



AIRCRAFT USED IN INTERSTATE COMMERCE EXEMPTION

EVALUATION SUMMARY | JULY 2021 | 2021-TE23

TAX TYPE	Sales and use	REVENUE IMPACT	Could not determine
YEAR ENACTED	1984	NUMBER OF TAXPAYERS	Could not determine
REPEAL/EXPIRATION DATE	None		

KEY CONCLUSION: The exemption appears to be commonly used to exempt purchases of aircraft used in interstate commerce from sales and use tax.

WHAT DOES THIS TAX EXPENDITURE DO?

The Aircraft Used in Interstate Commerce Exemption (Interstate Aircraft Exemption) [Section 39-26-711 (1)(a) and (2)(a), C.R.S.] provides a sales and use tax exemption to commercial airlines for the purchase, storage, or use of aircraft used in interstate commerce.

WHAT IS THE PURPOSE OF THIS TAX EXPENDITURE?

Statutes and the enacting legislation for the Interstate Aircraft Exemption do not explicitly state its purpose; therefore, we could not definitively determine the General Assembly's original intent. Based on the operation of the expenditure we considered a potential purpose: to be to prevent the taxation of transportation equipment used in interstate commerce, which may be administratively difficult to tax.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

The General Assembly may want to consider establishing a statutory purpose and performance measures for the exemption.



AIRCRAFT USED IN INTERSTATE COMMERCE EXEMPTION EVALUATION RESULTS

WHAT IS THE TAX EXPENDITURE?

In 1984, House Bill 84-1016 created the Aircraft Used in Interstate Commerce Sales and Use Tax Exemption (Interstate Aircraft Exemption) [Section 39-26-711(1)(a) and (2)(a) C.R.S.], which provides commercial airlines with a sales and use tax exemption for the purchase, storage, use, and consumption of aircraft used in interstate commerce.

Vendors apply the Interstate Aircraft Exemption by not charging sales or use tax at the time of sale. Vendors are required to report the value of exempt sales to the Department of Revenue (Department) on their Colorado Retail Sales Tax Return Form (Form DR 0100) or Retailer's Use Tax Return Form (Form DR 0173), if applicable. If a commercial airline is charged tax by a vendor at the time of sale, they can file a Claim for Refund Form (Form DR 0137B) with the Department to apply for a refund of the sales taxes they paid.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Statute does not explicitly state the intended beneficiaries of the Interstate Aircraft Exemption. Based on the operation of the exemption, we inferred that the intended direct beneficiaries are commercial airlines that operate in interstate commerce. "Commercial airlines" is not defined in statute, but the Department classifies a commercial airline as an airline carrying freight or passengers on regularly scheduled flights for a fee.

WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

Statute and the enacting legislation do not explicitly state the purpose for the Interstate Aircraft Exemption; therefore, we could not definitively determine the General Assembly's original intent. Based on the operation of the exemption and similar tax expenditures in the state, we considered the following potential purpose: to prevent the taxation of transportation equipment used in interstate commerce, which may be administratively difficult to tax. Equipment used to ship goods and provide transportation, such as trains, trucks, and aircraft, are often used in many states, and companies in the transportation industry often maintain physical locations in multiple states. Furthermore, sales and use taxes are generally used in coordination to tax the consumption of tangible property used within a state's taxing jurisdiction, but for equipment used in interstate transportation, most of its use tends to be outside of the state or in multiple states. Therefore, administering and enforcing sales and use taxes on this type of equipment can be difficult and such exemptions are common in other states. This is also consistent with other sales tax exemptions in Colorado for purchases of transportation property used in interstate commerce, such as commercial trucks [Section 39-26-712, C.R.S.] and trains [Section 39-26-710, C.R.S.].

IS THE TAX EXPENDITURE MEETING ITS PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We could not definitively determine whether the Interstate Aircraft Exemption is meeting its purpose because no purpose is provided for it in statute or its enacting legislation. However, we found that it is meeting the potential purpose we considered in order to conduct this evaluation because commercial airlines are aware of the exemption and use it to exempt their eligible purchases from sales and/or use tax.

Statute does not provide quantifiable performance measures for the exemption. Therefore, we created and applied the following

performance measure to determine if the expenditure is meeting the potential purpose we used for the purposes of this evaluation.

PERFORMANCE MEASURE: *To what extent are taxpayers using the Interstate Aircraft Exemption to avoid paying sales and use tax on eligible purchases?*

RESULTS: Based on feedback from stakeholders, including commercial airlines that operate in interstate commerce, we determined that industry members are aware of and use the Interstate Aircraft Exemption. However, we lacked the data from the Department to quantify its use. Stakeholders did not identify any issues with the exemption's administration and indicated that all purchases are exempted at the point of sale. Lastly, stakeholders indicated that a similar exemption is available in most states and that knowledge and use of these exemptions is widespread, as many commercial airlines seek out states with an exemption when considering their operations and making purchasing decisions.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURE?

We lacked the information from the Department necessary to quantify the revenue impact to the State for the exemption. However, the exemption may provide a relatively large benefit to taxpayers, since aircraft are often high-cost and the exemption is for both sales and use tax. For example, based on stakeholder feedback and research on the airline industry, a typical new passenger aircraft can cost around \$50 million or more. Thus, the revenue impact to the State based on the 2.9 percent sales or use tax would be \$1.5 million per purchase of a typical new aircraft.

Additionally, statute [Section 29-2-105(1)(d)(I), C.R.S.] mandates that local governments for which the State collects sales taxes apply most of the State's sales tax exemptions, including the Interstate Aircraft Exemption. As a result, the exemption may reduce local tax revenues and provide a corresponding savings to aircraft operators if they make

purchases or take delivery of aircraft in these areas of the state. Home rule cities established under Article XX of the Colorado Constitution have the authority to set their own tax policies independent from the State and 11 of the 14 commercial airports in the state are located in home rule cities. Of the five most populated home rule cities— Aurora, Colorado Springs, Denver, Fort Collins, and Lakewood— only Aurora does not have a similar exemption.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

Eliminating the Interstate Aircraft Exemption would result in the State's 2.9 percent sales or use tax being applied to purchases of commercial aircraft. Commercial airlines would also pay additional local taxes for purchases made in local jurisdictions for which the State collects sales taxes. Our discussions with stakeholders indicate that this could make commercial airlines less likely to make purchases in Colorado, since most other states provide a similar exemption. Stakeholders told us that they are aware of which states have similar tax expenditures and try to make purchases in states such as Colorado that have an exemption in place, when possible.

Repeal of the Interstate Aircraft Exemption could also pose an administrative burden to the State and purchasers. Specifically, the removal of the exemption may make it difficult for taxpayers to comply with and for the Department to enforce the sales or use tax on such purchases. For example, if aircraft are purchased from an out-of-state vendor and then immediately put into use in interstate commerce, it may be difficult to determine the correct apportioned use that occurred in Colorado versus other states, which is generally necessary under the U.S. Constitution's Commerce Clause [U.S. Const. art. I, § 8] to enforce sales and use tax on purchases of transportation equipment used in interstate commerce. Further, because the Commerce Clause generally restricts states from applying discriminatory or burdensome taxation on interstate commerce, a repeal of the exemption may require further legal analysis to ensure the State's tax is constitutionally permitted.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We examined the tax laws of the 44 states (excluding Colorado) with a sales tax and identified 36 states that provide a general exemption for purchases of aircraft used in interstate commerce from sales and use tax, including all of the states bordering Colorado. Of the states that apply a tax, North Carolina and South Carolina levy a maximum sales tax on aircraft sales of \$2,500 and \$500, respectively; Mississippi provides a reduced tax rate; and Nevada only exempts aircraft from tax if it is first used in interstate commerce outside the state.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

The NON-RESIDENT NEW AND USED AIRCRAFT SALES AND USE TAX EXEMPTION [Section 39-26-711.5, C.R.S.]—Exempts non-residents' purchases of new or used aircraft from sales and use tax if the aircraft is removed from the state within 120 days from the date of sale or 30 days after the completion of maintenance, repair, or refurbishment of the aircraft associated with its sale.

THE AIRCRAFT COMPONENT PARTS SALES AND USE TAX EXEMPTION – [Section 39-26-711(1)(b) and (2)(b), C.R.S.]—Exempts the purchase, storage, use, and consumption of component parts permanently affixed to aircraft from tax. The exemption applies to all aircraft component parts, not just those used in interstate commerce.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURE?

The Department does not collect specific information regarding the use of the exemption and was unable to provide data for our analysis. For this reason, we were unable to quantify its use and revenue impact. As discussed, although vendors are required to report the exemption, they must use a line for “other exemptions” on both forms used to report it (Forms DR 0100 or 0173) and the amounts listed on these lines is

combined with several other tax expenditures and cannot be disaggregated for analysis.

If the General Assembly wants information on the revenue impact of the exemption, the Department would need to add separate reporting lines to Forms DR 0100 and 0173 and capture the data in GenTax, its tax processing and information system. However, according to the Department, this type of change would require additional resources to change the form and complete the necessary programming in GenTax (see the Tax Expenditures Overview Section of the Office of the State Auditor's *Tax Expenditures Compilation Report* for additional details on the limitations of Department data and the potential costs of addressing the limitations).

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER AMENDING STATUTE TO ESTABLISH A STATUTORY PURPOSE AND PERFORMANCE MEASURES FOR THE INTERSTATE AIRCRAFT EXEMPTION. Statute and the enacting legislation for the exemption do not state the exemption's purpose or provide performance measures for evaluating its effectiveness. Therefore, for the purposes of this evaluation we considered a potential purpose for the exemption: to prevent the taxation of transportation equipment used in interstate commerce, which may be administratively difficult to tax. We identified this purpose based on the operation of the exemption and similar tax expenditures in Colorado and other states. We also developed a performance measure to assess the extent to which the exemption is meeting this potential purpose. However, the General Assembly may want to clarify its intent for the exemption by providing a purpose statement and corresponding performance measure(s) in statute. This would eliminate potential uncertainty regarding the exemption's purpose and allow our office to more definitively assess the extent to which the exemption is accomplishing its intended goal(s).