PROPERTY FOR USE IN SPACE FLIGHT EXEMPTION

EVALUATION SUMMARY | APRIL 2022 | 2022-TE23

TAX TYPE	Sales and use	REVENUE IMPACT (TAX YEAR 2019)	$12,000
YEAR ENACTED	2014		
REPEAL/EXPIRATION DATE	None	NUMBER OF TAXPAYERS	Could not determine

KEY CONCLUSION: Due to its minimal use, the exemption has not yet provided a significant benefit to the aerospace industry in the state. However, if space vehicle launches in Colorado increase in the future, the exemption would likely provide a more substantial benefit and industry stakeholders indicated that the exemption is important for the continued development of the aerospace industry in the state.

WHAT DOES THE TAX EXPENDITURE DO?

The Property for Use in Space Flight Exemption (Space Flight Exemption) [Section 39-26-728, C.R.S.] exempts the sale, storage, and use of qualified property for use in space flight from sales and use tax. Statute defines space flight as "any flight designed for suborbital, orbital, or interplanetary travel by a space vehicle," and defines space vehicle as "any tangible personal property that has space flight capability and is intended for space flight. . ." [Section 39-26-728(2)(b)&(c), C.R.S.]. The exemption includes the space vehicle and any of its components, tangible personal property to be placed aboard the vehicle, and fuel intended for space flight.

WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

The legislative declaration of House Bill 14-1178, which created the exemption, stated that, "Colorado has the potential to and should become a leader in the aerospace industry" and goes on to say "A sales and use tax exemption for qualified property for use in space flight will increase the availability of highly-skilled and highly-paid jobs in the state and will encourage capital investment in equipment, machinery, parts, and supplies used in aerospace manufacturing."

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations on this evaluation.

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EVALUATION RESULTS

WHAT IS THE TAX EXPENDITURE?

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In addition to providing a state-level sales and use tax exemption, under Section 29-2-105(1)(d)(I), C.R.S., local governments that have their sales taxes collected by the State have the option of adopting ordinances to apply the exemption to their sales taxes as well. As of January 1, 2022, three of 158 state-collected cities, and two of 53 state-collected counties have adopted this exemption. Under Article XX, Section 6 of the Colorado Constitution, home rule cities and counties that do not have their sales taxes collected by the State can set their own tax policies independently from the State and are not required to provide a similar exemption. We did not identify any home rule cities and counties that have adopted a similar exemption.

Vendors apply the exemption at the time of purchase and report sales to the consumers on line 9 of Schedule B of the Colorado Retail Sales Tax Return [DR 0100] or the Itemized Deductions and Exemptions Schedules of the Retailer's Use Tax Return [DR 0173]. Taxpayers who qualify for a use tax exemption for eligible space property are generally not required to file any form with the Department.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Based on the legislative declaration of House Bill 14-1178, we considered the direct beneficiaries of the exemption to be businesses within the private aerospace industry in Colorado, with the intent that encouraging aerospace industry growth would benefit the State's economy. Specifically, the legislative declaration states, "Studies indicate that the state would benefit significantly from private-oriented and state-implemented incentives designed to stimulate private-sector aerospace industry growth." [House Bill 14-1178].

According to a 2020 Metro Denver Economic Development Corporation report, the Colorado aerospace industry directly employs 33,460 workers at 290 companies, having the highest direct aerospace employment concentration in the U.S. Additionally, a report from the Brookings Institute determined that the Colorado aerospace industry reached an output of $8.7 billion – 3.8 percent of Colorado's GDP in 2011. Further, several aerospace businesses in Colorado are active in developing vehicles and other equipment used in space flight and, in recent years, there have been efforts to establish Colorado as a location for launching space vehicles. Specifically, the Colorado Air and Space Port in Adams County, previously known as Front Range Airport, received Federal Aviation Administration designation as a spaceport in 2018, although it has not yet been used for this purpose.

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IS THE TAX EXPENDITURE MEETING ITS PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We found that the exemption has not yet achieved its purpose because it is not widely used. However, usage of the exemption could increase if Colorado becomes established as a launching place for space vehicles and stakeholders indicated that the exemption is important for the continued development of Colorado's aerospace industry.

Statute does not provide quantifiable performance measures for this exemption. Therefore, we created and applied the following performance measures to determine the extent to which the exemption is meeting its purpose.

PERFORMANCE MEASURE: *To what extent has the Space Flight Exemption encouraged growth of the aerospace industry in Colorado?*

RESULT: This exemption has not provided a significant economic benefit to the aerospace industry in Colorado because it has not been widely used. Specifically, although the Department lacked data on the number of taxpayers that received the exemption because vendors are not required to report this information, the Department reported that taxpayers received a benefit of about $12,000 from the exemption based on about $414,000 in eligible sales during Tax Year 2019, the most recent year for which it had data. These are small figures relative to the high cost of property in the industry; a weather satellite, for instance, can cost nearly $300 million. Further, some taxpayers may have also been exempt from use tax under the exemption, for example, because they purchased qualifying space property in another state and brought it into Colorado for use or storage. While we could not determine the number of taxpayers that were exempt from use tax because taxpayers are generally not required to report use tax exemptions under the Space Flight Exemption to the Department, based on our conversations with stakeholders, it appears that few taxpayers use or store finished space property in the state such that it would be subject to use tax, regardless of the exemption.

Although industry stakeholders we contacted were aware of the exemption, currently, launches of space vehicles occur almost exclusively outside of Colorado. Therefore, while space vehicles and their components are often built in Colorado, they are typically sold to customers outside the state, meaning that most sales are not subject to sales tax in Colorado regardless of the exemption. Furthermore, the materials Colorado businesses purchase to build space vehicles are generally already exempt from sales tax under the Wholesale Sales Exemption [Section 39-26-102(20)(a), C.R.S.]. This appears to be similar to what was occurring in 2014 when the exemption was established, with the fiscal note of House Bill 14-1178 reporting that there were very few sales of completed space property occurring within the state.

If Colorado were to see an increased prevalence of launches, the exemption would likely be claimed considerably more frequently since more transactions that would otherwise be subject to sales tax would occur in the state. Similarly, stakeholders reported that they do not currently conduct much testing or storage of equipment used in space flight in Colorado, but this could become more common if Colorado becomes a location for launches. For these activities, businesses would likely benefit from being exempt from use tax which could otherwise apply to property that they purchase in another state but bring into Colorado.

We spoke with stakeholders, including an economic development representative, launch facility operations staff, and private businesses in the state, who reported that the exemption is important for the long-term effort to grow the aerospace and spaceflight industry in the state. With the establishment of the Colorado Air and Space Port, stakeholders indicated that Colorado has the potential to become a destination for launching space vehicles. Although the exemption is currently not frequently used, they felt the exemption is a key financial incentive in attracting businesses to Colorado who could benefit from it in the future, citing a lack of other cash incentives. However, stakeholders also acknowledged that other factors, in addition to the exemption, made Colorado an attractive place to do business, including having a well-educated and experienced work force and proximity to other companies in the aerospace industry.

We also found that the aerospace industry in Colorado has grown significantly since the implementation of the Space Flight Exemption, despite the limited use of the exemption. According to Metro Denver Economic Development Corporation reports, employment in the industry increased about 30 percent from 2015 to 2020 (12 percentage points above national average), with 10 percent of the growth being from Calendar Year 2019 to 2020 (6 percentage points above the national average). This is a significant increase from the Calendar Year 2009 through 2014 period, which saw a decrease in employment in the industry of 3.5 percent. Therefore, it appears that, although the exemption could encourage future aerospace industry growth within the space flight sector, the broader aerospace industry has grown without receiving a significant financial benefit from the exemption.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURE?

According to the Department of Revenue’s 2020 Tax Profile & Expenditure Report, the Space Flight Exemption resulted in $12,000 in forgone state revenue and a corresponding benefit to claimants of the exemption in Tax Year 2019, the most recent year with available data.

The exemption also reduces local government sales tax revenue and provides a corresponding benefit to claimants in three cities and two counties for which the State collects sales taxes that have adopted the exemption, although we lacked information necessary to quantify this impact.

Due to the limited benefit it provides, the exemption currently has a relatively small economic impact. However, as mentioned above, the revenue impact could increase substantially if launch facilities in Colorado, such as the Colorado Air and Space Port located in Adams County, are used more frequently in the future. Further, as discussed, stakeholders indicated that the exemption could make Colorado a more attractive location for businesses that plan to conduct space flight operations.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

Eliminating the Space Flight Exemption would subject the sale, transfer, or storage of property for use in space flight to the 2.9 percent state sales and use tax rate along with the sales and use taxes of any district, county, or city that has currently opted-in to the exemption. Although the exemption currently provides only a small benefit to its beneficiaries, eliminating it could have an impact on businesses considering establishing space flight operations in the state. Specifically, with increasing interest in the development of launching facilities in Colorado, stakeholders indicated that the exemption could become more frequently used in the future and that the exemption signaled that Colorado was welcoming of the aerospace industry and made Colorado a more attractive place to do business. Furthermore, equipment used in space flight tends to be expensive; therefore, if the exemption were no longer available, and businesses began purchasing or using more space flight property in the state, they could owe a substantial amount in sales or use tax. For example, the purchase of a $300 million satellite would result in $8.7 million in sales taxes. Additionally, other states offer similar exemptions for space flight property sales. Therefore, the elimination of this exemption could discourage businesses from establishing operations in Colorado.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We found that a few other states that have a significant space flight industry offer a similar tax exemption. Specifically, stakeholders mentioned Florida, Texas, and California as having strong space flight industries and we reviewed the sales tax policies in those states. We found that:

- Florida offers an exemption for machinery and equipment used in semiconductor, defense, or space technology production.

- California, similar to Colorado, exempts sales and use taxes on qualified property for use in space flight.

We did not identify a sales or use tax exemption in Texas for property or materials used in space flight, but aerospace companies can apply for flexible, low-interest loans from the state.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

We identified one other program and tax expenditure in the state that may also encourage private sector growth in Colorado's aerospace industry:

ADVANCED INDUSTRIES ACCELERATION GRANT PROGRAM [Section 24-48.5-117, C.R.S.]—Provides grants to advanced industries in Colorado, including aerospace. The program was established in 2013 by House Bill 13-1001, and provides several types of grants including advanced industries exports, early stage capital retention, and infrastructure funding. The program is administered by the Colorado Office of Economic Development and International Trade, and also includes an advanced industries investment tax credit, which provides taxpayers who invest in a qualified small advanced industry business with an income tax credit equal to 25 percent of their investment, limited to a $50,000 credit per investor for each small business.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURE?

There were no data constraints that impacted our ability to evaluate the tax expenditure.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

We did not identify any policy considerations on this evaluation.