
Finance Committee

HB 2111

Brief Description: Modifying the business and occupation tax credit for property tax payments related to the manufacture of commercial airplanes.

Sponsors: Representative McIntire; by request of Department of Revenue.

Brief Summary of Bill

- Modifies the business and occupation tax credit for commercial airplane and component manufacturers for property taxes paid, concerning which payments are eligible.

Hearing Date: 2/28/05

Staff: Mark Matteson (786-7145).

Background:

Business and Occupation Tax. Washington's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within the state, without any deduction for the costs of doing business. The tax is imposed on the gross receipts from all business activities conducted within the state. Revenues are deposited in the state General Fund. A business may have more than one B&O tax rate, depending on the types of activities conducted. Rates include 0.484 percent for manufacturers and wholesalers, in general, and 1.5 percent for most types of businesses that provide services.

The B&O tax does not permit deductions for the costs of doing business, such as payments for raw materials and wages of employees. Nonetheless, there are many exemptions for specific types of business activities and certain deductions and credits permitted under the B&O tax statutes.

Retail Sale and Use Taxes - Machinery and Equipment Exemption. The retail sales tax applies to the selling price of tangible personal property and of certain services purchased at retail. The tax is levied at a 6.5 percent rate by the state. Cities and counties may levy a local tax at a rate up to a maximum of 3.1 percent. Currently, local rates levied range from 0.5 percent to 2.4 percent. Sales tax is paid by the purchaser and collected by the seller.

The use tax is imposed on items used in the state that were not subject to the retail sales tax, and includes purchases made in other states and purchases from sellers who do not collect Washington sales tax. The state and local rates are the same as those imposed under the retail sales tax. Use tax is paid directly to the Department of Revenue (Department).

In 1995, following a study at the request of the Legislature by the Department concerning manufacturing activity in the context of the state tax structure, the Legislature enacted an exemption from the retail sales and use taxes on the purchase or acquisition of new or replacement machinery and equipment by manufacturers, if the machinery and equipment is used directly in the manufacturing activity.

Property Taxes. Property taxes are levied by state and local governments. Property taxes apply to both real property, which includes land, buildings, and fixtures attached to buildings, and personal property, which includes all other property, including tangible and intangible property. With regard to personal property, household items and furnishings are exempt, as are business inventories, but other business personal property is subject to tax.

Property taxes are administered by the counties at the local level for most types of property. The county assessor determines assessed value for each property. The county assessor also calculates the tax rate necessary to raise the correct amount of property taxes for each taxing district. The property tax bill for an individual property is determined by multiplying the assessed value of the property by the tax rate for each taxing district in which the property is located.

Aerospace Industry Incentives. In 2003 the Legislature enacted certain tax incentives provided to manufacturers of airplanes and airplane components. Eligible firms include subcontractors and suppliers that are manufacturers. Among the incentives enacted is a credit against the B&O tax for certain property taxes paid. The property tax payments that are eligible include:

1. property taxes paid on new buildings and the land upon which the buildings are located, or on renovations or expansions to existing buildings, if the buildings are used in the manufacturing of commercial airplanes or their components; and
2. property taxes paid on new machinery and equipment that is subject to the sales and use tax exemptions originally enacted in 1995 and that is used in manufacturing commercial airplanes or components of such airplanes.

According to its statement of need, the Department of Revenue is implementing the credit to require that the property be used a majority of the time in the manufacture of airplanes or components in order for the property tax payments to qualify. However, the Department believes that evaluating this criterion is likely to be difficult for both the taxpayer and the Department. In addition, there may be diversified businesses for which, as a proportion of total business operations, the manufacture of components for airplanes is a relatively small fraction.

Summary of Bill:

The B&O credit allowed for certain property taxes paid by manufacturers of commercial airplanes and airplane components is modified.

Property taxes paid with respect to newly acquired or constructed real property are eligible only if the building is used exclusively in the manufacturing of airplanes or airplane components.

Property taxes paid with respect to newly acquired machinery and equipment are eligible to the extent that the manufacturer conducts aerospace manufacturing activity relative to other manufacturing activity. This requirement is determined by applying a ratio to the total amount of property taxes paid on the new machinery and equipment, in which the numerator is the total taxable amount for the business for the prior calendar year that was subject to the manufacturing

rate for commercial airplane and commercial airplane component manufacturers, and the denominator is the total taxable amount that was subject to all manufacturing rates under the B&O tax. If the fraction is 0.9, it may be rounded up to 1.0.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect on July 1, 2005.