Background

The United States air transportation system is based on the concept that aviation is truly an interstate activity. The U.S. Congress has designated sole authority over the system to the Federal Aviation Administration by way of the Department of Transportation, granting the agency authority to set a unified standard for America's aviation policy. Such federal control also relates to the taxes paid by air carriers and aircraft operators and preventing such taxes from burdening interstate commerce. The federal government levies a series of taxes and fees on air passengers, while states assess taxes on companies that are based in the state or have significant business operation or "situs" within the state.

In an attempt to meet increasing budget demands, many states have instituted or are looking to assess new taxes on air charter companies and fractional ownership operators who conduct flights within the state, regardless of whether the companies or aircraft are based there. In addition, various states lack a uniform taxing method, making it possible to tax the same operation multiple times. For example, in California a unitary tax is imposed on a fractional operator's entire fleet of aircraft determined by the percentage of operations in the state divided by the total operations of the company's fleet. The diverse nature of state tax laws and the on-demand nature of operators make it difficult to identify and understand the potential tax liability of the charter and fractional operators when operating to states other than their home base, the practical effect of which is the burden to interstate travel and commerce.

This recent move by states to tax non-resident aircraft operations is reminiscent of the head/user tax movement in the early 1970s, which was thwarted by Congress' amendment to the Federal Aviation Act of 1958, often referred to as the Anti-Head Tax Act (AHTA).[1] The AHTA was Congress' attempt to stop the proliferation of head taxes, which were becoming a chaotic burden on interstate travel and commerce. The AHTA in its original form excluded property taxes from the prohibited fees and taxes. However, the states have consistently sought to use property taxes as a way to assess user fees/taxes and the AHTA has been amended to clarify that property taxes can be an unreasonable burden and discriminate against interstate commerce. The subsequent amendments to the AHTA have not stopped states from attempting to exploit other loopholes in the AHTA.

The unitary property tax of California is a new attempt by a state to use property tax to evade the AHTA, and also to rewrite the long-standing rules regarding taxation of aircraft. Traditionally, the common law doctrine held that personal property is taxable at the domicile of the owner. Many states have replaced the common law doctrine with a statute that provides that personal property is taxable in the jurisdiction where the property is located. The U.S. Constitution has been held to impose two limitations on the taxation of aircraft: (i) a state cannot tax an aircraft unless the aircraft has acquired a "situs" in the state;[2]and (ii) a state cannot impose an unapportioned tax where the aircraft has acquired a situ" in more than one state or country.[3] The problem with California's tax is that they are asserting that situ" has been established just by the mere fact that an aircraft lands at any airport within the state.

Burdens On Interstate Commerce And Due Process

It has always been a popular strategy for states to seek new sources of revenue by shifting new tax burdens as much as possible on out-of-state residents and corporations. The popular target for some states is currently aircraft and aircraft operators. Even though the Constitution's Due Process Clause and the Commerce Clause limit the ability of the states to levy or assess a property tax on aircraft, particularly aircraft not based in the taxing jurisdiction, this has not stopped the states in their attempt to create new methods of taxation. The U.S. Supreme Court, in cases interpreting those clauses, has held that in order for a state to assess a tax on interstate commerce, the activity must have a substantial nexus to the taxing state, be fairly apportioned, must not discriminate against interstate commerce and must be fairly related to the service provided by the state.[4] The focus is not on the formal language of the tax statute, but rather on the practical effect.[5]

The Supreme Court has held in a well-established line of cases that personal property used in interstate travel or commerce may only be subject to taxation by states in which the property maintains a substantial presence or have a situs.[6] If that situs exists, the tax must be fairly apportioned. The general presumption is that the domiciliary state has the right to tax the entire value of the aircraft, unless the owner can show that the aircraft has obtained situs elsewhere. In *Northwest Airlines*, the Supreme Court held that Minnesota was the domiciliary state and, as such, was entitled to impose an unapportioned tax on property unless the property is "permanently situated in a State other than the domiciliary State".[7] The state of domicile is typically the state of residency for individuals and in the case of a business where the entity was incorporated/formed, where the headquarters are located or where the aircraft is based.

A nondomiciliary state cannot impose a property tax unless the aircraft has obtained a situs in the state. Conversely, if the aircraft has obtained a situs outside the domiciliary state, then the domiciliary state cannot tax the entire aircraft. Courts have held that situs may be established where an aircraft is flown into the state "on fixed routes and regular schedules"[8] and where the property is "habitually employed" in the state.[9] The rationale for allowing a nondomiciliary state to assess a property tax on such aircraft is that the aircraft and its owner receive the "opportunities, benefits and protections" of the taxing jurisdiction by reason of its habitual or continuous presence in that jurisdiction.[10] The Constitutional principle of due process requires that the property subject to the tax must receive the "opportunities, benefits and protections" of the taxing jurisdiction.[11] However, a state is precluded from taking any action that may fairly be deemed to have the effect of impeding the free flow of trade between states.[12] A burden on interstate commerce is none the lighter and no less objectionable because it is imposed by a state under the taxing power rather than under manifestations of police power in the conventional sense.[13] While a state tax falling on interstate commerce may be justified because it is intended to make commerce bear a portion of the cost of the local government, if such taxes are found to inhibit the flow of trade between states it may violate the Commerce Clause.

States in their ambitious attempt to bring in more tax revenue have started assessing a personal property tax on out-of-state aircraft that land within the state. Our country's independence was based on unfair taxation. The founding fathers included the Commerce Clause as an enumerated power in the Constitution to allow Congress to regulate commerce among the states.[14] The Supreme Court determined that there is a dormant Commerce Clause that forbids states from enacting laws that interfere with interstate commerce and create obstacles that prompted the adoption of the Constitution.

The new taxes on aircraft operations are a burden to interstate travel and commerce and Congress has the power to stop the proliferation of these burdensome taxes.

State and Local Taxation, The New Head Tax

Almost forty years ago, Congress asserted its power to prohibit state and local governments from taxing interstate travel and commerce when it passed the AHTA. In 1972, the Supreme Court held that state and local head taxes on individuals travelling by air did not violate the Constitution as long as they were based on a fair approximation of the use of state-provided facilities for whose benefit they are imposed and they are neither discriminatory against interstate commerce nor excessive in comparison to the governmental benefit conferred.[15] Less than a month after this decision, three bills were introduced in the U.S. House of Representatives and U.S. Senate to overrule the decision legislatively.[16] Following the Senate hearings, the Senate Committee on Commerce, Science and Transportation reported out a bill that prohibited states and local jurisdictions from imposing a head tax on air travelers and amended the Airport and Airway Development Act of 1970 to increase the federal share of funding for airport development throughout the country.[17] The final bill was pocket-vetoed due to the bill's increase in federal funding. In 1973, similar bills were again introduced and the final bill was signed into law on June 18, 1973.[18]

Congress's concern with the Supreme Court's decision in *Evansville-Vanderburgh Airport Authority District v. Delta Airlines* was that while the user taxes did not violate the Commerce Clause, they did create a new, inequitable and potentially chaotic burden on the people who use air transportation.[19] Congress' limitation on the states' ability to assess such taxes was intended to prevent the states from burdening the traditional American right to travel among the states unburdened by travel taxes.[20] The legislative history indicates that the Senate Committee on Commerce, Science and Transportation never intended that air travelers would be subject to state and local head taxes as well as to national user charges.[21] The committee believed that there was no danger of this because of the basic constitutional guarantee of a citizen's right to unhindered interstate travel, and a U.S. Supreme Court decision that had prevailed since 1867, indicated that such taxes could NOT be constitutionally imposed.[22] Congress' belief that states would not attempt to assess taxes that hindered interstate travel was unfortunately misplaced.

Almost forty years later, some states have resumed their attempt to levy taxes on interstate travelers and commerce. The legislative history of the AHTA provides insight into the intent of the scope of the law. The AHTA prohibits any government agency other than the United States from establishing or levying a passenger head tax or use tax on any individual traveling in air commerce and the carriage of persons in air transportation.[23] The prohibition was to ensure that passengers and air carriers are taxed at a uniform rate--by the United States-- and that local head taxes will not be permitted to inhibit the flow of interstate commerce and the growth and development of air transportation.[24] Congress could not have envisioned that states would manipulate the long-standing situs requirement to use property tax to evade the intent of the Anti-Head Tax Act.

The 1973, AHTA was intended to prohibit state and local governments from implementing chaotic taxes on users of the national air transportation system, which ultimately resulted in an inequitable interstate travel tax. The AHTA carved out an exception for "the continuation of the levy and collection of reasonable rental charges, landing fees, and other service charges for the use of airport facilities."[25]

Congress understood that states may try to manipulate the exception for such property taxes as the language of the original AHTA prohibited taxes and head charges that were "directly or indirectly" assessed on persons traveling in air commerce.[26] Congress did not want to restrict the states from continuing their other then current methods of taxation, including property taxation. When it became clear that states may attempt to use property tax to burden interstate air transportation unfairly, the AHTA was amended by adding a provision identifying the potential for property taxes to be an unreasonable burden to interstate commerce.[27]

Unfortunately, some states have reverted to levying new taxes on interstate aircraft operations. Most of the taxes are disguised as a permissible property tax on aircraft, but their practical effect is similar to that of the prohibited user taxes. For example, California has implemented a property tax on any aircraft that has more than one owner that lands in the state.[28] California has carefully drafted the new tax as an apportioned property tax based on the number of flights into each county of the state. This California law not only ignores the long-standing Supreme Court precedent requiring situs for assessing property tax, its practical effect is to operate as a tax similar to the prohibited head/user taxes that states attempted to assess in the 1970s.

NATA Position

The on-demand air charter and fractional aircraft industry is unique in American transportation and an essential service provider to small and mid-sized businesses. Air charter and fractional operators allow customers to travel in a short period of time to far-reaching parts of the country that may not be easily accessible by the airlines. The association is concerned that assessing taxes at the state level will force on-demand air charter and fractional aircraft operators to forego doing business in these states altogether, further burdening the businesses that rely on their service. For example, in California the aviation industry accounts for 1.7 million jobs and contributes $111 billion to the state's GDP. General aviation (all operations other than airlines and military) provides $18.2 billion annually to the state and is responsible for 80% of all operations statewide. Should the state continue to levy its unitary tax, NATA is concerned that operators will simply opt not to operate into the state, thereby crippling California's economy even further.

The proliferation of these new state taxes on charter and fractional operators is similar to the head taxes of the 1970s. It is imperative that Congress recognize the burden these state taxes place on interstate travel and commerce and implement a legislative change just as Congress did nearly forty years ago with the Anti-Head Tax Act.

NATA Staff Contacts:

Kristen Moore
Director, Legislative Affairs
kmoore@nata.aero

-or-

Jacqueline Rosser
Director, Regulatory Affairs
jrosser@nata.aero

---

[1] Currently codified as 49 U.S.C. § 40116.

[2] *Northwest Airlines, Inc. v. Minnesota*, 322 U.S. 292 (1944).

[3] *Braniff Airways, Inc. v. Nebraska*, 247 U.S. 590 (1954).

[4] *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

[5] *Id.*
[6] 247 U.S. 590.
[7] 322 U.S. 292.
[8] 247 U.S. 590.
[9] *Central Railroad Co. of Pennsylvania v. Commonwealth of Pennsylvania*, 270 U.S. 607 (1962).
[10] *Braniff Airways, Inc. v. Nebraska*, 247 U.S. 590, 600 (1954).
[11] *Id*.
[12] Freeman v. Hewitt 329 U.S. 249, 251 (1946).
[13] *Id.*
[14] U.S. Const. art. I, § 8, cl. 3.
[15] *Evansville-Vanderburgh Airport Authority District v. Delta Airlines*, 405 U.S. 707 (1972).
[16] S. 3611, 92d Cong. (1972) (introduced May 16, 1972); H.R. 14847, 92d Cong. (1972) (introduced May 9, 1972); H.R. 14991, 92d Cong. (1972) (introduced May 16, 1972). In addition, a similar bill was pending in Congress at the time the Court decided Evansville-Vanderburgh. H.R. 2337, 92d Cong. (1971) (introduced on January 26, 1971).
[17] S. Rep. No. 92-1005 (1972).
[18] 119 Cong. Rec. 20,380 (1973).
[19] S. Rep. No. 93-12, at 12 (1973).
[20] *Id*. at 13.
[21] *Id.* at 14.
[22] *Id*.
[23] 49 U.S.C. § 40116.
[24] S. Rep. No. 93-12, at 1 (1973).
[25] *Id.* at 3; Pub. Law No. 93-44 (1973).
[26] Pub. Law No. 93-44 (1973)(added 49 U.S.C. §1513, which was re-codified in 1994 as §40116). The re-codification was not to have any substantive changes to the AHTA and the "directly or indirectly" was mistakenly removed as "surplus" language.
[27] Pub. Law No. 97-248 (1982) (adding subsection (d) to 49 U.S.C. § 1513, currently codified as § 40116(d)).
[28] Cal. Rev & Tax Code §1161(b)