a change in a half-century of valuation methodology that is consistent with the Board’s own literature that is of a similar vintage. On that basis we support the staff recommendation to designate the week of January 14, 2018, as the 2018 Representative Period.

### **Recommendations for Subsequent Years**

With regard to the recommendations of the staff regarding subsequent years, the airline industry is willing to engage in a process of further evaluation of the value allocation process under the auspices of the Board and in conjunction with other stakeholders.

**The 365-Day Approach** – We agree with the several aspects of the issue paper on the subject of subsequent years. First, we agree that Rule 202 as currently drafted precludes the use of actual operational data (the so-called “365-day approach”). We also agree that there are significant unanswered questions that would need to be answered before a move to such an alternative would be considered prudent, among these:

- What data is actually available? In the limited time this proposal has been discussed, there has been no real vetting of what data is alleged to exist, and what its limitations, costs, and availability are. Significant time is needed to fully understand this threshold question.
- Is the available data accurate? To date, virtually no time has been spent dissecting the data alleged to be available to determine its suitability. For example, we suspect that “ground time” as measured by FAA data is inconsistent with “ground time” as it is measured for property tax purposes. We question whether the analysis (apparently reviewed by assessors but not by the airlines) is using the correct measure (the time between when the chocks are set against the wheels to the time they are removed) – or

based on takeoff and touchdown times, which would overstate ground time because it would include taxiing. In addition, there is no discussion of how the analysis the assessors reviewed allocates code-share flights. In short, neither Board staff nor industry has had any opportunity to look behind the scenes to see if what vendors are selling has any relevance to how the law requires the calculations to be performed.

- What is the cost of the data and how is it procured? Even if such data exists and would be provided by a private vendor, who would be responsible for providing it -- the state or local government? If the Board mandated its use, would it become a “state mandated local expense” for which the state would be financially responsible? Staff correctly notes that the State Department of Finance will have to be involved with that discussion. Certainly, to the degree such data is to be procured by the state, an RFP would have to be issued, and a procurement process followed. This is a lengthy process that may also involve the legislative budget committees should the expenditure be deemed substantial. Once procured, would any party then have free access to the data in order to verify results?
- Would a statutory change be required? The current statutory structure for commercial aircraft value allocation involves a sample “representative period” during which scheduled operational data is used to project California fleet usage. It is likely that changing the structure to an *entire year’s actual usage from a previous year* will require legislation, not merely a change to Rule 202.
- Are multiple data sources available? Does the state or local government want to be in the position of relying on a single supplier of data with monopoly power to set prices and terms of usage for an annual tax event? What happens if the vendor exits the marketplace or announces a significant rate increase two weeks before the data is due out?
- Should last year’s data be used to allocate this year’s value? As discussed above, the strength of a representative period in January is its proximity to the lien date and the “ensuing tax year”. One thing is certain: a full year of last year’s data will be inaccurate as applied to this current year being valued if there are 1) significant changes in scheduling from year to year (cities added or dropped); 2) significant changes in equipment in the fleets between the years; or 3) significant single events (such as strikes, weather events, or political events that change passenger choice).

More data is not necessarily better data, and the severity of this temporal mismatch needs to be understood, as it could result in the overvaluation of a carrier in one instance, and undervaluation in others. For example, what happens in the case of a commencing airline with no “prior year’s data” or one with only partial year information available? What happens if the airline serves 10 California cities in Year 1, and only 2 cities in Year 2? There are countless other situations requiring study and discussion before action is dictated.

- If accurate plane-specific data for a full year is available, is there a better method than the current system to tax aircraft? If we conclude accurate, full-year, plane specific data is available, one could raise the same policy question as was raised with the property taxation of private rail cars: is there a more efficient way to tax them? Instead of having an ad valorem tax allocated between interstate and intrastate jurisdictions, plane-specific full year data may indicate that a “plane-day” tax, similar to the Private Rail Car Tax, administered on a centralized basis by the Board of Equalization would be far more

efficient than the administratively burdensome, expensive and contentious system currently in place.

To the degree a discussion of a movement to the prior year's actual data is contemplated, we suggest that the list of concerns to be addressed and resolved prior to that decision is somewhat longer than that mentioned in the staff issue paper. We urge the Board to consider this and to take into account that there are likely to be more "unknowns" that will be discovered as the process proceeds.

**The Short-term Transition to October** – For 2019, the Staff recommends that the representative period be moved to October based on their belief that it somehow is more "representative" of the California presence of an airline's fleet. The staff's belief is based on their own analysis of three decades of jet fuel sales data, which we have had almost no time to review thoroughly. The staff believes this data is a good proxy for aircraft activity in California, and while we are open to a structured discussion of this part of the recommendation, based on the data we see major flaws in their reasoning which do not support a move from January to October.

As we explained to the staff in a previous letter and at the interested parties meeting, we believe that the fuel sales data as presented does not accurately reflect aircraft activity for several reasons:

- The data is taken from sales at refineries, rather than the fuel that is pumped "into-wing" that would be the equivalent of measuring gasoline purchases for cars at the pump. We cannot be sure that that the data is not including fuel that is purchased by foreign airlines, fuel that is shipped out of California via pipeline, or bulk fuel purchases by airlines that is held in storage.
- Even if these issues are resolved, the Staff's analysis is incomplete because it only looks at California activity in a vacuum, and not the changes in California activity as a *percentage of national activity*. The staff assumes that because fuel sales and take-offs and landings in October more closely resemble the year's average it must mean October is somehow "more representative" than January. The staff's assumption is mistaken.

While activity in California in October is likely higher, activity *everywhere around the United States is also higher*. In other words, if we are trying to determine what fraction of the fleet's time is spent in California, both the numerator *and the denominator* of that fraction will be larger in October, resulting in a similar allocation ratio for both periods. The staff analysis only looked at the changes in the numerator (California activity), and came to an incorrect conclusion as a result. Further study would be needed to see if both California activity as a *percentage of national activity* changed or remained constant throughout the year. All things equal, if the fraction remained relatively constant as the airlines suspect it makes sense to keep the representative period close to the lien date for the reasons stated above.

- There are also potential income tax implications that may affect the state's general fund. The representative period for property tax purposes is also used to apportion income for the purposes of the Bank and Corporation Tax (See Regulation 25137-7(d)). As the income tax is a state-level tax, and the property tax is not, more work needs to be done

to understand what the likely fiscal impact would be on taxpayers and the general fund before a movement of the representative period to October is warranted.

A4A and its members appreciate the chance to offer our views to the Board and your continuing attention to our concerns. As the process moves forward, we intend to provide more analysis on the proposals to the Board and its staff. However, if I can provide any more information or analysis in the meantime, please do not hesitate to contact me.

Sincerely,

A handwritten signature in blue ink, appearing to read "Jon Almeras", with a large, stylized initial "J" on the left.

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