When making the decision on where to locate production activities, firms often consider state tax credits and state and local incentives. This chapter addresses these economic development activities, along with a discussion of state and local taxes. Because tax credits and incentives are generally taken as reductions to tax liabilities, they must be understood in the context of the broader tax climate of the location. We briefly discuss the historical use of tax credits and incentives to set the stage for the discussion of these issues with particular reference to JSF FACO.

Also in this chapter, we describe the specific tax and business incentives that would affect the costs of JSF FACO in Texas, California, and Georgia. We collected data from a number of sources in support of this analysis and gathered the tax information and program descriptions from the economic development offices in these states, from state Web sites, and from published sources. We also contacted Lockheed Martin and Northrop Grumman and local DCMA offices to learn about participation in these programs.

Tables 6.1–6.3 summarize the major taxes and incentive programs that would apply to FACO at the three potential locations of Fort Worth, Marietta, and Palmdale. The applicable tax liabilities and savings from economic development programs are incorporated into RAND cost estimates.
Table 6.1
State Taxes and Their Impact on JSF FACO

<table>
<thead>
<tr>
<th>Type of Tax</th>
<th>Basis of Application</th>
<th>California Rate</th>
<th>Applicable to JSF?</th>
<th>Georgia Rate</th>
<th>Applicable to JSF?</th>
<th>Texas Rate</th>
<th>Applicable to JSF?</th>
</tr>
</thead>
<tbody>
<tr>
<td>State/local sales taxes on real property</td>
<td>Purchase price</td>
<td>None</td>
<td>No</td>
<td>None</td>
<td>No</td>
<td>None</td>
<td>No</td>
</tr>
<tr>
<td>State/local property taxes on real property</td>
<td>Assessed value(^a)</td>
<td>1.10% annually on 100% of assessed value</td>
<td>Yes(^b)</td>
<td>Effective rate of 1.201% annually on 100% of assessed value</td>
<td>No: AFP 6 real property is not taxed</td>
<td>None</td>
<td>None/ exempt</td>
</tr>
<tr>
<td>State/local sales/use taxes on facilities, tooling, and equipment (contractor-owned)(^c)</td>
<td>Purchase price</td>
<td>8.25% at the time of purchase</td>
<td>Yes</td>
<td>5% at time of purchase</td>
<td>No(^d)</td>
<td>8.25% at time of purchase</td>
<td>No(^d)</td>
</tr>
<tr>
<td>State/local sales/use taxes on facilities, tooling and equipment (government-owned)</td>
<td>Purchase price</td>
<td>8.25% at the time of purchase</td>
<td>No(^e)</td>
<td>5% at time of purchase</td>
<td>No(^e)</td>
<td>8.25% at time of purchase</td>
<td>No(^e)</td>
</tr>
<tr>
<td>State/local property taxes on facilities, tooling, and equipment (contractor-owned)</td>
<td>Assessed value(^a)</td>
<td>1.10% annually</td>
<td>Yes</td>
<td>1.201% annually</td>
<td>Yes</td>
<td>2.64% annually</td>
<td>Yes</td>
</tr>
</tbody>
</table>
Table 6.1—continued

<table>
<thead>
<tr>
<th>Type of Tax</th>
<th>Basis of Application</th>
<th>California Rate</th>
<th>Applicable to JSF?</th>
<th>Georgia Rate</th>
<th>Applicable to JSF?</th>
<th>Texas Rate</th>
<th>Applicable to JSF?</th>
</tr>
</thead>
<tbody>
<tr>
<td>State/local property taxes on facilities, tooling, and equipment (government-owned)</td>
<td>Assessed value&lt;sup&gt;a&lt;/sup&gt;</td>
<td>1.10% annually</td>
<td>Yes&lt;sup&gt;b,e&lt;/sup&gt;</td>
<td>1.201% annually</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
<td>2.64% annually</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
</tr>
<tr>
<td>State/local sales/use taxes on raw material, purchased parts, and subassemblies</td>
<td>Purchase price</td>
<td>8.25% at time of purchase</td>
<td>No&lt;sup&gt;e,f&lt;/sup&gt;</td>
<td>5% at time of purchase</td>
<td>No&lt;sup&gt;e,f&lt;/sup&gt;</td>
<td>8.25% at time of purchase</td>
<td>No&lt;sup&gt;e,f&lt;/sup&gt;</td>
</tr>
<tr>
<td>Property taxes on raw material, purchased parts, and subassemblies</td>
<td>Purchase price&lt;sup&gt;a&lt;/sup&gt;</td>
<td>1.1% annually</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
<td>1.201% annually</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
<td>2.64% annually</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
</tr>
<tr>
<td>State/local sales tax on JSF sales to DoD</td>
<td>Sales price</td>
<td>8.25%</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
<td>5%</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
<td>8.25%</td>
<td>No&lt;sup&gt;e&lt;/sup&gt;</td>
</tr>
<tr>
<td>Corporate franchise/income taxes on JSF sales</td>
<td>Net income (sales price minus all costs)</td>
<td>8.84%</td>
<td>Yes</td>
<td>6%</td>
<td>Yes</td>
<td>4.50%</td>
<td>Yes&lt;sup&gt;h&lt;/sup&gt;</td>
</tr>
</tbody>
</table>

<sup>a</sup>For the purposes of modeling, this was assumed to be net book value.

<sup>b</sup>Although real property (land and improvements) located on government-owned facilities is normally not subject to property taxes, California taxes the “possessory interest” (value of the property) at the property tax rate.

<sup>c</sup>Handtools, office furniture, and equipment are already included in overhead rates and therefore taxes on these items are not included in the model.

<sup>d</sup>FACO purchases are exempt because—in Georgia and Texas—manufacturing machinery and equipment is exempt from state and local taxes.

<sup>e</sup>DoD will fund and retain title to the JSF tooling and equipment, parts, and subassemblies before use; therefore, it is not subject to state and local taxes.

<sup>f</sup>If sales taxes are applied on raw materials, they are already included in costs to the company.

<sup>g</sup>DoD is exempt from paying state or local sales taxes on purchases.

<sup>h</sup>Texas taxes corporations at the higher of either 0.25 percent of net taxable capital or on 4.5 percent of net income derived in Texas.
Table 6.2
California Tax Credits and Incentives

<table>
<thead>
<tr>
<th>Credit or Incentive</th>
<th>Basis of Application</th>
<th>Applicable to JSF FACO?</th>
<th>Credit/Incentive</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing investment credit on</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes</td>
<td>6% of purchase price and capitalized labor can be applied against California franchise (state income) tax liability</td>
<td>Limited to maximum of tax liability, may be carried over for eight years</td>
</tr>
<tr>
<td>manufacturing equipment and special-use aerospace buildings</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Research and development credits</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>No</td>
<td>11% of in-house costs; 24% for purchased efforts</td>
<td>JSF research and development to be accomplished in SDD phase in Fort Worth</td>
</tr>
<tr>
<td>JSF wage tax credit (expires in 2005)</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes (but credit will expire before FACO activities begin)</td>
<td>Percentage (50–10% declining, 10% annually from 2001–2006) of qualified wages (direct labor costs) not to exceed $10,000 per worker per year</td>
<td>Not applied in RAND cost model because it will expire</td>
</tr>
<tr>
<td>JSF property tax credit (expires in 2005)</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes (but credit will expire before FACO activities begin)</td>
<td>10% of the cost of qualified property (used 50% of the time or more in activities to manufacture the JSF)</td>
<td>Not applied in RAND cost model because it will expire</td>
</tr>
</tbody>
</table>
### Table 6.2—continued

<table>
<thead>
<tr>
<th>Credit or Incentive</th>
<th>Basis of Application</th>
<th>Applicable to JSF FACO?</th>
<th>Credit/Incentive</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Enterprise Zone Incentives</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State hiring tax credit</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes</td>
<td>$31,590 over first five years&lt;sup&gt;a&lt;/sup&gt;</td>
</tr>
<tr>
<td>Business equipment, furniture, and fixtures deduction</td>
<td>Deduction in year of purchase against revenue in calculating California franchise (state income) tax liability</td>
<td>Yes</td>
<td>40% of purchase price not to exceed $20,000 annually (onetime expense for each piece of equipment)</td>
</tr>
<tr>
<td>Net operating loss carryover</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes</td>
<td>Total offset against tax liability</td>
</tr>
<tr>
<td>State sales and use tax credit</td>
<td>Offset to California franchise (state income) tax liability</td>
<td>Yes</td>
<td>8% of purchase price, plus capitalized labor</td>
</tr>
</tbody>
</table>

<sup>a</sup>Credit is based on 50 percent of 150 percent of qualified wages (maximum of $6.75 per hour or minimum wage) for first year and declines to 40/30/20/10 percent, respectively, in next four successive years.

Experience at Palmdale indicates that about 20% of the hired workers qualify. Cannot be applied unless sales/use tax was paid on purchase; property may also be depreciated in subsequent years. Not applied in RAND cost model because information on California losses not available. First $20 million of purchases eligible for credit ($1.6 million maximum).
### Table 6.3
Georgia Tax Credits and Incentives

<table>
<thead>
<tr>
<th>Georgia Tier 4 Credits and Incentives&lt;sup&gt;a&lt;/sup&gt;</th>
<th>Basis of Application</th>
<th>Applicable to JSF?</th>
<th>Credit/Incentive</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Job tax credit</td>
<td>Offset to state income tax liability</td>
<td>Yes</td>
<td>$750 per job annually for five years following creation of the job</td>
<td>Limited to 50% of tax liability per year</td>
</tr>
<tr>
<td>Investment tax credit</td>
<td>Offset to state income tax liability</td>
<td>Yes</td>
<td>1% credit for each $50,000 investment (onetime); 3% for recycling, pollution control, and defense conversions</td>
<td>Only one of these three Georgia credits may be taken—this was the one used in the model</td>
</tr>
<tr>
<td>Optional investment tax credit</td>
<td>Offset to state income tax liability</td>
<td>Yes</td>
<td>See text for explanation</td>
<td></td>
</tr>
</tbody>
</table>

<sup>a</sup>Companies may only participate in one of these three programs.
STATE AND LOCAL ECONOMIC DEVELOPMENT

State and local governments regularly provide customized assistance to individual firms. Over the past 30 years, every state and almost all metropolitan areas have expanded the size and scope of economic development programs—i.e., those meant to induce businesses to locate (or remain) in their state or locality. Bartik (1991) describes three waves in this expansion. The first wave, occurring in the 1950s–1970s, included mainly financial assistance, such as tax relief or subsidizing business research. Before the 1970s, U.S. state and local governments, particularly in the South, developed financial programs to aggressively recruit manufacturing branch plants from the North.

Recessions and industrial restructuring during the 1970s and 1980s led states, during the second wave, to a significant expansion of financial programs and included nonfinancial incentives to start-up businesses, small businesses, and existing businesses. State and local governments cut back on many of these programs because of budgetary shortfalls from the 1990–1991 recession. In addition, critics of development programs argued that little evidence of the effectiveness of state and local economic development programs could be found, in part because these programs only directly benefited a relatively small number of businesses.

The third wave, in the 1990s, saw state and local governments outsourcing many development activities. Rather than having governments pay 100 percent of the costs of providing services to selected businesses, private or quasiprivate companies provided economic development with state or local governments’ guidance and subsidies.

Effectiveness of Development Programs

Today, state and local governments use these programs to compete with other states or localities for increased jobs in their jurisdictions. More jobs are expected to bring such benefits as lower local unemployment and increased wages, property values, profits for local businesses, and tax revenues—and reelection for the politicians who successfully attract new businesses.
The traditional economic view of state and local economic development programs is that, at best, they have no national benefit and, at worst, they are contrary to the national interest.\(^1\) There are three parts to this argument. First, from a national perspective, state and local economic development programs are thought to be a zero-sum game: one area’s benefits from gaining jobs are matched by another area’s costs from losing jobs. Second, more locally, the programs have little effect on the growth of a small region because state and local taxes are too small a percentage of business costs to affect business growth decisions, especially because these taxes are deductible from federal income tax. Third and most important, competition for jobs may lead to a “race to the bottom” that worsens the income distribution by lowering business-tax revenue and public expenditure levels.

Not all economists agree with the standard view. For example, Brennan and Buchanan (1980) suggest that the total size of government would be excessive in the absence of intergovernmental tax competition. More recently, Bartik (1991) argues that economic development can provide benefits, although these may not greatly outweigh the costs. Programs are not zero-sum if they provide jobs in depressed areas, where new jobs add most to overall national economic welfare. Bartik also points out that even small production cost differentials could be decisive in business location decisions if states and metropolitan areas are close substitutes.

STATE AND LOCAL TAXES IN CALIFORNIA, GEORGIA, AND TEXAS

Each state has a unique combination of tax instruments that vary by rates, bases, and—given that local governments may also tax businesses—by locality. State governments typically tax a portion of corporate net income based on the presence of that firm in the state. Local governments typically tax sales and property in their jurisdictions. In some states, property is also taxed at the state level.

To assess the impact of taxes on different FACO strategies, we examined the state and local tax rates and bases at the three potential

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\(^1\)See, for example, Oates, 1972; Zodrow and Mieszkowski, 1986; and Wilson, 1986.
FACO locations. Major taxes affecting FACO would be the state corporate income or franchise tax, state and local sales and use tax, and state and local property tax. AFACO locations. Major taxes affecting FACO would be the state corporate income or franchise tax, state and local sales and use tax, and state and local property tax.2 A summary of the relevant taxes for the three states is presented in Table 6.1.

State Franchise and Corporate Income Taxes

Generally, states tax net income earned in that state. The rules for determining taxable income base vary by state according to apportionment formulas that, for companies operating in more than one state, determine income earned in that state and state-specific deductions for business expenses and credits. Table 6.1 shows the state franchise tax rates for California, Georgia, and Texas. Corporations in Texas are taxed the greater of 0.25 percent of net taxable capital and 4.5 percent of net income derived in Texas.3 (In most years, Lockheed Martin has paid Texas franchise taxes according to the net income calculation.) Georgia’s corporate income tax rate is slightly higher, at 6 percent, while California has the highest franchise taxes of the three states, at 8.84 percent.

Property Taxes

States and localities may impose taxes on the assessed value of real and tangible “personal” property.4 Property taxes are determined by tax rates and assessment values that vary by location. In general, business personal property, such as machinery, equipment, and inventory, are assessed according to cost less depreciation. The value of real property, such as land and buildings, is determined by local appraisers according to the sales of comparable properties.5 Because we do not have data on comparable property, we assume that the taxable value for property for FACO is the cost less depreciation.

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2The employer’s share of workers’ compensation is included in the fringe rates.

3Taxable capital is a corporation’s state capital (capital stock) plus surplus. Surplus means the net assets of the company minus its members’ contributions.

4Businesses face tangible “personal” property taxes for all property that is not “real” property, which includes land and improvements to land.

5In California, growth in assessments is limited to 2 percent per year.
Texas has no state property tax. Furthermore, because the Lockheed Martin site in Fort Worth is in a federal enclave within AFP 4, it is exempt from local property taxes on its equipment. In California, the property tax is effectively a statewide tax. The state, city, county, and school districts all tax property in Georgia. Each government entity uses a different tax rate and assessment ratio. Table 6.1 reports the tax rates for each locality.

AFP 4 in Texas is exempt from property taxes. Property in Marietta is taxed at an effective rate $12.01 per $1,000 or 1.201 percent of assessed market value. However, real property on AFP 6 is exempt from Georgia property taxes. Property at the Palmdale location is taxed at 1.1 percent of assessed market value. In most states, like Texas and Georgia, the property for FACO activities that would be located on government-owned plants would not be subject to property taxes. However, California taxes the “possessory interests,” the value of government-owned property that is used by contractors. The tax rate and base are the same as if the property were privately owned. As will be discussed in the description of the cost analysis in Chapter Nine, property taxes on existing, privately owned property are already included in the overhead and are therefore addressed in the base rates in the cost model. Property taxes on new property for FACO are included in the calculation of the new effective overhead rates.

**Sales and Use Taxes**

Although sales taxes are collected at the time of purchase on goods and services, these taxes are not assessed on goods for which the title is passed to the government before use. Our analysis assumes that all manufacturing tooling and equipment purchased exclusively for the JSF will be owned by DoD and not subject to sales or use taxes. Therefore, these items are not eligible for sales or investment tax credits. There may be some non-JSF-specific facilities, tooling, and

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6Voters in local communities can increase property taxes with a two-thirds majority override referendum.

7Sales taxes are applied to gross receipts from retail sales of tangible personal property. Use taxes complement sales taxes. They are applied at the same rate as the sales tax for goods and services not subject to the sales tax, such as out-of-state or Internet
equipment purchased for FACO that could be used in nongovernmental programs. These items would be subject to sales or use taxes (as well as property taxes) and would be contractor-owned. However, these could qualify for tax credits.

TAX CREDITS AND DEDUCTIONS

State taxes cannot be evaluated alone without understanding the state tax benefits and state and local incentives offered to attract business. Generally, these are taken as a reduction in taxes, so merely looking at the tax rates fails to provide a complete picture of these costs of doing business.

State and Local Economic Development Programs

All three states use development programs to a greater or lesser extent to recruit businesses to relocate or expand in their jurisdiction. The states offer both tax credits and business incentives to firms in general; in specific industries, such as manufacturing; and in regions or enterprise zones. Of the three states, Texas offers the least-extensive tax credits and incentives applicable to JSF FACO activities, while California has the most generous package.

Texas

Limited development programs are available to Lockheed Martin in Texas. Most of the incentive programs in Texas are targeted to encourage development in rural areas, strategic investment areas, or enterprise zones. The Fort Worth site is not eligible for many franchise tax credits because it is not in these targeted areas. Texas established franchise tax credits for research and development conducted anywhere in the state. However, little research relating to FACO is expected during the production phase of the JSF program. Thus, these credits would not apply to FACO activities under study here.

purchases. Total state and local sales taxes are 8.25 percent in Palmdale, 5.00 percent in Marietta, and 8.25 percent in Fort Worth.
The Fort Worth site is in a federal enclave and is exempt from the local property taxes (the current local property tax rate for Tarrant County is $2.64 per $100). Thus, our model does not include any property tax liability for Lockheed Martin in Texas. Manufacturing equipment is exempt from sales and use tax in Texas.

**Georgia**

Georgia directs economic development toward counties in most need of economic growth. To determine need, the state ranks counties and census tracts into four economic tiers according to the unemployment rate, per-capita income, and percentage of residents below the poverty level. The Lockheed Martin–Marietta site is in Cobb County, which is ranked as a Tier 4 county. Counties with this ranking have the lowest unemployment rates, fewest poor residents, and highest per-capita income.

**Tier 4 Credits. Job Tax Credit.** Firms may reduce franchise taxes by $750 for each new job created if the jobs total 25 or more and the new jobs are held by residents in Cobb County. Credits are allowed for new full-time employee jobs for five years in years two through six following the creation of the jobs. In Tier 4 counties, the total credit amount may offset up to 50 percent of the state income tax liability in a taxable year.

**Investment Tax Credit.** This credit is based on the same tiers as the job tax credit program. The program allows existing manufacturing to obtain a credit against corporate income tax liability. Companies in Cobb County must invest $50,000 to receive a 1-percent tax credit. The credit increases to 3 percent for recycling, pollution control, and defense conversion activities.

**Optional Investment Tax Credit.** Firms in Cobb County that qualify for the investment tax credit and invest at least $20 million may choose this credit instead. The credit may be claimed for 10 years, provided the qualifying property remains in service throughout that period. The credit is calculated based on a three-year tax liability average. The annual credits are then determined using this base-year average. The credit available to the taxpayer in any given year is the minimum of: (1) the 90 percent of the increase in tax liability in the current taxable year over that in the base year; or (2) the excess of
the aggregate amount of the credit allowed over the sum of the amounts of credit already used in the years following the base year.

**Limitations.** Firms may only take advantage of one of these three programs. According to our analysis, the investment tax credit is likely to yield the largest savings. Hence, it is included in the cost analysis.

**Manufacturing Machinery and Computer Sales Tax Exemption.** These are exempt from sales and use tax in Georgia.

**California**

The California legislature offers an aggressive set of tax credit and business incentive programs to attract firms involved in aerospace manufacturing. This includes the statewide Manufacturers’ Investment Credit, Research and Development Credits, and Enterprise Zone programs. There are also tax credits directed specifically to the JSF, but these will expire before the production phase of the program starts, and are not expected to be renewed.

**Antelope Valley Enterprise Zone Development Programs.** California’s enterprise zone programs allow companies that are within any of the 39 designated zones incentives and programs not available to businesses outside of the zones. The Lockheed Martin and Northrop Grumman sites at Palmdale are located in the Antelope Valley Enterprise Zone (AVEZ) and would be eligible for many of the programs. The AVEZ was created in 1997 for a 15-year period, and thus would expire in 2012—in the middle of JSF FACO. The legislation allows for a single five-year extension if certain qualifications are met. The California legislature is considering extending these enterprise zone programs by five years for a total of 20 years. Given this history, we assume the enterprise zone will be renewed and therefore include these credits in our analysis up to 2017.

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8In a 1999 report, the city of Palmdale and the California Trade and Commerce Agency investigated the cost savings from California’s economic development programs. This study reported substantial program savings, but did not report on tax liabilities in California. Most of the programs would not apply to production (City of Palmdale and the California Trade and Commerce Agency, 1999).
State Hiring Tax Credit. Firms located in the AVEZ may reduce franchise taxes by a proportion of annual wage costs per qualified worker for the first 60 months that the worker is on the job. Qualified workers must

- Spend at least 90 percent of their time on activities related to businesses within the AVEZ
- Perform at least 50 percent of the work within the AVEZ
- When hired, fall into one of several targeted groups of workers, including veterans, displaced workers from military installation closures, and certain other unemployed workers.

The credit is a percentage of the smaller of the actual hourly wage paid or 150 percent of the minimum wage, which is $6.75 an hour. Actual wages paid to aircraft workers far exceed 150 percent of the minimum wage, so the amount based on the minimum wage would apply. The credit starts at 50 percent of the qualified wages, and declines to 40 percent the second year, 30 percent in the third year, 20 percent in the fourth year, 10 percent in the fifth year, and then disappears. Assuming no change in the minimum wage, the maximum benefit per worker would total $31,590 over five years. RAND received three estimates of the number of workers that would qualify for this credit. We used the average, 20 percent (which also was the median number) for both companies operating in Palmdale.

Business Expense Deductions. All firms in the AVEZ can deduct the cost of qualifying business equipment, furniture, and fixtures (or other depreciable personal property) as a business expense in the year they are placed into service. The maximum deduction is the lesser of 40 percent of the cost of the qualified property or $20,000 per year. We assume the maximum deduction of $20,000 per year. Property must be used within the enterprise zone.

Net Operating Loss Carryover. Firms in the AVEZ may carry 50 percent of a loss forward from one tax year to the next to offset income in the following years. As it is difficult to predict future business losses, no credit for this program is given in our analysis.

Other Major Statewide Development Programs. Manufacturing Investment Credit. The Manufacturing Investment Credit (MIC) is a
credit that can reduce a company’s California franchise taxes. This credit allows all manufacturers to deduct 6 percent of manufacturing equipment costs and also allows aerospace manufacturers to extend the credit to special-purpose buildings and foundation costs and capitalized labor costs that are directly applicable to the construction of manufacturing equipment or special-purpose buildings. To be eligible for the credit, firms must have paid California sales taxes or use taxes on the equipment purchases. The MIC may be claimed in addition to any enterprise zone franchise tax credits.

Research and Development Credit. California also provides firms supporting research conducted in the state a credit of 11 percent for research done in house and 24 percent for basic research payments to another entity. For fixed-price contracts, only a percentage of excess research costs would be allowable. This credit would not apply to the FACO activities because most or all research relating to FACO will be conducted during the program’s SDD phase. SDD activities will take place in Texas, and therefore this tax credit is not included in our analysis.

JSF Tax Credits. In 1998, the California Assembly passed Assembly Bill 2797, which created two new tax credits—the JSF Directed Wage Credit and JSF Directed Property Tax Credit—that would allow Lockheed Martin and other California-based subcontractors that manufacture components for ultimate use in the JSF program to deduct some wage and investment costs from franchise taxes. The JSF Directed Wage Credit would provide a credit against franchise taxes for direct labor costs for each employee who is at least 90 percent directly related to manufacturing property for ultimate use in the JSF. In 2001, the first year of the program, firms could take a credit equal to the lesser of $10,000 or 50 percent of a qualified employee’s annual wages. The allowable percentage declines 10 percent each year with the maximum allowable credit at $50,000 for wages in 2005. The JSF Directed Property Tax Credit would also apply toward franchise taxes. This is a credit for 10 percent of the cost of qualified property used to manufacture or assemble the JSF, including the labor and materials required to manufacture, assemble, and install the property. Qualified property includes tangible personal property used 50 percent of the time or more in activities to manufacture property for ultimate use in the JSF and the value of any capitalized labor costs that are direct costs allocable to manufacturing activities for the JSF.
Both of these credits expire January 1, 2006. Any unused credit may be carried forward until exhausted. To date, legislation has not extended these deadlines and thus these credits would not apply to FACO activities. Staff at the California Franchise Tax Board indicate that they consider it unlikely that these credits will be extended. Hence, the credits are not included in our analysis.

**SUMMARY**

Comparing the economic development programs across the states, it is clear that California offers the most aggressive economic development program for aerospace manufacturing. However, total tax liabilities are greater in California than in Georgia or Texas. It is RAND’s assessment that these benefits would not entirely offset these higher taxes.