



Legislative Fiscal Bureau

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March 10, 2004

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 933/Senate Bill 533: Airline Hub Incentive Grant Payments

Assembly Bill 933 was introduced and referred to the Joint Committee on Finance on March 4, 2004. Senate Bill 533 was introduced and referred to the Joint Committee on Finance on March 5, 2004.

CURRENT LAW

Commercial airlines that operate a terminal hub facility in the state are exempt from paying the ad valorem tax on airline property. (Non-exempt airlines pay a state ad valorem tax in lieu of local property taxes. Revenue from this tax is deposited in the transportation fund.) The definition of a terminal hub facility is either one of the following: (a) a facility from which an airline operated at least 45 common carrier departing flights each weekday in the prior year and from which it transported passengers to at least 15 nonstop destinations or transported cargo to nonstop destinations; or (b) an airport or any combination of airports in Wisconsin from which an air carrier company cumulatively operated at least 20 common carrier departing flights each weekday in the prior year, if the air carrier company's headquarters is in Wisconsin. Currently, Midwest Airlines and Air Wisconsin (a United Express carrier) qualify for the exemption. However, in response to a lawsuit filed by Northwest Airlines, a Dane County Circuit Court judge has ruled that the exemption violates the U.S. Constitution's "commerce clause," which prohibits states from discriminating against interstate commerce. That decision has been appealed by the state, but the timing of a decision by the Appeals Court is uncertain. The Department of Revenue indicates that, assuming that the circuit court ruling is upheld, the airlines will not be made to pay the ad valorem tax until the final court decision has been made.

Currently, the transportation fund bears the "cost" of the hub facility exemption, since the exemption eliminates the tax payment that would otherwise be deposited in the transportation fund. Beginning in 2004-05, however, an annual transfer will be made from the general fund to the transportation fund equal to the total amount of taxes paid by all of the exempt airlines in the year prior to becoming exempt. The transfer, which is made on July 1, will be calculated for all airlines that were exempt in the prior calendar year. The 2004-05 transfer, therefore, will be based upon the taxes paid by Midwest Airlines and Air Wisconsin in 2000, since those were the only two airlines that qualified for the exemption in calendar year 2003 and calendar year 2000 was the last year that they paid the ad valorem tax. In 2000, Midwest Airlines paid \$1,953,300 and Air Wisconsin Airlines paid \$577,100, for a total of \$2,530,400. Although the court struck down the exemption and the airlines may ultimately have to pay back taxes for 2003, the transfer from the general fund to the transportation fund will still occur because the airlines did not pay the taxes in 2003.

SUMMARY OF BILLS

Assembly Bill 933/Senate Bill 533 would require the Department of Commerce to make incentive grant payments to any airline that operates a hub terminal facility in Wisconsin based upon the number of passenger boardings that each airline has in the prior year. The amount of the payment would be determined by multiplying the number of passenger boardings for the airline and all its subsidiaries in the previous year times an amount specified in statute. [According to the bills' authors, the intent was to base the payment on the number of passenger boardings for eligible airlines at Wisconsin airports. The bills would have to be amended to accomplish this intent.] The following table shows the amounts that would be used to determine the payments. The amounts under "45 Flights" are for airlines qualifying under the definition of hub facility that requires at least 45 departing flights to at least 15 nonstop destinations (currently Midwest Airlines). The amounts under "20 Flights with Wisconsin Headquarters" are for airlines that qualify by virtue of having at least 20 weekday flights and having their headquarters in Wisconsin (currently Air Wisconsin and Midwest Airlines). Unlike the payments for airlines meeting the first definition, the per passenger payment for airlines meeting the second definition remains at a constant level of \$3.60, but is shown in the table for purposes of comparison. The year shown in the table is the calendar year from which the passenger data would be used to make the payment in the following year. For the purposes of calculating the payment, the number of passenger boardings would be the number of boardings reported to the Federal Aviation Administration by the airline and its subsidiaries.

<u>Year</u>	<u>"45 Flights" Hub Definition</u>	<u>"20 Flights with Wisconsin Headquarters" Hub Definition</u>
2003	\$1.70	\$3.60
2004	1.90	3.60
2005	2.50	3.60
2006	3.00	3.60
2007	3.40	3.60
2008	3.70	3.60
2009	4.00	3.60
2010	4.20	3.60
2011	4.30	3.60
2012 and thereafter	4.40	3.60

Under the bills, the first grant payment would be made on October 1, 2005, based upon the amount of the incentive grant calculated for calendar years 2003 and 2004. Beginning in calendar year 2006, the incentive grant payments would be made semiannually, on the first day of April and the first day of October, based upon the passenger boardings reported in the prior calendar year. [A technical amendment may be needed to clarify that each semiannual payment would be half of the full annual amount calculated for each airline.] In order to receive a payment, qualifying airlines would have to submit an application to the Department of Commerce. Payments would be made from a new GPR, sum sufficient appropriation.

The bills would transfer \$8,325,000 in 2004-05 from the transportation fund to the general fund. This transfer provision, however, would not take effect until October 1, 2005, which is in fiscal year 2005-06. A technical amendment is required to either make this transfer effective during the 2004-05 fiscal year or to modify the transfer to make it in the 2005-06 fiscal year.

FISCAL EFFECT

The bills would have impacts on both general fund appropriations and on the transportation fund. Although the Department of Commerce would make a payment for passenger boardings that the qualifying airlines had in 2003 and 2004, this payment would not be made until October, 2005, which is in 2005-06. Consequently, there would be no effect on general fund appropriations in the 2003-05 biennium.

While Midwest Airlines qualifies for the incentive grant payment by virtue of having over 45 weekday flights to over 15 nonstop destinations, the airline would also qualify under the other definition (over 20 flights for airlines that have Wisconsin headquarters), since the company's headquarters is in Wisconsin. Since the payment for airlines qualifying under this "Wisconsin headquarters" definition would be higher than the payment for the "over 45 flights" definition until

the 2008 payment (\$3.60 versus \$1.70 in 2003, for instance), both Midwest Airlines and Air Wisconsin could receive a payment based on the rate of \$3.60 per passenger. As drafted, it is possible that Midwest Airlines could claim and receive a payment under both hub definitions. If the intent of the bills is to pay Midwest Airlines only according to the payment schedule specified for airlines qualifying under the "over 45 flights" definition, the bills would need to be amended to accomplish this intent.

In order to estimate the amount of the first incentive grant payments (occurring on October 1, 2005), it is necessary to calculate what the payments would be for 2003 using passenger boarding data for that year and estimate the payments for 2004. The payment for 2004 will be based upon passenger boardings for qualifying airlines in that year, which are unknown. A representative of Midwest Airlines indicated that the company would not release information about its future projected passenger boardings in order to avoid revealing information about its future business plans to competitors. The representative did indicate, however, that it expects its 2004 payment under the bills would be about \$2,650,000, which would require a growth in passenger boardings at state airports of about 10% from 2003 to 2004. A representative of Air Wisconsin indicated that its passenger boardings are determined, to some extent, by decisions made by United Airlines, which makes it difficult for the company to make projections of passenger boardings for future years. The representative indicated that it would be a reasonable assumption that Air Wisconsin's passenger boardings at Wisconsin airports will be the same in 2004 as in 2003.

The following table shows the estimated payments for the two currently eligible airlines over the next several years. For 2003, actual passenger boardings data were used to calculate the payment for that year. For 2004, Midwest Airlines' estimate of its payment is used and the passenger boardings estimate that was used for this estimate is assumed to be the number of passenger boardings in subsequent years (that is, no growth after 2004). For Air Wisconsin, it is assumed that passenger boardings in 2004 and subsequent years will be the same as the number of passenger boardings in 2003. It is also assumed that the bill would be amended to specify that only passenger boardings at Wisconsin airports are counted and that Midwest Airlines will be paid an incentive grant according to the schedule of payments provided for airlines meeting the "45 flights" hub definition.

**Estimated Incentive Grant Payments to Currently-Eligible Airlines
(For Payment Years 2003 Through 2006)**

<u>Payment Year</u>	<u>Midwest Airlines</u>	<u>Air Wisconsin</u>	<u>Total</u>
2003 payment	\$2,157,900	\$2,197,900	\$4,355,800
2004 payment	2,650,000	2,197,900	4,847,900
2005 payment	3,486,800	2,197,900	5,684,700
2006 payment	4,184,200	2,197,900	6,382,100

As noted in the bill summary above, the Department of Commerce would make the 2003 and 2004 payments on October 1, 2005, which is in fiscal year 2005-06. Also in 2005-06, the Department would make the first installment of the 2005 payment (in April, 2006). The following table shows the estimated payments by fiscal year, using the same assumptions that were used in the previous table. As shown in this table, total estimated payments for the 2005-07 biennium would be \$18,079,500. Payment amounts would increase or decrease in the future based upon the number of eligible airlines and the passenger boardings reported by these airlines. For instance, if Midwest Airlines' passenger boardings at state airports continue to grow beyond the 2004 estimated level, or Air Wisconsin's passenger boardings grow beyond the 2003 level, then the payments to those airlines will increase.

**Estimated Incentive Grant Payments to Currently-Eligible Airlines
(Fiscal Years 2005-06 and 2006-07)**

<u>Fiscal Year</u>	<u>Midwest Airlines</u>	<u>Air Wisconsin</u>	<u>Total</u>
2005-06	\$6,551,300	\$5,494,800	\$12,046,100
2006-07	<u>3,835,500</u>	<u>2,197,900</u>	<u>6,033,400</u>
Biennial Total	\$10,386,800	\$7,692,700	\$18,079,500

As currently drafted, AB 933/SB 533 would result in a transfer of \$8,325,000 in 2004-05 from the transportation fund to the general fund (assuming that the bills are amended to make this provision effective in 2004-05). If this provision is amended to make the transfer occur in fiscal year 2005-06, the transfer from the transportation fund in that year will be \$878,700 less than the estimated 2003 and 2004 payments (totaling \$9,203,700), made on October 1, 2005. Additional payments estimated at \$2,842,400 would be made to the airlines on April 1, 2006, increasing the total cost of the bill to the general fund in 2005-06 (total payments minus the transfer from the transportation fund) to \$3,721,100.

Since the bill would not make an additional transfer from the transportation fund to the general fund in 2006-07, the estimated cost to the general fund for that year would equal the estimated payments in that year, or \$6,033,400.

The current law transfer from the general fund to the transportation fund associated with the airline hub facility ad valorem tax exemption will be \$2,530,400 in 2004-05, since the two airlines were exempt in 2003. If the Circuit Court's ruling that the exemption is unconstitutional is

ultimately upheld and the exempt airlines again become liable for the payment of ad valorem taxes, the current law transfer from the general fund to the transportation fund will cease. If this occurs in 2005-06, then the net cost to the general fund under the bill would be reduced by the amount of the transfer (from a net cost of \$3,721,100 to a net cost of \$1,190,700 in 2005-06 and from a net cost of \$6,033,400 to a net cost of \$3,503,000 in 2006-07).

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