

ASSEMBLY BILL

No. 485

Introduced by Assembly Member Runner

February 21, 2001

An act to amend Sections 17053.36, 17053.37, 23636, and 23637 of the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 485, as introduced, Runner. Income and bank and corporation taxes: credit: Joint Strike Fighter.

The Personal Income Tax Law and the Bank and Corporation Tax Law authorize various credits against the taxes imposed by those laws, including a credit against those taxes for each taxable year beginning on or after January 1, 2001, and before January 1, 2006, in an amount equal to a specified percentage of the qualified wages, as defined, paid or incurred during the taxable or income year or in connection with an initial contract or subcontract to manufacture property for ultimate use in a Joint Strike Fighter, as specified. The Personal Income Tax Law and the Bank and Corporation Tax Law also authorize a credit against the taxes imposed by those laws for each taxable year beginning on or after January 1, 2001, and before January 1, 2006, in an amount equal to 10% of the qualified cost, as provided, of property for use in the manufacture of a product for ultimate use in a Joint Strike Fighter, as specified, that is placed in service in this state.

This bill would change the operative date of these credits to apply to taxable years beginning before January 1, 2008.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. Section 17053.36 of the Revenue and Taxation
2 Code is amended to read:
3 17053.36. (a) For each taxable year beginning on or after
4 January 1, 2001, and before January 1, ~~2006~~ 2008, a qualified
5 taxpayer shall be allowed as a credit against the “net tax,” as
6 defined in Section 17039, an amount equal to the following:
7 (1) Fifty percent of qualified wages paid or incurred during any
8 taxable year beginning on or after January 1, 2001, and before
9 January 1, ~~2002~~ 2004.
10 (2) Forty percent of qualified wages paid or incurred during
11 any taxable year beginning on or after January 1, 2002, and before
12 January 1, ~~2003~~ 2005.
13 (3) Thirty percent of the qualified wages paid or incurred
14 during any taxable year beginning on or after January 1, 2003, and
15 before January 1, ~~2004~~ 2006.
16 (4) Twenty percent of the qualified wages paid or incurred
17 during any taxable year beginning on or after January 1, 2004, and
18 before January 1, ~~2005~~ 2007.
19 (5) Ten percent of the qualified wages paid or incurred during
20 any taxable year beginning on or after January 1, 2005, and before
21 January 1, ~~2006~~ 2008.
22 (b) For purposes of this section:
23 (1) (A) “Qualified taxpayer” means any taxpayer under an
24 initial contract or subcontract to manufacture property for ultimate
25 use in a Joint Strike Fighter.
26 (B) In the case of any pass-through entity, the determination of
27 whether a taxpayer is a qualified taxpayer under this section shall
28 be made at the entity level and any credit under this section or
29 Section 23636 shall be allowed to the pass-through entity and
30 passed through to the partners or shareholders in accordance with
31 applicable provisions of this part or Part 11 (commencing with
32 Section 23001). For purposes of this paragraph, “pass-through
33 entity” means any partnership or S corporation.
34 (2) “Qualified wages” means that portion of wages paid or
35 incurred by the qualified taxpayer during the taxable year with



1 respect to qualified employees that are direct costs as defined in
2 Section 263A of the Internal Revenue Code allocable to property
3 manufactured in this state by the qualified taxpayer for ultimate
4 use in a Joint Strike Fighter.

5 (3) “Qualified employee” means an individual whose services
6 for the qualified taxpayer are performed in this state and are at least
7 90 percent directly related to the qualified taxpayer’s contract or
8 subcontract to manufacture property for ultimate use in a Joint
9 Strike Fighter.

10 (4) “Joint Strike Fighter” means the next generation air
11 combat strike aircraft developed and produced under the Joint
12 Strike Fighter program.

13 (5) “Joint Strike Fighter program” means the multiservice,
14 multinational project conducted by the United States government
15 to develop and produce the next generation of air combat strike
16 aircraft.

17 (c) The credit allowed by this section shall not exceed ten
18 thousand dollars (\$10,000) per year, per qualified employee. For
19 employees that are qualified employees for part of a taxable year,
20 the credit shall not exceed ten thousand dollars (\$10,000)
21 multiplied by a fraction, the numerator of which is the number of
22 months of the taxable year that the employee is a qualified
23 employee and the denominator of which is 12.

24 (d) In the case where the credit allowed by this section exceeds
25 the “net tax,” the excess may be carried over to reduce the “net
26 tax” in the following year, and the seven succeeding years if
27 necessary, until the credit is exhausted.

28 (e) No credit shall be allowed unless the credit is reflected
29 within the bid upon which the qualified taxpayer’s contract or
30 subcontract to manufacture property for ultimate use in a Joint
31 Strike Fighter is based by reducing the amount of the bid by the
32 amount of the credit allowable.

33 (f) All references to the credit and ultimate cost reductions
34 incorporated into any successful bid that was awarded a contract
35 or subcontract and for which a qualified taxpayer is making a claim
36 shall be made available to the Franchise Tax Board upon request.

37 (g) This section shall remain in effect only until December 1,
38 ~~2006~~ 2008, and as of that date is repealed.

39 SEC. 2. Section 17053.37 of the Revenue and Taxation Code
40 is amended to read:



1 17053.37. (a) For each taxable year beginning on or after
2 January 1, 2001, and before January 1, ~~2006~~ 2008, a qualified
3 taxpayer shall be allowed as a credit against the “net tax,” as
4 defined in Section 17039, an amount¹ equal to 10 percent of the
5 qualified cost of qualified property that is placed in service in this
6 state.

7 (b) (1) For purposes of this section, “qualified cost” means
8 any costs that satisfy each of the following conditions:

9 (A) Except as otherwise provided in this subparagraph, is a cost
10 paid or incurred by the qualified taxpayer for the construction,
11 reconstruction, or acquisition of qualified property on or after
12 January 1, 2001, and before January 1, ~~2006~~ 2008. In the case of
13 any qualified property constructed, reconstructed, or acquired by
14 the qualified taxpayer (or any person related to the qualified
15 taxpayer within the meaning of Section 267 or 707 of the Internal
16 Revenue Code) pursuant to a binding contract in existence on or
17 before January 1, 2001, costs paid pursuant to that contract shall
18 be subject to allocation as follows. Contract costs shall be allocated
19 to qualified property based on a ratio of costs actually paid prior
20 to January 1, 2001, and total contract costs actually paid. “Cost
21 paid” shall include, without limitation, contractual deposits and
22 option payments. To the extent of costs allocated, whether or not
23 currently deductible or depreciable for tax purposes, to a period
24 prior to January 1, 2001, the cost shall be deemed allocated to
25 property acquired before January 1, 2001, and is thus not a
26 “qualified cost.”

27 (B) Except as provided in paragraph (2) of subdivision (d), is
28 an amount upon which the qualified taxpayer has paid, directly or
29 indirectly, as a separately stated contract amount or as determined
30 from the records of the qualified taxpayer, sales or use tax under
31 Part 1 (commencing with Section 6001).

32 (C) Is an amount properly chargeable to the capital account of
33 the qualified taxpayer.

34 (2) (A) For purposes of this subdivision, any contract entered
35 into on or after January 1, 2001, that is a successor or replacement
36 contract to a contract that was binding before January 1, 2001,
37 shall be treated as a binding contract in existence before January
38 1, 2001.

39 (B) If a successor or replacement contract is entered into on or
40 after January 1, 2001, and the subject of the successor or



1 replacement contract relates both to amounts for the construction,
2 reconstruction, or acquisition of qualified property described in
3 the original binding contract and to costs for the construction,
4 reconstruction, or acquisition of qualified property not described
5 in the original binding contract, then the portion of those amounts
6 described in the successor or replacement contract that were not
7 described in the original binding contract shall not be treated as
8 costs paid or incurred pursuant to a binding contract in existence
9 on or prior to January 1, 2001, under subparagraph (A) of
10 paragraph (1).

11 (3) (A) For purposes of this section, an option contract in
12 existence before January 1, 2001, under which a qualified taxpayer
13 (or any other person related to the qualified taxpayer within the
14 meaning of Section 267 or 707 of the Internal Revenue Code) had
15 an option to acquire qualified property, shall be treated as a binding
16 contract under the rules in paragraph (2). For purposes of this
17 subparagraph, an option contract shall not include an option under
18 which the optionholder will forfeit an amount less than 10 percent
19 of the fixed option price in the event the option is not exercised.

20 (B) For purposes of this section, a contract shall be treated as
21 binding even if the contract is subject to a condition.

22 (c) (1) For purposes of this section, “qualified taxpayer”
23 means any taxpayer under an initial contract or subcontract to
24 manufacture property for ultimate use in a Joint Strike Fighter.

25 (2) In the case of any pass-through entity, the determination of
26 whether a taxpayer is a qualified taxpayer under this section shall
27 be made at the entity level and any credit under this section or
28 Section 23637 shall be allowed to the pass-through entity and
29 passed through to the partners or shareholders in accordance with
30 applicable provisions of Part 10 (commencing with Section
31 17001) or Part 11 (commencing with Section 23001). For purposes
32 of this paragraph, the term “pass-through entity” means any
33 partnership or S corporation.

34 (3) The Franchise Tax Board may prescribe regulations to carry
35 out the purposes of this section, including any regulations
36 necessary to prevent the avoidance of the effect of this section
37 through splitups, shell corporations, partnerships, tiered
38 ownership structures, sale-leaseback transactions, or otherwise.

39 (d) (1) For purposes of this section, “qualified property”
40 means property that is described as either of the following:



1 (A) Tangible personal property that is defined in Section
2 1245(a)(3)(A) of the Internal Revenue Code for use by a qualified
3 taxpayer primarily in qualified activities to manufacture a product
4 for ultimate use in a Joint Strike Fighter.

5 (B) The value of any capitalized labor costs that are direct costs
6 as defined in Section 263A of the Internal Revenue Code allocable
7 to the construction or modification of property described in
8 subparagraph (A).

9 (2) Qualified property does not include any of the following:

10 (A) Furniture.

11 (B) Inventory.

12 (C) Equipment used to store finished products that have
13 completed the manufacturing process.

14 (D) Any tangible personal property that is used in
15 administration, general management, or marketing.

16 (e) For purposes of this section:

17 (1) “Fabricating” means to make, build, create, produce, or
18 assemble components or property to work in a new or different
19 manner.

20 (2) “Joint Strike Fighter” means the next generation air
21 combat strike aircraft developed and produced under the Joint
22 Strike Fighter program.

23 (3) “Joint Strike Fighter program” means the multiservice,
24 multinational project conducted by the United States government
25 to develop and produce the next generation of air combat strike
26 aircraft.

27 (4) “Manufacturing” means the activity of converting or
28 conditioning property by changing the form, composition, quality,
29 or character of the property for ultimate use in a Joint Strike
30 Fighter. Manufacturing includes any improvements to tangible
31 personal property that result in a greater service life or greater
32 functionality than that of the original property.

33 (5) “Primarily” means tangible personal property used 50
34 percent or more of the time in an activity described in
35 subparagraph (A) of paragraph (1) of subdivision (d).

36 (6) “Process” means the period beginning at the point at which
37 any raw materials are received by the qualified taxpayer and
38 introduced into the manufacturing, processing, or fabricating
39 activity of the qualified taxpayer and ending at the point at which
40 the manufacturing, processing, or fabricating activity of the



1 qualified taxpayer has altered tangible personal property to its
2 completed form, including packaging, if required. Raw materials
3 shall be considered to have been introduced into the process when
4 the raw materials are stored on the same premises where the
5 qualified taxpayer’s manufacturing, processing, or fabricating
6 activity is conducted. Raw materials that are stored on premises
7 other than where the qualified taxpayer’s manufacturing,
8 processing, or fabricating activity is conducted, shall not be
9 considered to have been introduced into the manufacturing,
10 processing, or fabricating process.

11 (7) “Processing” means the physical application of the
12 materials and labor necessary to modify or change the
13 characteristics of property.

14 (8) “Qualified activities” means manufacturing, processing,
15 or fabricating of property, beginning at the point at which any raw
16 materials are received by the qualified taxpayer and introduced
17 into the process and ending at the point at which the
18 manufacturing, processing, or fabricating has altered tangible
19 personal property to its completed form, including packaging, if
20 required.

21 (f) The credit allowed under subdivision (a) shall apply to
22 qualified property that is acquired by or subject to lease by a
23 qualified taxpayer, subject to the following special rules:

24 (1) A lessor of qualified property, irrespective of whether the
25 lessor is a qualified taxpayer, shall not be allowed the credit
26 provided under subdivision (a) with respect to any qualified
27 property leased to another qualified taxpayer.

28 (2) For purposes of paragraphs (2) and (3) of subdivision (b),
29 “binding contract” includes any lease agreement with respect to
30 the qualified property.

31 (3) (A) For purposes of determining the qualified cost paid or
32 incurred by a lessee in any leasing transaction that is not treated as
33 a sale under Part 1 (commencing with Section 6001), the following
34 rules shall apply:

35 (i) Except as provided by subparagraph (C) of this paragraph,
36 subparagraphs (A) and (C) of paragraph (1) of subdivision (b)
37 shall not apply.

38 (ii) Except as provided in subparagraph (B) and clause (iii), the
39 “qualified cost” upon which the lessee shall compute the credit
40 provided under this section shall be equal to the original cost to the



1 lessor (within the meaning of Section 18031) of the qualified
2 property that is the subject of the lease.

3 (iii) The requirement of subparagraph (B) of paragraph (1) of
4 subdivision (b) shall be treated as satisfied only if the lessor has
5 made a timely election under either Section 6094.1 or subdivision
6 (d) of Section 6244 and has paid sales tax reimbursement or use
7 tax measured by the purchase price of the qualified property
8 (within the meaning of paragraph (5) of subdivision (g) of Section
9 6006). For purposes of this subdivision, the amount of original
10 cost to the lessor which may be taken into account under clause (ii)
11 shall not exceed the purchase price upon which sales tax
12 reimbursement or use tax has been paid under the preceding
13 sentence.

14 (B) For purposes of applying subparagraph (A) only, the
15 following special rules shall apply:

16 (i) The original cost to the lessor of the qualified property shall
17 be reduced by the amount of any original cost of that property that
18 was taken into account by a predecessor lessee in computing the
19 credit allowable under this section.

20 (ii) Clause (i) shall not apply in any case where the predecessor
21 lessee was required to recapture the credit provided under this
22 section pursuant to the provisions of subdivision (g).

23 (iii) For purposes of this section only, in any case where a
24 successor lessor has acquired qualified property from a
25 predecessor lessor in a transaction not treated as a sale under Part
26 1 (commencing with Section 6001), the original cost to the
27 successor lessor of the qualified property shall be reduced by the
28 amount of the original cost of the qualified property that was taken
29 into account by any lessee of the predecessor lessor in computing
30 the credit allowable under this section.

31 (C) In determining the original cost of any qualified property
32 under this paragraph, only amounts paid or incurred by the lessor
33 on or after January 1, 2001, and before January 1, ~~2006~~ 2008, shall
34 be taken into account. In the case of any qualified property
35 constructed, reconstructed, or acquired by a lessor pursuant to a
36 binding contract in existence on or prior to January 1, 2001, the
37 allocation rule specified in subparagraph (A) of paragraph (1) of
38 subdivision (b) shall apply in determining the original cost to the
39 lessor of qualified property.



1 (D) Notwithstanding subparagraph (A), in the case of any
2 leasing transaction for which the lessee is allowed the credit under
3 this section and thereafter the lessee (or any party related to the
4 lessee within the meaning of Section 267 or 318 of the Internal
5 Revenue Code) acquires the qualified property from the lessor (or
6 any successor lessor) within one year from the date the qualified
7 property is first used by the lessee under the terms of the lease, the
8 lessee's (or related party's) acquisition of the qualified property
9 from the lessor (or successor lessor) shall be treated as a
10 disposition by the lessee of the qualified property that was subject
11 to the lease under subdivision (g).

12 (4) For purposes of determining the qualified cost paid or
13 incurred by a lessee in any leasing transaction that is treated as a
14 sale under Part 1 (commencing with Section 6001), the following
15 rules shall apply:

16 (A) Subparagraph (A) of paragraph (1) of subdivision (b) shall
17 be applied by substituting the term "purchase" for the term
18 "construction, reconstruction, or acquisition."

19 (B) Subparagraph (C) of paragraph (1) of subdivision (b) shall
20 apply.

21 (C) The requirement of subparagraph (B) of paragraph (1) of
22 subdivision (b) shall be treated as satisfied at the time that either
23 the lessor or the qualified taxpayer pays sales or use tax under Part
24 1 (commencing with Section 6001).

25 (5) (A) In the case of any leasing transaction described in
26 paragraph (3), the lessor shall provide a statement to the lessee
27 specifying the amount of the lessor's original cost of the qualified
28 property and the amount of that cost upon which a sales or use tax
29 was paid within 45 days after the close of the lessee's taxable year
30 in which the credit is allowable to the lessee under this section.

31 (B) The statement required under subparagraph (A) shall be
32 made available to the Franchise Tax Board upon request.

33 (g) No credit shall be allowed if the qualified property is
34 removed from the state, is disposed of to an unrelated party, or is
35 used for any purpose not qualifying for the credit provided in this
36 section in the same taxable year in which the taxpayer first places
37 the qualified property in service in this state. If any qualified
38 property for which a credit is allowed pursuant to this section is
39 thereafter removed from this state, disposed of to an unrelated
40 party, or used for any purpose not qualifying for the credit



1 provided in this section within one year from the date the taxpayer
2 first places the qualified property in service in this state, the
3 amount of the credit allowed by this section for that qualified
4 property shall be recaptured by adding that credit amount to the net
5 tax of the qualified taxpayer for the taxable year in which the
6 qualified property is disposed of, removed, or put to an ineligible
7 use.

8 (h) In the case where the credit allowed by this section exceeds
9 the “net tax,” the excess may be carried over to reduce the “net
10 tax” in the following year, and the seven succeeding years if
11 necessary, until the credit is exhausted.

12 (i) (1) No credit shall be allowed under this section if a credit
13 is claimed under Section 17053.49 in connection with the same
14 property.

15 (2) No credit shall be allowed unless the credit is reflected
16 within the bid upon which the qualified taxpayer’s contract or
17 subcontract to manufacture property for ultimate use in a Joint
18 Strike Fighter is based by reducing the amount of the bid by the
19 amount of the credit allowable.

20 (j) All references to the credit and ultimate cost reductions
21 incorporated into any successful bid that was awarded a contract
22 or subcontract and for which a qualified taxpayer is making a claim
23 shall be made available to the Franchise Tax Board upon request.

24 (k) This section shall remain in effect only until December 1,
25 ~~2006~~ 2008, and as of that date is repealed.

26 SEC. 3. Section 23636 of the Revenue and Taxation Code is
27 amended to read:

28 23636. (a) For each taxable year beginning on or after
29 January 1, 2001, and before January 1, ~~2006~~ 2008, a qualified
30 taxpayer shall be allowed as a credit against the “tax,” as defined
31 in Section 23036, an amount equal to the following:

32 (1) Fifty percent of qualified wages paid or incurred during any
33 taxable year beginning on or after January 1, 2001, and before
34 January 1, ~~2002~~ 2004.

35 (2) Forty percent of qualified wages paid or incurred during
36 any taxable year beginning on or after January 1, 2002, and before
37 January 1, ~~2003~~ 2005.

38 (3) Thirty percent of the qualified wages paid or incurred
39 during any taxable year beginning on or after January 1, 2003, and
40 before January 1, ~~2004~~ 2006.



1 (4) Twenty percent of the qualified wages paid or incurred
2 during any taxable year beginning on or after January 1, 2004, and
3 before January 1, ~~2005~~ 2007.

4 (5) Ten percent of the qualified wages paid or incurred during
5 any taxable year beginning on or after January 1, 2005, and before
6 January 1, ~~2006~~ 2008.

7 (b) For purposes of this section:

8 (1) (A) “Qualified taxpayer” means any taxpayer under an
9 initial contract or subcontract to manufacture property for ultimate
10 use in a Joint Strike Fighter.

11 (B) In the case of any pass-through entity, the determination of
12 whether a taxpayer is a qualified taxpayer under this section shall
13 be made at the entity level and any credit under this section or
14 Section 17053.36 shall be allowed to the pass-through entity and
15 passed through to the partners or shareholders in accordance with
16 applicable provisions of Part 10 (commencing with Section
17 17001) or this part. For purposes of this paragraph, “pass-through
18 entity” means any partnership or S corporation.

19 (2) “Qualified wages” means that portion of wages paid or
20 incurred by the qualified taxpayer during the taxable year with
21 respect to qualified employees that are direct costs as defined in
22 Section 263A of the Internal Revenue Code allocable to property
23 manufactured in this state by the qualified taxpayer for ultimate
24 use in a Joint Strike Fighter.

25 (3) “Qualified employee” means an individual whose services
26 for the qualified taxpayer are performed in this state and are at least
27 90 percent directly related to the qualified taxpayer’s contract or
28 subcontract to manufacture property for ultimate use in a Joint
29 Strike Fighter.

30 (4) “Joint Strike Fighter” means the next generation air
31 combat strike aircraft developed and produced under the Joint
32 Strike Fighter program.

33 (5) “Joint Strike Fighter program” means the multiservice,
34 multinational project conducted by the United States government
35 to develop and produce the next generation of air combat strike
36 aircraft.

37 (c) The credit allowed by this section shall not exceed ten
38 thousand dollars (\$10,000) per year, per qualified employee. For
39 employees that are qualified employees for part of a taxable year,
40 the credit shall not exceed ten thousand dollars (\$10,000)



1 multiplied by a fraction, the numerator of which is the number of
2 months of the taxable year that the employee is a qualified
3 employee and the denominator of which is 12.

4 (d) In the case where the credit allowed by this section exceeds
5 the “tax,” the excess may be carried over to reduce the “tax” in
6 the following year, and the seven succeeding years if necessary,
7 until the credit is exhausted.

8 (e) No credit shall be allowed unless the credit is reflected
9 within the bid upon which the qualified taxpayer’s contract or
10 subcontract to manufacture property for ultimate use in a Joint
11 Strike Fighter is based by reducing the amount of the bid by the
12 amount of the credit allowable.

13 (f) All references to the credit and ultimate cost reductions
14 incorporated into any successful bid that was awarded a contract
15 or subcontract and for which a qualified taxpayer is making a claim
16 shall be made available to the Franchise Tax Board upon request.

17 (g) This section shall remain in effect only until December 1,
18 ~~2006~~ 2008, and as of that date is repealed.

19 SEC. 4. Section 23637 of the Revenue and Taxation Code is
20 amended to read:

21 23637. (a) For each taxable year beginning on or after
22 January 1, 2001, and before January 1, ~~2006~~ 2008, a qualified
23 taxpayer shall be allowed as a credit against the “tax,” as defined
24 in Section 23036, an amount equal to 10 percent of the qualified
25 cost of qualified property that is placed in service in this state.

26 (b) (1) For purposes of this section, “qualified cost” means
27 any costs that satisfy each of the following conditions:

28 (A) Except as otherwise provided in this subparagraph, is a cost
29 paid or incurred by the qualified taxpayer for the construction,
30 reconstruction, or acquisition of qualified property on or after
31 January 1, 2001, and before January 1, ~~2006~~ 2008. In the case of
32 any qualified property constructed, reconstructed, or acquired by
33 the qualified taxpayer (or any person related to the qualified
34 taxpayer within the meaning of Section 267 or 707 of the Internal
35 Revenue Code) pursuant to a binding contract in existence on or
36 before January 1, 2001, costs paid pursuant to that contract shall
37 be subject to allocation as follows. Contract costs shall be allocated
38 to qualified property based on a ratio of costs actually paid prior
39 to January 1, 2001, and total contract costs actually paid. “Cost
40 paid” shall include, without limitation, contractual deposits and



1 option payments. To the extent of costs allocated, whether or not
2 currently deductible or depreciable for tax purposes, to a period
3 prior to January 1, 2001, the cost shall be deemed allocated to
4 property acquired before January 1, 2001, and is thus not a
5 “qualified cost.”

6 (B) Except as provided in paragraph (2) of subdivision (d), is
7 an amount upon which the qualified taxpayer has paid, directly or
8 indirectly, as a separately stated contract amount or as determined
9 from the records of the qualified taxpayer, sales or use tax under
10 Part 1 (commencing with Section 6001).

11 (C) Is an amount properly chargeable to the capital account of
12 the qualified taxpayer.

13 (2) (A) For purposes of this subdivision, any contract entered
14 into on or after January 1, 2001, that is a successor or replacement
15 contract to a contract that was binding before January 1, 2001,
16 shall be treated as a binding contract in existence before January
17 1, 2001.

18 (B) If a successor or replacement contract is entered into on or
19 after January 1, 2001, and the subject of the successor or
20 replacement contract relates both to amounts for the construction,
21 reconstruction, or acquisition of qualified property described in
22 the original binding contract and to costs for the construction,
23 reconstruction, or acquisition of qualified property not described
24 in the original binding contract, then the portion of those amounts
25 described in the successor or replacement contract that were not
26 described in the original binding contract shall not be treated as
27 costs paid or incurred pursuant to a binding contract in existence
28 on or prior to January 1, 2001, under subparagraph (A) of
29 paragraph (1).

30 (3) (A) For purposes of this section, an option contract in
31 existence before January 1, 2001, under which a qualified taxpayer
32 (or any other person related to the qualified taxpayer within the
33 meaning of Section 267 or 707 of the Internal Revenue Code) had
34 an option to acquire qualified property, shall be treated as a binding
35 contract under the rules in paragraph (2). For purposes of this
36 subparagraph, an option contract shall not include an option under
37 which the optionholder will forfeit an amount less than 10 percent
38 of the fixed option price in the event the option is not exercised.

39 (B) For purposes of this section, a contract shall be treated as
40 binding even if the contract is subject to a condition.



1 (c) (1) For purposes of this section, “qualified taxpayer”
2 means any taxpayer under an initial contract or subcontract to
3 manufacture property for ultimate use in a Joint Strike Fighter.

4 (2) In the case of any pass-through entity, the determination of
5 whether a taxpayer is a qualified taxpayer under this section shall
6 be made at the entity level and any credit under this section or
7 Section 17053.37 shall be allowed to the pass-through entity and
8 passed through to the partners or shareholders in accordance with
9 applicable provisions of Part 10 (commencing with Section
10 17001) or Part 11 (commencing with Section 23001). For purposes
11 of this paragraph, the term “pass-through entity” means any
12 partnership or S corporation.

13 (3) The Franchise Tax Board may prescribe regulations to carry
14 out the purposes of this section, including any regulations
15 necessary to prevent the avoidance of the effect of this section
16 through splitups, shell corporations, partnerships, tiered
17 ownership structures, sale-leaseback transactions, or otherwise.

18 (d) (1) For purposes of this section, “qualified property”
19 means property that is described as either of the following:

20 (A) Tangible personal property that is defined in Section
21 1245(a)(3)(A) of the Internal Revenue Code for use by a qualified
22 taxpayer primarily in qualified activities to manufacture a product
23 for ultimate use in a Joint Strike Fighter.

24 (B) The value of any capitalized labor costs that are direct costs
25 as defined in Section 263A of the Internal Revenue Code allocable
26 to the construction or modification of property described in
27 subparagraph (A).

28 (2) Qualified property does not include any of the following:

29 (A) Furniture.

30 (B) Inventory.

31 (C) Equipment used to store finished products that have
32 completed the manufacturing process.

33 (D) Any tangible personal property that is used in
34 administration, general management, or marketing.

35 (e) For purposes of this section:

36 (1) “Fabricating” means to make, build, create, produce, or
37 assemble components or property to work in a new or different
38 manner.



1 (2) “Joint Strike Fighter” means the next generation air
2 combat strike aircraft developed and produced under the Joint
3 Strike Fighter program.

4 (3) “Joint Strike Fighter program” means the multiservice,
5 multinational project conducted by the United States government
6 to develop and produce the next generation of air combat strike
7 aircraft.

8 (4) “Manufacturing” means the activity of converting or
9 conditioning property by changing the form, composition, quality,
10 or character of the property for ultimate use in a Joint Strike
11 Fighter. Manufacturing includes any improvements to tangible
12 personal property that result in a greater service life or greater
13 functionality than that of the original property.

14 (5) “Primarily” means tangible personal property used 50
15 percent or more of the time in an activity described in
16 subparagraph (A) of paragraph (1) of subdivision (d).

17 (6) “Process” means the period beginning at the point at which
18 any raw materials are received by the qualified taxpayer and
19 introduced into the manufacturing, processing, or fabricating
20 activity of the qualified taxpayer and ending at the point at which
21 the manufacturing, processing, or fabricating activity of the
22 qualified taxpayer has altered tangible personal property to its
23 completed form, including packaging, if required. Raw materials
24 shall be considered to have been introduced into the process when
25 the raw materials are stored on the same premises where the
26 qualified taxpayer’s manufacturing, processing, or fabricating
27 activity is conducted. Raw materials that are stored on premises
28 other than where the qualified taxpayer’s manufacturing,
29 processing, or fabricating activity is conducted, shall not be
30 considered to have been introduced into the manufacturing,
31 processing, or fabricating process.

32 (7) “Processing” means the physical application of the
33 materials and labor necessary to modify or change the
34 characteristics of property.

35 (8) “Qualified activities” means manufacturing, processing,
36 or fabricating of property, beginning at the point at which any raw
37 materials are received by the qualified taxpayer and introduced
38 into the process and ending at the point at which the
39 manufacturing, processing, or fabricating has altered tangible



1 personal property to its completed form, including packaging, if
2 required.

3 (f) The credit allowed under subdivision (a) shall apply to
4 qualified property that is acquired by or subject to lease by a
5 qualified taxpayer, subject to the following special rules:

6 (1) A lessor of qualified property, irrespective of whether the
7 lessor is a qualified taxpayer, shall not be allowed the credit
8 provided under subdivision (a) with respect to any qualified
9 property leased to another qualified taxpayer.

10 (2) For purposes of paragraphs (2) and (3) of subdivision (b),
11 “binding contract” includes any lease agreement with respect to
12 the qualified property.

13 (3) (A) For purposes of determining the qualified cost paid or
14 incurred by a lessee in any leasing transaction that is not treated as
15 a sale under Part 1 (commencing with Section 6001), the following
16 rules shall apply:

17 (i) Except as provided by subparagraph (C) of this paragraph,
18 subparagraphs (A) and (C) of paragraph (1) of subdivision (b)
19 shall not apply.

20 (ii) Except as provided in subparagraph (B) and clause (iii), the
21 “qualified cost” upon which the lessee shall compute the credit
22 provided under this section shall be equal to the original cost to the
23 lessor (within the meaning of Section 18031) of the qualified
24 property that is the subject of the lease.

25 (iii) The requirement of subparagraph (B) of paragraph (1) of
26 subdivision (b) shall be treated as satisfied only if the lessor has
27 made a timely election under either Section 6094.1 or subdivision
28 (d) of Section 6244 and has paid sales tax reimbursement or use
29 tax measured by the purchase price of the qualified property
30 (within the meaning of paragraph (5) of subdivision (g) of Section
31 6006). For purposes of this subdivision, the amount of original
32 cost to the lessor which may be taken into account under clause (ii)
33 shall not exceed the purchase price upon which sales tax
34 reimbursement or use tax has been paid under the preceding
35 sentence.

36 (B) For purposes of applying subparagraph (A) only, the
37 following special rules shall apply:

38 (i) The original cost to the lessor of the qualified property shall
39 be reduced by the amount of any original cost of that property that



1 was taken into account by a predecessor lessee in computing the
2 credit allowable under this section.

3 (ii) Clause (i) shall not apply in any case where the predecessor
4 lessee was required to recapture the credit provided under this
5 section pursuant to the provisions of subdivision (g).

6 (iii) For purposes of this section only, in any case where a
7 successor lessor has acquired qualified property from a
8 predecessor lessor in a transaction not treated as a sale under Part
9 1 (commencing with Section 6001), the original cost to the
10 successor lessor of the qualified property shall be reduced by the
11 amount of the original cost of the qualified property that was taken
12 into account by any lessee of the predecessor lessor in computing
13 the credit allowable under this section.

14 (C) In determining the original cost of any qualified property
15 under this paragraph, only amounts paid or incurred by the lessor
16 on or after January 1, 2001, and before January 1, ~~2006~~ 2008, shall
17 be taken into account. In the case of any qualified property
18 constructed, reconstructed, or acquired by a lessor pursuant to a
19 binding contract in existence on or prior to January 1, 2001, the
20 allocation rule specified in subparagraph (A) of paragraph (1) of
21 subdivision (b) shall apply in determining the original cost to the
22 lessor of qualified property.

23 (D) Notwithstanding subparagraph (A), in the case of any
24 leasing transaction for which the lessee is allowed the credit under
25 this section and thereafter the lessee (or any party related to the
26 lessee within the meaning of Section 267 or 318 of the Internal
27 Revenue Code) acquires the qualified property from the lessor (or
28 any successor lessor) within one year from the date the qualified
29 property is first used by the lessee under the terms of the lease, the
30 lessee's (or related party's) acquisition of the qualified property
31 from the lessor (or successor lessor) shall be treated as a
32 disposition by the lessee of the qualified property that was subject
33 to the lease under subdivision (g).

34 (4) For purposes of determining the qualified cost paid or
35 incurred by a lessee in any leasing transaction that is treated as a
36 sale under Part 1 (commencing with Section 6001), the following
37 rules shall apply:

38 (A) Subparagraph (A) of paragraph (1) of subdivision (b) shall
39 be applied by substituting the term "purchase" for the term
40 "construction, reconstruction, or acquisition."



1 (B) Subparagraph (C) of paragraph (1) of subdivision (b) shall
2 apply.

3 (C) The requirement of subparagraph (B) of paragraph (1) of
4 subdivision (b) shall be treated as satisfied at the time that either
5 the lessor or the qualified taxpayer pays sales or use tax under Part
6 1 (commencing with Section 6001).

7 (5) (A) In the case of any leasing transaction described in
8 paragraph (3), the lessor shall provide a statement to the lessee
9 specifying the amount of the lessor's original cost of the qualified
10 property and the amount of that cost upon which a sales or use tax
11 was paid within 45 days after the close of the lessee's taxable year
12 in which the credit is allowable to the lessee under this section.

13 (B) The statement required under subparagraph (A) shall be
14 made available to the Franchise Tax Board upon request.

15 (g) No credit shall be allowed if the qualified property is
16 removed from the state, is disposed of to an unrelated party, or is
17 used for any purpose not qualifying for the credit provided in this
18 section in the same taxable year in which the taxpayer first places
19 the qualified property in service in this state. If any qualified
20 property for which a credit is allowed pursuant to this section is
21 thereafter removed from this state, disposed of to an unrelated
22 party, or used for any purpose not qualifying for the credit
23 provided in this section within one year from the date the taxpayer
24 first places the qualified property in service in this state, the
25 amount of the credit allowed by this section for that qualified
26 property shall be recaptured by adding that credit amount to the tax
27 of the qualified taxpayer for the taxable year in which the qualified
28 property is disposed of, removed, or put to an ineligible use.

29 (h) In the case where the credit allowed by this section exceeds
30 the "tax," the excess may be carried over to reduce the "tax" in
31 the following year, and the seven succeeding years if necessary,
32 until the credit is exhausted.

33 (i) (1) No credit shall be allowed under this section if a credit
34 is claimed under Section 23649 in connection with the same
35 property.

36 (2) No credit shall be allowed unless the credit is reflected
37 within the bid upon which the qualified taxpayer's contract or
38 subcontract to manufacture property for ultimate use in a Joint
39 Strike Fighter is based by reducing the amount of the bid by the
40 amount of the credit allowable.



1 (j) All references to the credit and ultimate cost reductions
2 incorporated into any successful bid that was awarded a contract
3 or subcontract and for which a qualified taxpayer is making a claim
4 shall be made available to the Franchise Tax Board upon request.

5 (k) This section shall remain in effect only until December 1,
6 ~~2006~~ 2008, and as of that date is repealed.

7 SEC. 5. This act provides for a tax levy within the meaning of
8 Article IV of the Constitution and shall go into immediate effect.

O

