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**Technology & Economic Development  
Committee**

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**HB 2203**

**Brief Description:** Amending the definition of commercial airplane for specific tax preferences to include other types of commercial aircraft to encourage the migration of good wage jobs in the state.

**Sponsors:** Representatives Orcutt, Takko, Blake, Haler, DeBolt, Buys, Magendanz and Vick.

**Brief Summary of Bill**

- Extends certain aerospace tax preferences to the design, engineering, manufacturing, and repairing of commercial rotorcrafts.

**Hearing Date:** 1/21/14

**Staff:** Kelly Leonard (786-7147).

**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 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

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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; 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 currently available to 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.

Among other preferences, examples of those available to the aerospace industry include the following:

- Preferential B&O tax rate of 0.2904 percent for the manufacturing, wholesaling, and retailing of commercial airplanes and airplane components, the tooling used in the manufacturing of commercial airplanes and airplane components; and retailing by a Federal Aviation Regulation Part 145 certificated repair station;
- 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 taxes on property used exclusively in manufacturing commercial airplanes or components of airplanes, aerospace product development, the manufacturing of tooling, and 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 commercial airplanes and components; and
- Sales and use tax exemption for the construction of facilities used in the manufacturing of superefficient airplanes.

Businesses that exercise any of these preferences must 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.

Many aerospace tax preferences were scheduled to expire in 2024. However, the Legislature extended the preferences to 2040 by passing ESSB 5952 in the 2013 third special session. The

Legislature also expanded the sales and use tax exemption for the construction of facilities used in the manufacturing of superefficient airplanes to include commercial airplanes in general.

The effect of ESSB 5952 is contingent upon the final decision to locate a significant commercial airplane manufacturing program in the state of Washington. If a decision to locate a significant commercial airplane manufacturing program is not made by June 30, 2017, ESSB 5952 is null and void. Furthermore, 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 and wing assembly of the airplane within the state.

#### Tax Preference Performance Statement.

In 2013 the Legislature passed ESSB 5882, which requires 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:**

"Commercial aircraft" is defined as a "commercial airplane" or "commercial rotorcraft."

"Commercial rotorcraft" is defined as an aircraft supported in flight by one or more rotors to provide lift, which may also include rotorcrafts with additional thrust engines or propellers, certified by the FAA for transporting persons or property, and any military derivative of such an aircraft.

The bill expands certain aerospace tax preferences to include the engineering, manufacturing, and repairing of commercial rotorcrafts as well as the research and design pertaining to commercial rotorcrafts. The following tax preferences are expanded to commercial rotorcrafts:

- Preferential B&O tax rate for the manufacturing, wholesaling, and retailing of commercial aircraft and aircraft components, and the tooling used in the manufacturing of commercial aircraft and aircraft components;
- Preferential B&O tax rate for aerospace product development;
- B&O tax credit for aerospace product development expenditures;
- B&O tax credit for property taxes and leasehold taxes on property used exclusively in manufacturing commercial aircraft or components of aircraft, aerospace product development, and the manufacturing of tooling;
- B&O tax credit on the sale of certain parts to manufacturers where final testing and inspection occurs out of state;
- B&O tax deduction for tax, interest, and fees on loans secured by commercial aircraft used to provide routine air service and owned by out of state air carriers;
- Sales tax exemption for computer equipment and software, and its installation, used primarily in the development of commercial aircraft and components; and
- Sales tax exemption for the construction of facilities used in the manufacturing of commercial aircraft, provided that the expansion of this exemption goes into effect pursuant to the contingency in ESSB 5952.

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

The contingent effective date in ESSB 5952 that requires the siting of a significant manufacturing program in the state to occur prior to the extension of certain tax preferences is modified by changing certain references to "commercial airplane" to "commercial aircraft," effectively allowing a significant manufacturing program to be created through qualifying rotorcraft manufacturing.

The effective dates in ESSB 5952 for the extension of certain preferences from 2024 to 2040 are mirrored in the bill.

The bill's tax preference performance statement specifies that the public policy objective is to create and retain jobs. The tax preference performance statement requires JLARC to assess employment changes and tax revenue changes in the commercial aircraft industry in comparison to employment and tax revenues prior to the extension of tax preferences to commercial rotorcrafts. To the extent practicable, JLARC must use data provided by state agencies responsible for administering unemployment insurance and collecting tax revenue as well data statistics provided by the Bureau of Labor Statistics.

**Appropriation:** None.

**Fiscal Note:** Received.

**Effective Date:** The bill takes effect July 1, 2014, except for the following sections:

- Section 4 takes effect July 1, 2015;
- Section 6 takes effect July 1, 2015 if the siting of a significant commercial airplane manufacturing program in the state of Washington occurs by June 30, 2017; and
- Sections 5, 9, 11, 14, 15, and 16 take effect upon the date of the siting of a significant commercial airplane manufacturing program in the state of Washington if it occurs by June 30, 2017.