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Eliminating the Aviation Sales Tax: Implications for Pennsylvania

Executive Summary

""Competition is not only the basis of protection to the consumer, but is the incentive to progress."
- *Herbert Hoover*

Since 2001 many of the northeastern states have evaluated the impact of, and experimented with eliminating, sales taxes on aircraft sales and maintenance activities. Connecticut, Massachusetts, New Hampshire, New Jersey, New York and Rhode Island determined a need to reform their tax and fee structure on aviation. These states have since created tax exemptions on aircraft sales, parts and maintenance in an effort to remain competitive in a developing marketplace. The incentives generated by the application of a sales tax exemption on aircraft parts and maintenance has migrated investment from both corporate and general aviation business to the northeastern United States. As a result, states have created opportunities to seize new aviation investment and jobs in-state.

This trend amongst Pennsylvania's neighbors has served as a barrier to entry for the aviation industry. This and historical factors have prevented the Commonwealth of Pennsylvania from participating fully in the burgeoning aviation market and from collecting revenue generated from job development in maintenance and operations

Additionally, states employing aviation sales tax exemptions denotes a broader industry trend. It underlies the anticipated growth of small to medium aircrafts particularly in the emerging areas of aero-tourism and very light jets (VLJs). If the Commonwealth of Pennsylvania does not engage fully with the growing aviation industry it could forego the opportunity to enhance revenues, even after the sales tax exemptions via income and corporate taxes, and to strengthen its overall state economy.

LESSONS LEARNED: MASSACHUSETTS CASE STUDY

- Prevalence of Aviation related tax exemption in the Northeastern United States
- Tax Exemption Value Chain

BASIC PRIVATE ANALYSIS

- Reality of Pennsylvania's Aviation environment
- Pennsylvania Resources
- Aviation Industry Trends

Impact on State

- Workforce
- Pennsylvania –Foregoing an Economic Development Opportunity

Eliminating the Aviation Sales Tax: Implication for Pennsylvania

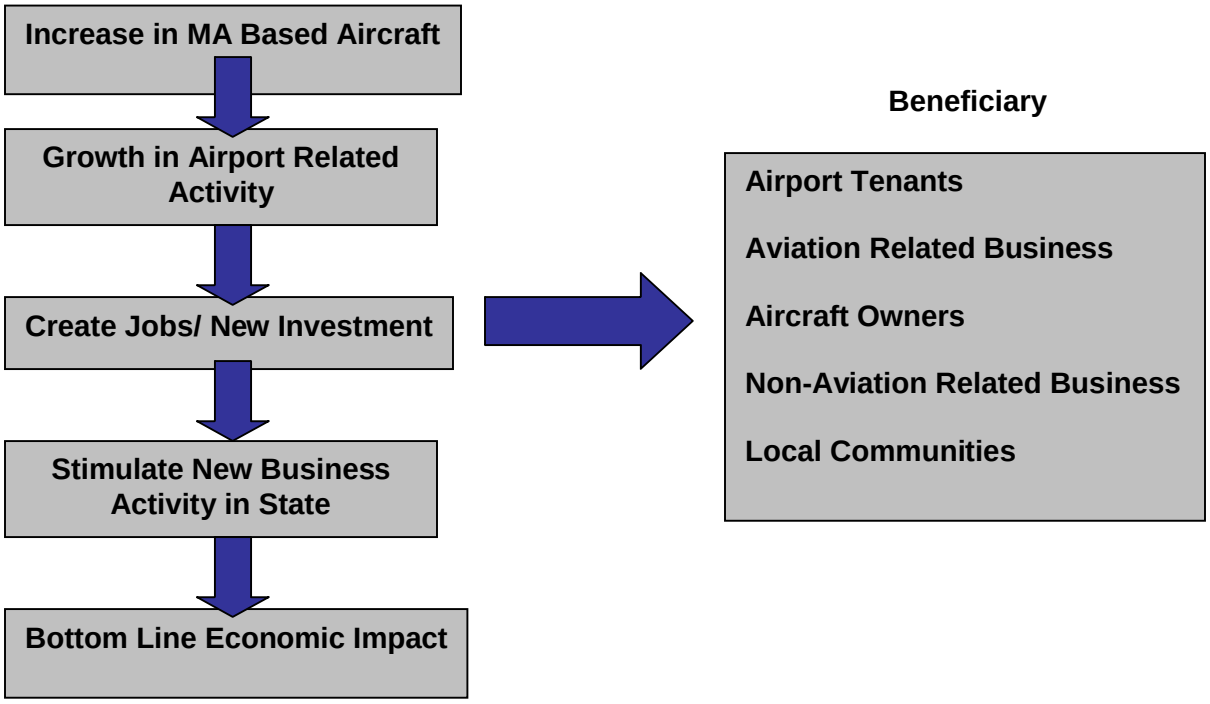
Lessons Learned: Massachusetts Case Study

Many northeastern states have implemented sales tax exemptions on aircraft sales, parts and maintenance in an effort to remain competitive with their neighbors by capturing corporate and general aviation business and retaining a portion of in-state jobs. The case study of the Commonwealth of Massachusetts provides an illustrative report on how a state's aviation system is important for overall economic development.

In 2000, the Massachusetts Aeronautics Commission (MAC) released the findings of a statewide Economic Impact Report for public-use airports. An objective of the report was to conduct a comparative evaluation of applicable state taxes and fees in the Massachusetts' aviation industry to its neighbors (i.e. Connecticut and New Hampshire) who already offered tax exemptions on aircraft sales, parts and maintenance. The report concluded that Massachusetts' companies and residents traveled out of state for aircraft sales and maintenance as a result of the savings offered by tax exemptions in Connecticut and New Hampshire.

Subsequently in March 2002, the Massachusetts State Legislature voted to exempt sales tax on in-state purchases of aircrafts and parts. The report attributes the tax exemption as a method for "stabilizing the aviation industry in Massachusetts as it continues to experience difficult times".[1] The enclosed chart[2] produced by MAC graphically explains the value-added by sales tax exemption.

Tax Exemption Value Chain



[1] SH&E International Air Transport Consultancy, The Massachusetts Aeronautics Commission & Massachusetts Airport Management Association, "Impact of Aviation-Related Tax Exemptions", 30 December 2005, p.4.
[2] Ibid, p.13.

The tax exemption fosters a more cost effective environment for which beneficiaries seek to base their aircraft purchase and maintenance in-state. As a result of the savings, aircraft owners and aviation related businesses further invest in airport related activities generating aviation jobs. The investment stimulates more new business and is the gateway for Massachusetts to follow broader industry trends thereby creating sustained economic development in the industry.

Moreover, according to the records maintained by MAC the state's post tax exemption statistics reveal that, " the number of based aircrafts in Massachusetts increased by 40% (420 aircrafts) , and fleet of multi-engine jet aircrafts as well as fleet of business owned aircrafts registered in Massachusetts doubled from 32 to 66. The three recipient groups: general aviation airports, business aircraft owners, and airport tenants and aviation related businesses, served by the aviation industry were also surveyed for the report. General aviation airports stated their revenues increased by 17% since the enactment of the tax exemption and also noted an increase in the number of based jets on their airfield. While business aircraft owners asserted they used the savings from the tax exemptions to conduct more maintenance and aircraft improvements which made it more cost effective to base their aircrafts in Massachusetts.[3] Lastly, the third group of respondents, airport tenants and aviation related businesses, witnessed an overall increase in sales, maintenance, aircraft storage and activity. The anecdotal evidence of these respondent groups reiterates the positive impact and savings experienced by Massachusetts companies and residents.

It is also, however, important to note the quantitative affect the tax exemption legislation had on the Massachusetts aviation industry. The Commonwealth of Massachusetts has 41 public-use airports (excluding Logan International Airport and Hansom Field) which generates over "$900 million in annual economic impact, $261 million in annual payroll, and provided 10,000 jobs".[4] Sales tax exemption has enabled Massachusetts to compete with Connecticut, New Hampshire, New York and Rhode Island in the areas of aircraft, parts and maintenance by promoting investment within the state and applying savings to finance maintenance and service repairs. Additionally, Massachusetts' enhanced participation in the northeastern aviation industry has positioned them to be even more competitive in the emerging VLJ market.

Basic Private Analysis

Compared to Massachusetts, the Commonwealth of Pennsylvania has 134 public-use airports of which six are international.[5] According to data collected by the Pennsylvania Department of Transportation (DOT) economic impact study, the combined 55 rural and 79 urban airports would yield and estimated "$101.5 million in economic activities and approximately $40 per capita".[6] The economic impact report further explains that more than 90% of the $12.4 billion in economic activities generated by urban airports came from just five airports with scheduled service while more than 66%[7] of the economic output in rural areas came from both general and business service airports. Based on the existing airport infrastructure and related aircraft resources/services within the Commonwealth of

[3] Ibid, p.8.
[4] Ibid, p.1.
[5] Pennsylvania Department of Community & Economic Development, 2007.
[6] The Center for Rural Pennsylvania - A Legislative Agency of the Pennsylvania General Assembly, "Landing on a Rural Opportunity", March 2001, p.3.
[7] Ibid.

Pennsylvania's boundaries it is a conundrum why the state is not fully capitalizing on emerging small to medium aircraft market trends in aero-tourism and VLJ.

The Center for Rural Pennsylvania defines aero-tourism as the "concept of getting pilots and passengers from a local airport to surrounding areas of interest".[8] Aero-tourism provides the state of Pennsylvania with a "market niche" whose magnitude of economic impact could be augmented with an aviation sales tax exemption. In 2001, the Pennsylvania DOT[9] also reported rural airports generated and estimated 1,650 jobs with a total payroll of about $31.5 million while the state's urban airports create 286,500 jobs with a total payroll of about $5.5 billion.

Like aero-tourism, the area of Very Light Jets (VLJs) is also expected to exhibit growth in the next six to ten years and further propel the small to medium size aircraft industry. VLJs are small jets which have a "maximum take off weight of less than 10,000 pounds and operate into airports and runways that re less than 3,000 feet long".[10] The Federal Aviation Administration (FAA) forecast 100 VLJs to become part of the US active fleet in 2006 and estimate the market will grow consistently by 400 to 500 VLJs per annum, reaching 4,950 aircrafts[11] by 2017. Some air taxi operators are investing in VLJs to offer flights at cheaper rates than traditional charters and avoid airline time delays. VLJs would primarily cater to aircraft owners and airports. Because the VLJs only require a 3,000 square runway corporate executives and wealth individuals are looking to local airports to avoid time delays and annoyance of post 9/11 security procedures.

Furthermore, the FAA ranked Pennsylvania as ninth (18,000 active pilots) in the total number of pilots, while some of its northeastern neighbors like Vermont, Delaware, and Rhode Island each had less than 1,600 active pilots. Similarly, in 2001, the FAA [12] explained that the states nearest Pennsylvania with a competitive number of licensed pilots were that of New Jersey, New York and Ohio. Since the release of this report Delaware, New Jersey, New York and Rhode Island have all eliminated sales tax on aircraft sales, maintenance, and repairs. Thus, Pennsylvania despite its resources in the aviation industry could be lagging behind its neighboring competitors by neither protecting it current access to the aviation industry nor aligning its availability to airports with aero-tourism and VLJ market.

The Aviation Council of Pennsylvania reported in their February 2005 newsletter of an aircraft owner who declined to purchase a $60 million dollar aircraft in Pennsylvania because the owner faced a $3.6 million sales tax[13]. The gravity of the aviation industry migration as a result of the high sales tax is emphasized by Pennsylvania's Deputy Secretary for Tax Policy, Daniel Hassell, explaining the states sales and use tax revenues from activities decreased approximately by 31% from $6.8 million in 2000-01 to $4.7 million in 2005-06. Though, a portion of this decrease is attributed to the general decline in aviation after 9/11 the state still reflected a drop of 74% in sales and use tax revenue associated to aircraft, aircraft parts and manufacturing from 2001 to 2006. The Pennsylvania

[8] Ibid, p.1
[9] Ibid, p.4.
[10] A Journal of the Federal Aviation Administration Managers Association, "Managing The Skies," Vol/4 N.3, May/June 2006, p.18.
[11] Ibid, p.18.
[12] Ibid.
[13] Aviation Council of Pennsylvania, "Pennsylvania Aviation News", Vol.45, No.2, December 2006.

Department of Revenue estimates that the state generates less than $1 million[14] in sales tax revenue from aircraft, aircraft parts, maintenance and repair per annum. Aircraft owners and fixed base operators do not mitigate Pennsylvania's use tax even if an aircraft is purchased out of state but maintained and operated within Pennsylvania. In other words, buyers are beset my two taxes: sales and use fees.

Impact on State Incomes & Employment

The Pennsylvania Department of Labor and Industry most recent statistics from 2002 reports a total of 74 work location with a total of 910 employees in the industry of "Other Support Activities – Air Transport in Pennsylvania (which excludes air traffic control and other airport operations)".[15] The Other Support Activities related to Air Transport is projected to grow by 11.3 % between 2004 and 2014. Based on these growth rates, Pennsylvania expects to see 440 new jobs created by 2014 at 44 jobs per year.

Aircraft mechanics and service technicians demonstrated the highest, 11.7 %[16] of total employment within this industry classification for 2004. The second largest employment of 9.9% was composed of transportation attendants and baggage porters which were then followed by "other –airport transportation workers" at 9.9%.

Within the industry cluster of "Scheduled Air Transportation", the Pennsylvania Department of Labor and Industry documented 99 work locations and a total of 20, 818 employees for 2002. The Department defines this industry as "providing air transportation of passengers and/or cargo over regular routes and on regular schedules".[17] The "Scheduled Air Transportation" Industry is predicted to grow by 6.8% between 2004 and 2014 and is estimated to add 1,180 jobs during this period at 118 jobs per year.

The enclosed Pennsylvania Occupational Wage chart[18] illustrates the projected hourly wage demanded by in-state aviation related jobs. Based upon the Department of Labor and Industry projects if Pennsylvania's "Scheduled Air Transportation" Industry is projected to grow by 118 jobs per year and the average annual salary for aircraft mechanic and service technicians is $46,840 then Pennsylvania would generate approximately $5,527, 120.00 a year for this single aviation related job category.

All of these economic developments could be accelerated in Pennsylvanian aviation companies were able to compete more effectively in the northeastern aviation market.

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[14] Commonwealth of Pennsylvania's Department of Revenue, March 7 2007.

[15] Pennsylvania's Department of Labor & Industry: http://www.dli.state.pa.us/landi/taxonomy/taxonomy.asp?DLN=858

[16] Ibid.
[17] Ibid.

[18] PA Workforce Continued: http://www.paworkstats.state.pa.us/analyzer/session/session.asp?cat=IND

PENNSYLVANIA OCCUPATIONAL WAGES STATEWIDE (All PA counties) MAY 2005 (Note: When data for a specific occupation is not available, the most relevent area containing this occupation has been provided, see Area Type.)										
SOC Code	Occupational Title	Area Type	Average Hourly Wage ($)	Average Annual Wage ($)	Median Annual Wage ($)	Entry Annual Wage ($)	Exper'd Annual Wage ($)	Mid Range Annual Wage ($)		
43-5011	Cargo and Freight Agents	PA	$17.82	$37,070.00	$32,500.00	$23,840.00	$43,690.00	$26,010.00	to	$49,660
49-2091	Avionics Technicians	PA	$20.26	$42,150.00	$41,210.00	$37,110.00	$44,670.00	$37,580.00	to	$45,170
49-3011	Aircraft Mechanics and Service Technicians	PA	$22.52	$46,840.00	$45,930.00	$35,060.00	$52,730.00	$38,830.00	to	$53,850
49-3093	Tire Repairers and Changers	PA	$10.73	$22,330.00	$21,250.00	$15,830.00	$25,570.00	$17,430.00	to	$26,350
53-1011	Aircraft Cargo Handling Supervisors	PA	$16.81	$34,970.00	$28,670.00	$21,980.00	$41,460.00	$23,190.00	to	$42,450
53-1031	First-Line Supervisors/Managers of Transportation and Material-Moving Machine and Vehicle Operators	PA	$24.78	$51,540.00	$49,000.00	$32,420.00	$61,110.00	$37,920.00	to	$59,340
53-2012	Commercial Pilots	PA	*	$67,530.00	$65,360.00	$40,050.00	$81,270.00	$48,760.00	to	$87,940
53-2021	Air Traffic Controllers	PA	$47.41	$98,610.00	$97,910.00	$72,280.00	$111,780.00	$80,130.00	to	$122,110
53-2022	Airfield Operations Specialists	PA	$16.72	$34,770.00	$27,350.00	$16,810.00	$43,750.00	$19,040.00	to	$47,850

Conclusion

Enacting a sales and use tax exemption for aircrafts, parts, maintenance and services merits a discussion by Commonwealth of Pennsylvania General Assembly. Doing so would thwart the migration of out of state aircraft purchases and maintenance to its competing neighbors. Additionally, Pennsylvania already commands numerous aviation related resources such as fixed based operations (134 airports), and a cadre of aircraft related occupations that are projected to increase in the next ten years. Eliminating the sales and use tax could allow the potential of the aviation industry to be fully realised and allow Pennsylvania to compete more aggressively in this fast-developing market.

Find out more about Aviation in Pennsylvania:

- Massachusetts Aeronautic Commission, http://www.massaeronautics.org/.
- "Managing the Skies", A Journal of the Federal Aviation Administration Managers Association, http://www.faama.org/.
- The Center for Rural Pennsylvania - A Legislative Agency of the Pennsylvania General Assembly, "Landing on a Rural Opportunity", March 2001.
- Pennsylvania Department of Labor & Industry http://www.dli.state.pa.us/landi/taxonomy/taxonomy.asp?DLN=858
- Pennsylvania Workforce: http://www.paworkstats.state.pa.us/analyzer/session/session.asp?cat=IND