



# Special Notice

WASHINGTON STATE DEPARTMENT OF REVENUE

JUNE 13, 2008

## Aerospace Manufacturers Tax Incentives

SSB 6828 (Chapter 81, Laws of 2008) broadens several existing aerospace tax incentives and requires business that take advantage of the incentives to file their return electronically (E-file). For manufacturers and processors for hire of commercial airplanes and component parts of commercial airplanes, the new law changed the definition of “preproduction development expenditures” and broadened it to include “aerospace product development expenditures.” This notice provides a comprehensive overview of the tax incentives available to aerospace manufacturers and processors for hire.

### Retail Sales and Use Tax Exemption for Computers

Effective December 1, 2003, manufacturers and processors for hire of commercial airplanes and component parts of commercial airplanes were eligible for a retail sales and use tax exemption on purchases of computer hardware, software and peripherals used primarily in the development, design and engineering of commercial airplanes and component parts of commercial airplanes.

Effective July 1, 2008, the exemption is broadened to include computer hardware, software and peripherals used primarily in the development, design and engineering of aerospace products or in providing aerospace services. The exemption also applies to charges for labor and services related to the installation of qualifying computer hardware, software and computer peripherals. Computer peripherals include keyboards, monitors, mouse devices, and other devices that operate outside the computer excluding cables, conduit, wiring, and similar property. The purchaser must provide the vendor with a completed **Buyers’ Retail Sales Tax Exemption Certificate**. This exemption expires July 1, 2024.

### Business and Occupation Tax Rate Decrease

The preferential business and occupation (B&O) tax rate for manufacturers and processors for hire of commercial airplanes or component parts of commercial airplanes is outlined below. The rate applies to both the manufacturing activity and the subsequent sale of the manufactured product by the manufacturer. The manufacturer is also eligible for the multiple activities tax credit (MATC). Persons who qualify for this B&O tax rate decrease should report the income under the Aerospace B&O tax classification on the Electronic Filing (E-file) return.

Period	Rate
December, 1, 2003 - September 30, 2005	.00484
October 1, 2005 - June 30, 2007	.004235 (reduction of 12.5%)
July 1, 2007 - June 30, 2024	.002904 (reduction of 40.0%)

The rate expires on July 1, 2024.

### Property and Leasehold Excise Tax B&O Tax Credits

The law provides a B&O tax credit equal to the property taxes paid on new buildings constructed after December 1, 2003, the land upon which the new buildings are located and the increased value of renovated

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buildings constructed after December 1, 2003 when the buildings, land and renovations are used exclusively in manufacturing commercial airplanes or component parts of commercial airplanes. RCW 82.04.4463.

The law also provides for a B&O tax credit on machinery and equipment acquired after December 1, 2003, used in manufacturing commercial airplanes or component parts of commercial airplanes. The amount of credit is equal to the amount of property taxes paid on the equipment exempt under the Manufacturers' Machinery and Equipment Sales and Use Tax Exemption (M&E), (see RCW 82.08.02565) multiplied by a fraction. The numerator of the fraction is the total taxable amount subject to the tax imposed under RCW 82.04.260(11) and the denominator of the fraction is the total taxable amount subject to the tax imposed under all manufacturing classifications in Chapter 82.04 RCW. The fraction for the year in which the credit is earned is calculated using amounts reported on the previous year's combined excise tax returns. If either the numerator or denominator of the fraction is zero, no credit is available. If the fraction is greater than or equal to nine-tenths, then the fraction is rounded to one.

This B&O tax credit cannot be claimed until the property taxes associated with the qualifying land, buildings or machinery and equipment have actually been paid. If a persons B&O tax obligation is less than the property taxes paid on qualifying property, the credit may carry forward one year but may not be carried over a second year. B&O tax refunds will not be granted in lieu of a credit for property taxes paid. These credits expire July 1, 2024.

### **Qualified Aerospace Product Development Expenditures B&O Tax Credit**

Effective December 1, 2003, the law provided a B&O tax credit equal to 1.5% of qualified preproduction development expenditures used in manufacturing commercial airplanes or component parts of commercial airplanes by manufacturers and processors for hire of commercial airplanes or component parts of commercial airplanes.

Effective July 1, 2008, SSB 6828 broadens the definition of qualified preproduction development expenditures to include aerospace product development expenditures.

“Qualified aerospace product development expenditures” are operating expenses, including wages, benefits, supplies and computer expenses, directly incurred in qualified aerospace product development by a person claiming the credit. The term includes expenses directly incurred in the discovery of technological information, the translating of technological information into new or improved products, processes, techniques, formulas, or inventions, and the adaptation of existing products and models into new products or new models, or derivatives of products or models. The term also includes expenditures for tool design and engineering design for the manufacturing process. However, the term does not include manufacturing expenditures or other production-oriented expenditures. Nor does the term include the cost of surveys and studies, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste and seasonal design. In addition, the term does not include capital costs and overhead, such as expenses for land, structures or depreciable property, or amounts paid to a person to conduct qualified aerospace product development, or to the state and any of its departments and institutions, other than a public educational or research institution.

Credit may not be claimed for expenditures claimed for purposes of the High Technology Research and Development B&O tax credit provided by RCW 82.04.4452.

Unused preproduction development expenditure credits accrued from December 1, 2003, through June 30, 2005, may be carried over until used. Unused preproduction development expenditure credits accrued after June 30, 2005, cannot be carried over beyond the calendar year in which they are accrued. The expenditures that qualify for the credit during the periods outlined above are only those defined as preproduction expenditures and not aerospace product development expenditures.

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Any unused aerospace product development expenditure credits accrued after July 1, 2008, cannot be carried over beyond the calendar year in which the qualifying expenditures are incurred.

The credit cannot exceed B&O taxes due. Pre-approval from the Department of Revenue is not required to use the credit, but a form prescribed by the Department of Revenue must be filed when the credit is taken. The form can be found within E-file on the “credits” page. This credit expires July 1, 2024.

### **Annual Reporting Requirements**

Manufacturers and processors for hire who report taxes under the preferential B&O tax rate or who claim a tax credit or exemption under the aerospace incentive program must submit an annual report to the Department of Revenue detailing employment, wages and employer-provided health and retirement benefits for employment positions in Washington.

The report must detail employment by the total number of full-time, part-time and temporary positions. The report shall not include names of employees. The report must be submitted by March 31 of each year.

The first report filed must include employment, wage and benefit information for the 12-month period immediately before first use of the decreased rate or tax credit programs listed above. This information is not subject to the confidentiality provisions of RCW 82.32.330 and may be disclosed to the public upon request.

### **Electronic Filing Required**

All reports and other such documents required by the Department of Revenue to take advantage of the aerospace tax incentives must be filed electronically.

### **Important Definitions**

“Aerospace product” means commercial airplanes and their components as defined in RCW 82.32.550; machinery and equipment that is designed and used primarily for the maintenance, repair overhaul or refurbishing of commercial airplanes or their components by federal aviation regulation (FAR) part 145 certificated repair stations; and tooling specifically designed for use in manufacturing commercial airplanes or their components.

“Providing aerospace services” means the maintenance, repair, overhaul, or refurbishing of commercial airplanes or their components, but only when such services are performed by a FAR part 145 certificated repair station.

“Aerospace product development” means research, design and engineering activities performed in relation to the development of an aerospace product, including prototype development, testing and certification. The term includes the discovery of technological information, the translating of technological information into new or improved products, processes, techniques, formulas, or inventions, and the adaptation of existing products and models into new products or new models or derivatives of products or models.

“Primarily” means greater than 50% of the equipment’s capacity or total time the equipment is used.

“Commercial airplane” means an airplane certified by the Federal Aviation Administration (FAA) for transporting persons or property or any military derivative of such an airplane.

“Component” means a part or system certified by the FAA for installation or assembly into a commercial airplane.