Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Finance Committee

HB 2089

Brief Description: Incentivizing a long-term commitment to maintain and grow jobs in the aerospace industry in Washington state by extending the expiration date of aerospace tax preferences and expanding the sales and use tax exemption for the construction of new facilities used to manufacture superefficient airplanes to include the construction of new facilities used to manufacture commercial airplanes or the wings or fuselage of commercial airplanes.

Sponsors: Representatives Carlyle, Hunter and Morrell; by request of Governor Inslee.

Brief Summary of Bill

- Extends the expiration date of aerospace tax incentives to July 1, 2040, upon the siting of a significant commercial airplane manufacturing program in Washington.
- Expands the availability of a sales and use tax exemption for the construction of facilities used to manufacture commercial airplanes.
- Terminates the preferential business and occupation (B&O) tax rate applicable to new versions or models of commercial airplanes if final assembly, wing assembly, or wing fabrication of the new model or version is moved outside the state of Washington.
- Requires the Joint Legislative Audit and Review Committee to specifically review employment changes in the aerospace industry every five years as part of its tax preference review process.

Hearing Date: 11/7/13

Staff: Jeffrey Mitchell (786-7139).

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

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deduction for the costs of doing business. Businesses must pay B&O tax even though they may not have any profits or may be operating at a loss. A business may have more than one B&O tax rate, depending on the types of activities conducted. Major tax rates are 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 percent for services, and activities not classified elsewhere. Several lower rates also apply to specific business activities.

Sales and Use Tax:
Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products and some services. A retail sale is a sale to the final consumer or end user of the property, digital product or service. If retail sales taxes were not collected when the user acquired the property, digital products or services, then use taxes applies to the value of property, digital product or service when used in this state. The state, most cities and all counties levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent; local sales and use tax rates vary from 0.5 percent to 3.0 percent, depending on the location.

Property Tax:
Property taxes are imposed by state and local governments. All real and personal property in this state is subject to the property tax based on its value, unless a specific exemption is provided by law. There are exemptions for certain properties, including property owned by federal, state, and local governments, churches, farm machinery, and business inventory.

Property owned by federal, state, or local governments is exempt from the property tax. However, private lessees of government property are subject to the leasehold excise tax. The purpose of the leasehold excise tax is to impose a tax burden on persons using publicly owned, tax-exempt property similar to the property tax that they would pay if they owned the property. The tax is collected by public entities that lease property to private parties.

Legislative Background of Aerospace Tax Incentives:
In 2003 the Legislature adopted tax incentives that were limited to aerospace manufacturers. The incentives included: a reduction in the B&O tax rate; a B&O tax credit for pre-production development expenditures; and a B&O tax credit for property taxes paid on property used in the manufacture of commercial airplanes and airplane components. A leasehold tax exemption for port district facilities is available to manufacturers of super-efficient airplanes that are not using the B&O tax credit for property taxes. Also included were sales and use tax exemptions for computer equipment and software, and its installation, used primarily in the development of commercial airplanes and components. These exemptions are scheduled to end in 2024.

In addition, the Legislature reduced the B&O tax rate from 0.484 percent to 0.275 percent for firms that repair equipment used in interstate or foreign commerce. The firms must be classified by the Federal Aviation Administration (FAA) as a Federal Aviation Regulation part 145 certificated repair station with airframe and instrument ratings and limited ratings for nondestructive testing, radio, class 3 accessory, and specialized services.

Businesses that exercise any of these incentives file an annual report with the Department of Revenue (DOR). The report includes employment, wage, and employer-provided health and retirement benefit information for full-time, part-time, and temporary positions.

In 2006 the Legislature extended the sales and use tax exemption for computer equipment and software to nonmanufacturing firms engaged in the development, design, and engineering of commercial airplanes and components of commercial airplanes. The B&O tax credit for preproduction development expenditures related to commercial aircraft was also extended to nonmanufacturing firms. Businesses that use these incentives file an annual report with the DOR.

In 2008 the Legislature extended aerospace tax programs to manufacturers, Federal Aviation Regulation (FAR) repair stations, and design/engineering services. Sales and use tax exemptions were provided for computer equipment and software, and installation, which are used primarily in aerospace products or providing aerospace services. Until July 1, 2024, the B&O tax rate is 0.2904 percent for: sales, either retail or wholesale, of commercial airplanes or components; the manufacturing or sales of tooling used in the manufacturing of commercial airplanes and components of airplanes; or persons classified by the Federal Aviation Administration as a FAR 145 certified repair station. Persons claiming this rate must file an annual survey with DOR. Persons performing aerospace product development are qualified for a 0.9 percent B&O rate and must file an annual survey with DOR. The preproduction 1.5 percent B&O tax credit on qualified expenditures was expanded to include Aerospace product development. The B&O tax credit for property taxes paid was extended to aerospace product development, the manufacturing of tooling, and FAR Part 145 certified repair stations.

Summary of Bill:

Summary
The expiration date is extended from 2024 to 2040 for the following aerospace tax preferences:
1. the preferential business and occupation (B&O) tax rate for the manufacturing, wholesaling, and retailing of commercial airplanes and airplane components;
2. the preferential B&O tax rate for the manufacturing, wholesaling, and retailing of tooling used in the manufacturing of commercial airplanes and airplane components;
3. the preferential B&O tax rate for retail sales by a part 145 certificated repair station;
4. the preferential B&O tax rate for businesses performing aerospace product development for others;
5. the B&O tax credit for aerospace product expenditures;
6. the B&O tax credit for property taxes and leasehold taxes on property used exclusively in manufacturing commercial airplanes or components of airplanes;
7. the sales and use tax exemptions for computer hardware, computer peripherals, and software used primarily in the development, design, and engineering of aerospace products; and
8. the leasehold excise tax exemption for lessees of port facilities used exclusively in manufacturing commercial airplanes.

The sales and use tax exemption for the construction of facilities used in the manufacturing of superefficient airplanes is modified to apply to facilities used for the manufacturing of commercial airplanes in general.

The bill is contingent upon the Department of Revenue making a determination that a final decision to locate a significant commercial airplane manufacturing program in the state of Washington has occurred. If a decision to locate a significant commercial airplane manufacturing program is not made by June 30, 2017, the bill is null and void. A significant commercial airplane manufacturing program is the commencement of manufacturing of a new model of a commercial airplane or a new version of an existing model and the manufacturing of the fuselage and wings of the new model or new version.

The ongoing availability of the preferential B&O tax rate for the production of a new or remodeled commercial airplane is contingent upon maintaining all final assembly of the aircraft, wing assembly, and wing fabrication within the state.

The explicitly described public policy objective of the bill is to maintain and grow Washington's aerospace industry workforce. The Joint Legislative Audit and Review Committee (JLARC) is required to review the tax preferences provided in the bill by December 1, 2019, and every five years thereafter to determine whether this public policy objective is being achieved. The JLARC is required to specifically assess changes in aerospace industry employment in Washington in comparison with other states and internationally.

Appropriation: None.

Fiscal Note: Requested on November 7, 2013.

Effective Date: This bill takes effect 90 days after adjournment of the session in which the bill is passed, except for section 6, relating to preferential B&O rates, the effective date is contingent upon the siting of a significant commercial airplane manufacturing program in the state of Washington. The effective date of section 6 is July 1, 2015.