Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Technology & Economic Development Committee

HB 2226

Brief Description: Extending specific aerospace tax preferences to include spacecrafts to encourage the migration of good wage jobs in the state.

Sponsors: Representative Morris.

Brief Summary of Bill

- Extends the existing aerospace industry preferential business and occupation tax rates and credits, and sales and use tax exemptions to manufacturers of spacecraft and spacecraft components, and spacecraft product development, effective October 1, 2015 and expiring on July 1, 2025.
- Requires taxpayers claiming the tax preferences to file a tax preference annual report with the Department of Revenue.
- Establishes tax preference performance metrics to assist the Joint Legislative Audit and Review Committee with their review of the tax preferences.

Hearing Date: 4/15/15

Staff: Kirsten Lee (786-7133).

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. 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

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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 apply to the value of property, digital products, 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 and local sales and use tax rates vary from 0.5 percent to 3.1 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. 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.

Aerospace Tax Preferences.
In recent years, the Legislature has adopted, modified, and extended specific tax preferences for the aerospace industry. Tax preferences are available for the engineering, manufacturing, and repairing of commercial airplanes as well as research and design pertaining to commercial airplanes. "Commercial airplane" has its ordinary meaning, which is, an airplane certified by the Federal Aviation Administration (FAA) for transporting persons or property, and any military derivative of such an airplane.

Examples of preferences available to the aerospace industry include the following:

- preferential B&O tax rate of 0.2904 percent for the manufacturing of commercial airplanes and components and the tooling used in manufacturing commercial airplanes and components;
- preferential B&O tax rate of 0.9 percent for aerospace product development;
- B&O tax credit of 1.5 percent for aerospace product development expenditures;
- B&O tax credit for property taxes and leasehold excise taxes on property used exclusively for manufacturing commercial airplanes or components, for the manufacturing of tooling, aerospace product development, or aerospace services provided by Federal Aviation Regulation (FAR) Part 145 certificated repair stations;
- sales and use tax exemption for computer equipment and software, and its installation, used primarily in the development of aerospace products or for aerospace services provided by FAR Part 145 certificated repair stations; and
- sales and use tax exemption for the construction of facilities used in the manufacturing of superefficient airplanes.

Many aerospace tax preferences were scheduled to expire in 2024. However, in 2013 the tax preferences were extended to 2040. The extension of the preferences was contingent upon the Department of Revenue (DOR) making a determination by June 30, 2017, that a significant commercial airplane manufacturing program would be located in Washington. The DOR has made the required determination.

Tax Preference Performance Statement.
In 2013 legislation was enacted requiring all new tax preference legislation to include a tax preference performance statement. Tax preferences include deductions, exemptions, preferential tax rates, and tax credits. The performance statement must clearly specify the public policy objectives of the tax preference, and the specific metrics and data that will be used by the Joint Legislative Audit and Review Committee (JLARC) to evaluate the efficacy of the tax preference.

Summary of Bill:

Business and Occupational Tax Preferences.
Certain aerospace tax preferences including the following are extended to the spacecraft industry. Beginning October 1, 2015:

- preferential B&O tax rate of 0.2904 for the manufacturing of spacecraft or spacecraft components;
- preferential B&O tax rate of 0.9 percent for spacecraft product development;
- B&O tax credit of 1.5 percent for spacecraft product development expenditures;
- B&O tax credit for property taxes and leasehold taxes on property used exclusively for manufacturing spacecraft or spacecraft components, or spacecraft product development;
- sales and use tax exemption for computer equipment and software, and its installation, used primarily in development of spacecraft products or for spacecraft services; and
- sales and use tax exemption for the construction of facilities used exclusively in the manufacturing of spacecraft or spacecraft components.

Businesses that exercise any of these preferences must file an annual report with the DOR.

The spacecraft tax preferences expire on July 1, 2025.

Tax Preference Performance Statement.
The tax preference performance statement specifies that the public policy objective is to create economic growth and jobs. The JLARC is required to assess employment changes and tax revenue changes in the spacecraft and spacecraft component industry in comparison to employment and tax revenues prior to the extension of spacecraft related tax preferences. If the JLARC finds that the number of jobs in the spacecraft industry has increased by 10 percent during the term of the tax preferences, then the Legislature intends for JLARC to recommend extending the expiration date of the tax preferences. To the extent practicable, the JLARC must use data provided by state agencies responsible for administering unemployment insurance and collecting tax revenue and data statistics provided by the Bureau of Labor Statistics.

Definitions.
The following definitions are added:

"Spacecraft" means all types of manned or transportation vehicles intended to be used for the purpose of operating in, or transporting a payload to, from, or within outer space, or in suborbital trajectory.

"Spacecraft component" means a part or system specifically designed for installation or assembly into spacecraft.

"Payload" means crew, instruments, or equipment carried by spacecraft.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect on October 1, 2015.