

# Boeing's Cash Cow

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A corporate  
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America



INSTITUTE FOR WISCONSIN'S FUTURE  
*policy research in the public interest*



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## Introduction

It was early spring, a splendid time to be in Savannah, Georgia. That's why it had been chosen to host the 2004 annual meeting of the State Government Affairs Council, a blue-chip trade organization whose members are the chief state-capitol lobbyists for America's biggest corporations.

Amid Savannah's spring blossoms, the content of the meetings was typical conference fare. One of the workshops stood out, though, for its provocative title: *Turning Your State Government Relations Department from a Money Pit into a Cash Cow*. The co-presenters were Robin Stone, then the former vice president of The Boeing Company's state and local government relations, and Michael Press, then national director of Ernst & Young's Business Incentives Practice.<sup>1</sup>

"Cash cow" may be a CEO's favorite two-word phrase. It refers to a business operation that requires little investment but steadily generates large amounts of cash. Cash cows are highly profitable. The workshop focused on how a company can leverage its influence with state and local leaders to force them to give the firm large "incentives" to locate a new operation there or expand an existing one.

"Incentives" is the economic development euphemism for when governments provide financial help to a company, from tax exemptions to free training for employees, from free airport expansion to low-cost loans. The presentation cited five multinational firms as incentive success stories, starting with Ernst & Young – the accounting and consulting giant – and Boeing, the employer or former employer of both presenters.

This report examines how Boeing has implemented this 'cash cow' philosophy of state and local government relations. It will show how doing so drives down the quality of life for America's middle-class working families.

Boeing – following the pattern set out in the Savannah 'cash cow' presentation – demands that state and local governments help with the company's "hard costs," such as taxes. It demands government help with "human resource costs," from wage rebates and free help in hiring and training employees to laws restricting union organizing. It demands government help with "soft costs" such as financing and sewers and roads. It backs up these demands by using its size, its insider connections, its skill in manipulating public opinion and ultimately its threat to abandon the community.

Boeing relentlessly milks revenue from state and local governments while forcing large public spending on infrastructure. It holds down employee wages – further minimizing local tax revenue – at a time when governments at all levels are in desperate financial condition, slashing services to try to balance budgets.

All this matters because Boeing is so big and so influential, across the United States and around the globe. It is the largest aerospace company in the world. It is the most successful export firm in America. It designs and builds aircraft and spacecraft that are potent expressions of progress and modernity. Its senior management includes former high-ranking government officials both Democratic and Republican. Legions of Senators, Congressmen, cabinet officials and state and local leaders faithfully enact its interests.

Boeing is on the eve of receiving an important verdict from the World Trade Organization (WTO), the Brussels-based institution that is the court-of-last-resort for international trade disputes. Boeing and its European competitor in commercial aircraft, Airbus, have been fighting for a decade over each other's use of government incentives. Each claims the other's incentives violate international trade law.

In March 2010, the WTO ruled that Airbus was receiving illegal subsidies. The verdict against Boeing is expected this spring or summer. The issue is highly technical and the proceedings are secret. But whatever the WTO verdict against Boeing, from any common sense point of view, when it comes to seducing communities into being its financial patron, Boeing is guilty.

The global aircraft wars – and the government subsidies that fuel them – are important because they are establishing a new pattern for competition in high-tech industries. In the United States, we are accustomed to the economic development ‘war between the states,’ a race to the bottom with states outdoing each other to curry favor with mobile corporations dangling job possibilities.

Boeing and Airbus have taken the incentives game global. It is no longer a matter of Washington state competing against South Carolina and Kansas and Alabama. In Boeing versus Airbus, it means also competing with incentive deals in Bremen, Lower Saxony and Hamburg, Flintshire, Cadiz and Sevilla, Aichi, Apulia, Haute Garonne.

Economic development in the 21<sup>st</sup> century is not just a war between the states but a war among the states of America, the federal states of Germany, the counties of Britain, the provinces of Spain, the prefectures of Japan, the regions of Italy, the departments of France. But it is still a race to the bottom.

The Boeing story is a case study of what the *Wall Street Journal* recently called the new “global tax competition.”<sup>2</sup> It is depleting public resources everywhere, even as the demands for public structures and services soar.

Boeing sees itself as a template for a new kind of global corporation. “Breakthrough innovation is what we do,” proclaims Chairman and Chief Executive W. James McNerney, Jr., as the company’s latest motto.<sup>3</sup>

But this template is horribly flawed. In the long run, Boeing’s demands are a recipe for economic disaster and the deconstruction of America’s middle class.

## ***Part One: What Boeing Wants***

The ‘cash cow’ presentation in Savannah divided incentives into three categories: hard costs, human resource costs and soft costs. For this report, we’ll summarize these in the following terms:

- Hard costs: A demand for maximum breaks on all income, property and sales taxes;
- Human resource costs: A demand both for government assistance but more importantly for a submissive work force, a non-union employee base eager to work for reduced wages;
- Soft costs: A demand for a high level of infrastructure, from specially-built roads and harbors and airfields, to quality schools and colleges with Boeing-tailored aerospace programs, to an overall quality of life that attracts employees.

### ***A. Hard costs – maximum tax breaks***

There is no large company in America better at avoiding taxes than Boeing. The title of the Savannah presentation, *Turning Your State Government Relations Department from a Money Pit into a Cash Cow*, is a straightforward description of the company’s view that a primary role of government is to provide money for Boeing.

Examples are easy to come by. For example:

- Boeing developed its operations in Wichita, Kansas, by loaning itself several billion dollars, funneling the cash through a city program to avoid paying property and sales taxes.<sup>4</sup>

- Boeing built an assembly plant in North Charleston, South Carolina, by extracting a 63% discount on its property tax from the county – plus reimbursement for half of the remaining taxes it did agree to pay. Some of the tax breaks may last beyond 2060.<sup>5</sup>
- Boeing agreed to assemble a new product in the Seattle area, after Washington state promised it over three billion dollars – \$3,000,000,000 – in tax breaks, just after the state cut the company's unemployment and worker compensation taxes, built Boeing a huge addition to the port of Seattle and promised a four-billion dollar road project to meet the firm's traffic needs.<sup>6</sup>
- Boeing rented headquarters office space in Chicago, Illinois, after obtaining \$60 million worth of state and local tax breaks, then engineering a middle-of-the-night promise by Chicago's mayor to give the current tenant one million dollars of city money as an 'encouragement' to vacate and make room for Boeing.<sup>7</sup>

The Savannah presentation listed fifteen different kinds of incentives companies can demand. For Boeing, this is no mere 'wish list' but is instead a list of accomplishments. Boeing has obtained every one of the fifteen benefits in one or more states, save possibly a waiver of permit fees. Examples include:

- Income tax credits in Washington state, South Carolina, Illinois and Missouri;
- Sales tax exemptions or refunds in Washington, Kansas and South Carolina;
- Property tax abatements in Washington, Kansas, Illinois and South Carolina;
- Infrastructure grants in Washington, Illinois and South Carolina;
- Free or discounted land and buildings in Illinois and South Carolina;
- Wage rebates and job tax credits in Illinois, South Carolina and Pennsylvania;
- Training grants in South Carolina and Missouri;
- Targeted employment credits in South Carolina;
- Hiring assistance in Washington;
- Low-cost capital financing in Kansas, Illinois and South Carolina;
- Utility discounts in Washington and South Carolina;
- Waiver of permit fees has not been documented;
- But expedited permits has, with Washington's promise to give Boeing's permit applications "priority status over all other projects" and Chicago granting Boeing an exemption to a prohibition on corporate logos on top of buildings;
- Environmental incentives in California;
- Research and development credits from the U.S. government.

Boeing's prowess at obtaining tax breaks is well-documented by numerous studies of corporate tax avoidance. For example:

- Boeing's federal income tax during 2001-2003 was negative 18.8%, the fourth lowest rate among profitable Fortune 500 companies, according to Citizens for Tax Justice and the Institute on Taxation and Economic Policy, nonprofit research groups. This means it received more in federal tax breaks than it paid. Boeing got \$3.06 billion in federal tax breaks over the period while reducing its total capital investments by 65%.<sup>8</sup>

- Boeing's state corporate income taxes during the same three years were also negative, meaning that the company booked a net inflow of \$41 million in state income taxes while accumulating profits of \$5.6 billion. Boeing's effective state income tax rate of negative 0.7% was fifth lowest among the 252 companies in the Fortune 500 that disclosed state income tax payments, according to the same two nonprofit research groups.<sup>9</sup>
- Boeing had the second largest reduction in effective state tax rates during the period from 1997-1999 through 2004-2006. Boeing cut its effective state income tax rates by 4.2 percentage points, according to a report in *State Tax Notes*.<sup>10</sup>
- Boeing had 38 corporate subsidiaries headquartered in tax-avoidance jurisdictions, including Bermuda, Cayman Islands, Gibraltar, Hong Kong, Ireland, Netherlands Antilles, Singapore and the U.S. Virgin Islands, according to the U.S. Government Accountability Office (GAO). The GAO looked at the 100 largest publicly traded U.S. corporations and found only fifteen firms – mostly financial institutions and oil firms – with more tax haven subsidiaries than Boeing.<sup>11</sup>
- Boeing's effective federal income tax rate during 2002-2006 was only 0.7%. This was third lowest among the corporations in Standard & Poor's 500 Index, according to BusinessWeek magazine in 2007.<sup>12</sup>
- Boeing's effective federal income tax rate during 2005-2008 was 3.2%, ninth lowest in the S&P 500. Boeing was by far the most profitable company among the twenty-five lowest taxpayers.<sup>13</sup>
- And in 2009, the most recent full year, Boeing reported a negative federal income tax, getting a net \$132 million in payment from the federal government despite pre-tax profits in the U.S. of \$1.6 billion. The year before, 2008, Boeing paid only \$44 million in federal income tax on U.S. profits of \$3.8 billion, an effective rate of less than 1%.<sup>14</sup>

None of this is because Boeing failed to earn a profit. Its last money-losing year was 1997, and it was profitable throughout both recessions of the last decade.

Boeing will pursue extreme strategies in its efforts to avoid taxes. In 2006, for example, the firm paid a \$615 million fine to the federal government for two major ethical violations. The fine allowed the company to avoid criminal charges for stealing secret documents from a competitor and for illegally recruiting a top Air Force procurement official who was overseeing Boeing contracts.

The misdeeds were significant, as the size of the fine suggests. In addition, Boeing went so far as to argue that the payment fell in a tax loophole that allowed it to take a tax deduction for the fine. This would enable it to recoup a sizable portion of the payment, perhaps more than a third of it. It wasn't until strong public criticism from Congress – expressed in letters to the Justice Department – that Boeing decided not to claim the deduction. Critics included Republican Senators Chuck Grassley of Iowa, chairman of the Senate Finance Committee; John Warner of Virginia, chairman of the Armed Services Committee; and John McCain of Arizona.<sup>15</sup>

## War Between the States

One way Boeing wins lucrative tax concessions is by forcing a public contest among states for a new Boeing investment. Boeing has been at the center of three of the most celebrated cases of site-location competition in recent U.S. history: the location of the first assembly line for its new 787 Dreamliner passenger airplane; the re-location of its corporate headquarters away from Seattle; and the location of the second 787 assembly line. All three were high-profile national campaigns, with publicity in national, local and trade newspapers pressuring officials in many places to create tax-break packages larger than had ever been proposed in those states.

## South Carolina

In the most recent case – in which details are still emerging – Boeing received about one billion dollars in tax incentives to select North Charleston, South Carolina, as the site of its second 787 assembly line. South Carolina had not landed the first 787 assembly line – which went to the Seattle area – but was selected as a major subassembly site.

Details of South Carolina's bid for the second assembly line began emerging last October, when the state legislature went to work on an incentives deal. Boeing's decision to build there came later that month, after the passage of an incentive package. At the time, no one was sure about the details of what Boeing would receive nor the total value of the package, despite legislative action. As late as January 2010, the *Charleston Post and Courier* reported that "months after celebrating the groundbreaking for a massive jet assembly facility in North Charleston, state officials credited with luring Boeing to the Lowcountry say they still don't know what all the incentives offered to the aircraft giant are worth."<sup>16</sup>

The price tag didn't seem to matter, though initial estimates pegged the ultimate value of state and local tax breaks at about \$450 million, by far the largest ever given in the state. Later, state officials who had trumpeted the \$450 million value backed off, with comments such as, "I don't know where the \$450 million (figure) came from." As the *Post and Courier* noted, "Of the 163 state and county officials who voted on the deal, it was difficult to find a single person who claims to know what incentives were actually worth."

Through its research – difficult because both government officials and Boeing tried hard to avoid releasing details – the newspaper concluded in January that "the incentive package promised to Boeing is worth more than \$900 million, at least double the highest estimate first circulated by state officials."<sup>17</sup> One of the reporting team that compiled the estimate later told the *Seattle Times*, "These are lowball estimates, counting only the incentives we could put a reasonably firm value on... I would expect the (final) value is well above \$1 billion."<sup>18</sup>

The package of tax incentives includes at least the following:

- Property tax breaks in Charleston County worth at least \$360 million over thirty years. Boeing's new factory would pay property taxes of 4% rather than the usual 10.5% on the assessed value, and half of the property taxes the company would pay would be rebated back to the firm for fifteen years;
- Up-front money to Boeing through a state-issued bond of \$270 million, which would require about \$399 million in total including interest payments (all paid by the state);
- Ten-year property tax exemptions on the two specially-designed aircraft Boeing uses to transport large aircraft subassemblies. Each plane is valued at about \$250 million and the tax exemption at more than \$100 million.
- Training costs of \$33 million, paid by the state;
- A grant of \$5 million to help Boeing pay for site preparation;
- Job tax credits, up to \$12,500 per worker, to offset state income taxes;
- A \$150,000 study by the County of traffic needs around the airport;
- And \$100,000 as a utility tax credit to help Boeing with road and utility construction expenses.



This is the package agreed to in order to secure Boeing's investment. It does not include other costs required by the deal. For example, two new major road construction projects, aimed at alleviating traffic congestion around the airport and Boeing's new plant, are to cost an estimated \$155 million.<sup>19</sup> And the state approved a \$3.1 million program to train Boeing workers, in the South Carolina Technical College System. The approval, in February 2010, was accomplished using a special legal provision "last used in fiscal year 1994-95," said a spokeswoman for the Technical College System.<sup>20</sup>

## Illinois

Boeing was founded in Seattle in 1916 and for the rest of the twentieth century it located its corporate headquarters and the majority of its workforce there. It was the most significant private employer in the state. But in 2001, Boeing decided to move its headquarters to another city in order to separate its corporate office from production and engineering facilities. The shocking announcement led to a short, intense battle among Chicago, Denver and Dallas/Ft. Worth to land Boeing's headquarters.

Chicago won the battle with more than \$63 million worth of incentives, dwarfing the packages from Dallas/Ft. Worth and Denver, both estimated in the range of \$14 million to \$18 million. Chicago incentives included:

- State tax breaks totaling \$41 million, including:
  - Corporate income tax credits equal up to 60% of Boeing employees' personal income taxes (in effect, Boeing was allowed to keep most of the state income tax it withheld from employee paychecks);
  - Sales tax exemptions;
  - Grants to cover half of Boeing's moving expenses;
  - Job-training grants;
  - Grants for technology and capital improvements.
- Local tax breaks amounting to about \$22 million, including:
  - Local property tax abatements of \$16 million over 20 years (technically, a reimbursement of 73% of all city and school property taxes);
  - Reimbursement of at least \$4 million for taxes expected to be paid over 20 years to Cook County, the Chicago Park District, local community colleges and the Metropolitan Water Reclamation District;
  - A \$2 million energy grant;
  - Improvements to Midway Airport to accommodate Boeing's fleet of executive aircraft;
  - And a remarkable \$1 million gift by the city to convince a tenant to vacate the space Boeing wanted. As recounted in *Site Selection* magazine: "Last-minute troubles in securing space almost capsized the deal...that spurred several all-night negotiating sessions...In the wee hours of May 10, the deal finally came together. City officials agreed to fork over an additional \$1 million to nudge Rohm & Haas [the tenant] out."<sup>21</sup>

Not quite enough? The city also agreed to waive a city ordinance prohibiting company logos on the top of buildings.

The irony is that many observers believed that the package was far in excess of what Chicago needed to attract Boeing's headquarters. Boeing Chief Administrative Office John Warner, who led the headquarters search team, said afterward that tax incentives, while an attractive part of Chicago's bid, "is not a major factor." Of greater importance, he said, was a so-called "pro-business" attitude and "the capacity of state and local leaders to work together to facilitate Boeing's move."<sup>22</sup>

As a team from Good Jobs First, a non-profit tracking economic development projects, soon noted, "Financial incentives, it seems, were less important in themselves than they were as a sign of that pro-business attitude. The cumulative evidence strongly suggests that Illinois and Chicago overpaid for the Boeing deal."<sup>23</sup>

## Washington

Boeing and Seattle have a long and mutually beneficial relationship. With its pioneering commercial and military aircraft, Boeing was the core of a regional economy that grew to incubate Microsoft, Starbucks and a host of other major businesses. Boeing jobs "are the backbone of the middle class in my county," said Snohomish County Executive Aaron Reardon.<sup>24</sup> Snohomish County, including suburban Seattle, is home to Everett, site of the first 787 assembly line.

September 11, 2001 changed many things, including Boeing's plans for its upcoming superfast new passenger plane. In the wake of the attack, airlines demanded fuel efficiency rather than extra speed. Boeing dropped plans for its Sonic Cruiser and replaced it with the 7E7 (E for efficiency), later renamed the 787.

In March 2003, Boeing announced an open competition for a site to build the 787. First delivery was planned for 2008. This launched one of the biggest site-selection contests in history.

Washington state, which once took Boeing's presence for granted, was nervous. It had just lost the corporate headquarters to Chicago. Boeing executives had for several years been strongly and openly criticizing the state's business climate, including everything from the level of workers compensation taxes to too many delays on Seattle-area freeways.

Despite a short time frame – bidding was opened in March and closed in June – twenty-two states submitted proposals. Bids included \$300 million in tax breaks in Michigan, \$543 million in North Carolina; \$500 million from Kansas, \$350 million from Tulsa County plus a secret state package in Oklahoma; and other similar deals.<sup>25</sup>

Desperate to hold onto the new airplane, Washington was quick to act. In June, Gov. Gary Locke signed a \$3.2 billion, twenty-year package of tax breaks for Boeing. In addition, changes were made in workers compensation and unemployment taxes, in the port, and a \$4 billion roads program was launched.

"If they'd wanted us to bulldoze Mount Rainier so their planes would take off easier, we'd have done it," state Representative Hans Dunshee later told the *Seattle Times*.

Noted *Times* columnist Brier Dudley: "Boeing's engineering brilliance may only be surpassed by its lobbying savvy."<sup>26</sup>

Many of the other 21 states bidding for the work expressed concern that they were invited to bid simply in an effort to help Boeing drive a better deal with Washington. Arkansas Gov. Mike Huckabee said, "One of the things that we don't know at this point is, is Boeing seriously shopping the national marketplace for a plant,

or are they using this opportunity to really squeeze the state of Washington for deeper incentives.”<sup>27</sup>

The economic development director of Palmdale, California, said: “What I hear from people, including some of our elected officials, is this: ‘We’re still not 100 percent convinced that Boeing is not doing this just to get Washington to cough up money. To go through a lot of brain damage just to get Boeing a better deal in Washington is not something we want to do.’ Palmdale submitted a proposal anyway.”<sup>28</sup>

And in December, Boeing announced that, indeed, Washington was the winner. As would happen later in South Carolina, it took a barrage of freedom-of-information demands before the full details of the package were unveiled. Washington’s \$3.2 billion incentive package, in addition to the changes in workers compensation and unemployment, along with construction at the port and on the highways, included:

- A 40% cut in Boeing’s Business & Occupation tax (a tax on receipts, what Washington has instead of a corporate income tax);
- A further tax credit of 1.5% of all Boeing’s preproduction development expenses for any aircraft;
- \$20 million in rebates for previously paid sales taxes on computer hardware and software;
- Exemption from sales tax on new purchases of computer equipment and software;
- Exemption from sales tax on labor, materials and fixtures in the new assembly line;
- Exemption from property taxes on the new plant, including its equipment;
- Exemption from leasehold taxes for Boeing facilities in the public port;
- And a continuation of all tax incentives through June 30, 2024.

Washington had won the battle for assembling the 787.

The 787, made mostly with composite materials rather than metals, is a big deal. The company calls it “the most important new airplane since the Boeing 707 at the dawn of the Jet Age, half a century ago.”<sup>29</sup> It quickly became the best-selling new airplane in history, with nearly 900 of the giant aircraft ordered by airlines around the world even before the first test model had been built. Its sales book tallied over \$120 billion in purchase orders.

Within a year of picking Washington for its assembly line, Boeing had begun new operations in South Carolina, to serve as a subassembly site for the 787. The company would use a new system for building the 787. Most of the work would be done in subassembly plants rather than in Boeing’s Washington operations, with partially completed airplanes shipped to Washington for only the final piecing together. When Boeing decided to put its second 787 assembly line in South Carolina, it meant that soon some of the 787 production would never go through Washington.

### *B. Human resource costs – low-cost work force*

The second category of demands relates to human resource costs. In addition to wage rebates and job-creation tax incentives, employee training grants, targeted employment credits and help with hiring, this includes an ample supply of ‘acceptable’ workers. The word “acceptable” summarizes a willingness to work for less than middle-income wages, a resistance to labor unions and support for local political compliance with company interests.

This is easiest to see in the contrast between workforces in the Seattle area and the Charleston area. It is a major part of the reason why Boeing chose to put its second 787 assembly line in Charleston rather than Seattle. The difference in wages was made explicit by the *Seattle Times*, which reported last October on some of the conditions in the Charleston subassembly plant.

The newspaper reported that because Charleston didn't have enough skilled workers to do Boeing's somewhat challenging work, at least one-third of the employees there were free-lance machinists hired from across the U.S. and other countries. These temporary workers were "experienced airplane mechanics paid about \$26 an hour, compared with the \$14 an hour for local employees." The \$26 wage, the *Times* notes, is the average Boeing wage for union machinists in Everett, Washington.<sup>30</sup>

The difference between \$26 an hour and \$14 an hour is exactly the difference between a middle-class job and one that does not measure up to that designation. The higher rate translates into about \$54,000 a year; the lower rate to about \$29,000.

Consider these federal statistics on income distribution in America, in which household incomes are divided into five equal parts, from the lowest-paid fifth to the highest-paid fifth. The average income in the middle-fifth in 2008 was \$50,132. This would place the household of a \$26/hour Boeing worker (if he/she were the sole worker in the home) about 8% higher than the average for America.

Now step down one category, from the middle fifth to the second-lowest fifth. The average income was \$29,517, according to the US Census Bureau. This is the equivalent of Boeing's \$14/hour worker.

By downgrading its production workforce from a \$26 wage to a \$14 wage, Boeing drops its workers from being in the middle income fifth to a lower bracket. In Boeing's future, today's middle fifth would disappear into the lower bracket.

The absence of unions in Charleston was an important factor for Boeing. In South Carolina, 4.5% of workers belong to unions, the 3<sup>rd</sup> lowest rate in the nation. In Washington, 20.2% of workers are unionized, the 4<sup>th</sup> highest in the nation.<sup>31</sup> South Carolina's laws are among the most union-hostile in the country. This includes a 'right-to-work' law so even in a unionized workplace, employees cannot be required to join a union.

The contrast between Washington and South Carolina goes much deeper than wages and unions. The difference in quality of life can be seen in a variety of statistics. For example, South Carolina has the third highest infant mortality rate in the U.S. (9 per 1,000 births); Washington has the third lowest (5).<sup>32</sup> In the proportion of adults with a college degree, South Carolina ranks 40<sup>th</sup> (24%); Washington is 12<sup>th</sup> (31%).<sup>33</sup> In the proportion of children living in poverty, South Carolina ranks 11<sup>th</sup> (21.7%); Washington is 36<sup>th</sup> (14.3%).<sup>34</sup>

Boeing frequently blamed its unions, especially the International Association of Machinists and Aerospace Workers, which represents Boeing production workers in many locations, for strikes and wage increases. "The overriding factor" in choosing South Carolina, said Boeing's Jim Albaugh, CEO of the company's Commercial Airplanes unit, "was that we can't afford to have a work stoppage every three years. And we can't afford to continue the rate of escalation of wages."<sup>35</sup>

Albaugh's comment about "the rate of escalation of wages" is a clear statement that the \$26-an-hour, middle-class wage of Boeing's Seattle-area production workers is not to be continued. Even the slow growth that has characterized overall wage gains in recent years is too much for Boeing, Albaugh says. The point is straightforward: Boeing will not continue to support middle-class wages for the bulk of its employees.

Why don't unions organize Boeing's South Carolina workers? They did. During the early stages of setting up a worldwide production system to build the 787, Boeing gave a subassembly contract to Vought Aircraft Industries, a Texas-based company that would build 787 rear fuselage sections in North Charleston. The Machinists won bargaining rights at the Vought North Charleston plant in 2007 and the next year negotiated a contract that was to run until November 2011.

But by the middle of 2008, the entire 787 program was way behind schedule. The various South Carolina operations, including the Vought plant, contributed to the delays, having "been plagued with startup problems, partly due to the inexperienced work force," said the *Seattle Times*. So in stages Boeing bought out various subassembly plants in South Carolina it had been using as subcontractors.

In July 2009, Boeing completed its acquisition of the Vought South Carolina plant, with its unionized workforce. This would have brought Charleston's unionized workers into Boeing itself, a major strategic inroad for the Machinists' effort to bring unions to the area.

But on July 30, 2009, the same day the acquisition of Vought North Charleston was announced, a decertification petition was filed with federal labor officials. In the September election, the union was decertified. The next month – free from a union presence in North Charleston – Boeing announced that South Carolina had won the competition for siting the second 787 assembly line.

There was no mistaking the message that was heard across the nation. Under the headline "Boeing's S.C. jobs a setback for unions," the *Washington Post* quoted a labor expert as saying: "This is the escape from collective bargaining."<sup>36</sup>

Boeing also had at one time a large number of Machinist-represented workers in its extensive operations in the Wichita, Kansas area. But in recent years Boeing has divested itself of most of those operations, selling off its unionized commercial aircraft facilities there to a new company it helped establish, Spirit Aerospace. In 2001, Boeing employed 16,700 people in Kansas. By 2007, that had plunged to under 3,000.<sup>37</sup>

### The irony of job growth promises

Why do state and local governments give the incentives? Obviously, the answer is jobs. The only way to imagine that the long-term tax breaks are worthwhile is to assume that their cost will be trumped by the value of the jobs Boeing brings to the community. The facts do not support such an optimistic view of how Boeing operates.

First, Boeing itself is not in the business of creating jobs. Its strategy is just the opposite – worldwide global outsourcing and – at most – a stable number of employees. At the end of 1998, Boeing employed 231,260 people. Ten years later that had dropped to 162,191.<sup>38</sup>

In Washington state, for example, Boeing seriously overstated the employment impact of its decision to locate the first 787 assembly line there. The *Seattle Times* reported, "In 2003, state officials forecast that the 787 would add 3,600 supplier jobs at existing Boeing subcontractors and at new suppliers drawn to Washington. But four years later, new suppliers have established just four modest new Dreamliner manufacturing operations employing around 200 people in Washington, half of those jobs in unskilled assembly or distribution work."<sup>39</sup>

The newspaper quoted a former Boeing executive – who left the company to work for the state on economic development issues – acknowledging, "We have failed miserably at attracting new engineering companies. We missed out on the big stuff."

Further, Boeing has long maintained a two-tier wage structure, even in Washington where its own employees are well paid. The "flinty reality" of the aerospace industry, as the *Seattle Times* put it, "Outside Boeing, the hours are long and the pay is hardly sky-high."<sup>40</sup> In 2007, the newspaper analyzed wages at Boeing and an additional 160 companies claiming state tax breaks for aerospace. It found that while 93% of Boeing's production workers earned at least \$20 an hour, only 21% of non-Boeing workers earned that much. Nearly half the non-Boeing workers earned less than \$15 an hour, compared with only 4% of Boeing's workers. Similar discrepancies were found among engineers.

So even in Washington, where the wages of Boeing workers are solidly middle-class, once one steps beyond Boeing itself, wage levels plummet. There is no reason to expect anything different in South Carolina, especially with the absence of union pressure there. But in South Carolina, the supposedly higher wage Boeing jobs themselves are only at the \$16 range, equivalent to about \$33,000 a year.

Even those jobs – paying less than \$30,000 annually – are likely to emerge in fewer numbers than many Boeing boosters in South Carolina project. This is because of the radically global approach to contracting that Boeing is pushing to the limit. Unlike older manufacturing techniques, where a large factory in a community spawned numerous nearby jobs with suppliers, Boeing's twenty-first century sourcing philosophy means that parts that are needed in its South Carolina factories can come from literally anywhere on the globe.

That's why the company has such high demands for the local infrastructure, such as ports, airports and roads. It expects to bring in an enormous amount of material, rather than sourcing them locally. Rather than building the airplane in one location, putting together smaller components from local and distant suppliers, the 787 was designed to have large subassemblies created in factories around the world. These large components are then transported to the final assembly line – in Washington or South Carolina – for a final assembly which requires many fewer workers and much less time than the traditional technique.

*Wikipedia* compiled a well-documented overview of how widely distributed the new supplier system is (or at least, was intended to be). The tail fin for the plane is made in Washington. Ailerons and flaps come from Australia. Wings are made in Japan. Horizontal stabilizers are built in Italy; fuselage sections in South Carolina, Japan and Kansas. Passenger doors are from France. Cargo and other doors are built in Sweden. Floor beams are made in India and sent to subassembly plants in Italy, Japan and the U.S. The landing gear is from France, using titanium from Russia and brake parts from Italy.<sup>41</sup> Twenty countries are reported to be involved in the total production and assembly procedure.

The global pattern was not restricted to the production part. Even designing the new plane, the most technically advanced part of the operation, was shared worldwide to an unprecedented degree. As Boeing itself bragged: "The program's approach to the development of the airplane has been as revolutionary as the jetliner itself."<sup>42</sup>

This new approach to outsourcing has not been an obvious success. The plane has been plagued with problems from the beginning, forcing numerous delays. Originally the plane was to enter commercial operation in 2008. But the first commercial airplane still has not been delivered, though it is now promised for the fourth quarter of 2010. Problems with suppliers have been routinely blamed for the constantly delayed launch date for the new plane.

Clearing up supplier issues is one reason Boeing bought the original facilities in South Carolina that were supposed to be owned by independent suppliers. Boeing acknowledged problems with suppliers in various countries, with the company sending its own employees around the world to help clear up the problems. In well-publicized comments in 2007, both Boeing CEO Jim McNerney and Boeing Vice President Mike Bair confirmed disappointment with the global sourcing strategy.

Still, this is unlikely to change the basic thrust of Boeing's commitment to worldwide sourcing. The company may have taken it too far too quickly with the 787, but that is its desired path. "The 787 defines the place we want to be [on outsourcing]," said an executive, especially with Boeing pressing its worldwide suppliers to form their own local supply chains and infrastructure systems. "We have to be global," he said. "It's a whole world full of people's talents and capabilities we're bringing together to make this."<sup>43</sup>

It is also a whole world full of untenable choices between reduced-wage work or no work at all.

### *C. Soft costs – maximizing Boeing-friendly infrastructure*

First, Boeing demands huge tax breaks to reduce its hard costs. Second, Boeing demands low wages and no unions, to reduce its human resource costs. To complete its package of demands, Boeing also requires communities to provide expensive, high-quality infrastructure, to reduce its soft costs.

Certainly a company building the biggest airplanes in the world is going to have many infrastructure needs. It requires a large workforce, with all that entails in terms of roads, schools and a wide range of public services. It requires huge pieces of equipment to be moved in and out, putting maximum stress on roads, airports, railroads and ports.

Boeing prefers to pay for as little of it as possible. It demands that state and local government bear the costs of providing an environment fit for Boeing's needs. The most explicit demonstration of this occurred in its multistate competition to land the 787's first assembly plant, which ultimately went to Washington state with its \$3 billion-plus package of tax breaks.

Early in the site-location process, Boeing made public what it called a "Summary of 7E7 site selection criteria."<sup>44</sup> The items on the list aren't surprising, given the scope of Boeing's project. But many of the items on the list require major spending by state and local governments. The following items require substantial investment by state and local governments, using taxpayer funds:

- Suitable runways;
- A port capable of around-the-clock operations;
- Continuous availability of heavy traffic ways;
- Proximity to railways and interstate highways;
- Support services (fire, police, emergency and medical services);
- Training infrastructure with local agencies or governments;
- And quality public schools.

Other criteria require varying degrees of taxpayer spending, including the need for convenient and affordable utilities (water, sewer, power, waste and telecommunications) and what Boeing calls "transportation enhancements." The company won the right to a veto on which contractors are hired to work on infrastructure.

Boeing further expects that local government would devote their own resources to finding out Boeing's needs and meeting them. Its agreement with Washington in 2003 included not just the billions in tax breaks but also the use of at least four government employees working to maximize benefits to Boeing. All four are to be paid by the state (or local government) but "selected in consultation with Boeing."<sup>45</sup> These include:

- A Tax Commitment and Incentives Coordinator, whose job includes not just overseeing the agreed-upon tax breaks but also "apply[ing] for and pursue[ing] all grants for which Boeing may be eligible;"
- A Transportation Infrastructure Coordinator, to coordinate all Boeing needs regarding road, rail, port and airport transportation;
- A Workforce Development Coordinator, to coordinate all training and recruiting;

- And a Large Cargo Freighter Coordinator, to coordinate issues relating to the development and operation of giant new cargo airplanes Boeing needed to move parts for the 787.

## *Part Two: How Boeing Gets What It Wants*

How is Boeing able to extract such enormous tax packages?

For starters, Boeing is a huge company. It is not a company that can consider major new operations without drawing attention. Boeing coming to town is somewhat like the proverbial large gorilla entering the room. It's impossible not to notice.

Boeing is an aggressive company. As the Savannah 'cash cow' presentation stressed, its approach is to "control publicity ... be proactive ... communicate progress to the elected officials and their constituents ... involve elected officials in press announcements."

Boeing's control over local government is intricate. In Washington, South Carolina and Kansas, for example, it has pushed for the creation of special degree programs in state institutions of higher education to meet their needs.

The Savannah presentation was filled with tips about how to court local officials in order to obtain tax incentives. Chief among them was the recognition that since the "public doesn't like 'corporate welfare,'" the company should be sure to use a "'But for' threat." This is a threat that in the absence of large incentives, the company will not invest in the area.

Other recommendations in the 'cash cow' presentation include:

- The need for the firm to "Control publicity" and "Avoid legislation if possible" (presumably because of potential public controversy);
- The need to "involve elected officials in press announcements." Tax breaks are a "Quid Pro Quo," the presentation noted, so one thing local officials get in exchange for lower taxes is good publicity for bringing investment.
- The importance of showing gratitude. "Thank everybody a zillion times," the presentation stressed, and offer to "conduct a 'lessons learned' session."
- Finally, "Be mindful of the election & legislative cycle," "Be mindful of local turf battles," and "Don't settle for 'off the shelf' but don't be greedy."

One important reason that Boeing knows how to deal with elected officials and other government decision-makers is that so many senior executives at the company are themselves former high-ranking public officials. One of the most striking facts about Boeing's executive group is the high proportion with previous experience at senior levels in government, both under Democratic and Republican administrations and Congresses.

Boeing's board of directors includes:

- William M. Daley, former U.S. Secretary of Commerce and Chairman of Al Gore's 2000 presidential campaign;
- Kenneth M. Duberstein, former White House Chief of Staff;



- Edmund P. Giambastiani, Jr., former Vice Chairman of the U.S. Joint Chiefs of Staff;
- And Susan C. Schwab, former U.S. Trade Representative.<sup>46</sup>

Boeing's most senior executives include these former government officials:

- Senior Vice President Shephard W. Hill, former chief of staff and legislative affairs for Congressman Bill Chappell;
- Senior Vice President Timothy Keating, former special assistant to the President and White House staff director for legislative affairs;
- And Senior Vice President and General Counsel J. Michael Luttig, former judge on the U.S. Court of Appeals for the Fourth Circuit, former assistant Attorney General and counsel to the Attorney General.

Management ranks below these senior levels are full of former ranking federal officials. The U.S. GAO reported in 2008 that 15 Boeing employees were former "senior" Department of Defense officials and 76 other Boeing managers had been involved in Defense Department procurement matters.<sup>47</sup> The federal jobs formerly held by Boeing managers include:<sup>48</sup>

- Assistant Secretary to the Department of Veterans Affairs;
- Communications Director for the House Armed Services Committee;
- Deputy Assistant Secretary of Commerce;
- Deputy Assistant to the U.S. Trade Representative;
- Majority Staff Director of Senate Appropriations Subcommittees
- Deputy Secretary of Defense;
- Staff Director for the House Armed Services Committee;
- Policy Advisor and Counsel to the House Minority Leader;
- Staff Director of the House Armed Services Committee;
- Director of the Standard of Conduct Office at the Department of Defense;
- Assistant Administrator for Policy at the Federal Aviation Administration;
- Staff Director of the House Appropriations Subcommittee on Defense;
- Chief of Regulation/Certification at the Federal Aviation Administration;
- Deputy General Counsel at the Department of Transportation;
- Associate Counsel in the Executive Office of the President;
- Assistant Secretary of State;
- And Deputy White House Press Secretary.

Boeing is also one of the nation's largest corporate lobbyists and donors to political campaigns. At the federal level, Boeing was the 15<sup>th</sup> most active lobbyist in the U.S. in 2009, spending \$17 million. In just the current two-year election cycle, it has donated to campaigns for 295 current members of the U.S. House of Representatives (68% of members) and for 35 current Senators (35%). Democratic recipients outnumber Republicans 204 to 126.<sup>49</sup>

Boeing's close ties with politicians hold true at the state level as well as the federal. In the 2007-2008 election cycle (the most recent for which data are available), Boeing made campaign contributions to an astounding 504 candidates in 18 states: Alabama, Arizona, California, Florida, Georgia, Illinois, Kansas, Missouri, Montana, Nevada, New Mexico, North Carolina, Oklahoma, Pennsylvania, Texas, Utah, Virginia and Washington. The offices Boeing made donations to include not just state legislators (both houses) but also governor, lieutenant governor, attorney general, treasurer, comptroller, secretary of state, insurance commissioner, commissioner of public lands, auditor and state board of education. Its donations were split almost evenly between Democrats and Republicans.<sup>50</sup>

In Washington state, the company hired Bob Watt, former deputy mayor of Seattle, and Fred Kiga, former chief of staff to the governor. When Boeing decided to enter South Carolina, the names of the local lawyers and lobbyists it hired "read like a proverbial who's who of Palmetto State power brokers."<sup>51</sup>

Boeing, in other words, is a company full of experience in how government works and how best to take advantage of opportunities for government contracts and government tax breaks. Such close ties can lead to conflicts of interest, and Boeing has had a full share of these. In 2006, Boeing was fined \$615 million and had a \$20 billion contract cancelled because of conflicts of interest involving an Air Force procurement officer, Darleen Druyun, and the company. Druyun negotiated jobs for herself, her daughter and her son-in-law while negotiating the contract with Boeing. Both Druyun and a Boeing official served prison time.

In South Carolina, three lobbyists hired by Boeing were at the same time also being paid to work for the South Carolina Research Authority, the state's premier economic development agency.

In Washington, the same firm that served as Boeing's auditor, Deloitte Consulting, also received \$715,000 from state government to help get Boeing to choose Washington for the first 787 assembly line. Tax scholar David Brunori characterized the deal this way: "Deloitte gets money from Washington to get Boeing to build in the state. Deloitte gets money from Boeing to persuade Washington to give it money to build. Boeing gets money from Washington. Washington pays Boeing and Deloitte. There might be more egregious conflicts of interest out there, but there might not be."<sup>52</sup>

In California, Boeing recently received a \$16 million contract for environmental monitoring at the same site where it had been fined for polluting a creek with chromium, dioxin, lead and mercury.<sup>53</sup>

Boeing is the second most-cited company in the Federal Contractor Misconduct Database, with 36 instances ranging from improper invoicing to gender discrimination, from overbilling to sexual harassment, and from arms control violations to building defective helicopters.<sup>54</sup>

### ***Part Three: What Is the Impact of Boeing's Method?***

Boeing wants its many demands met immediately. But the only way states and communities can afford the expensive infrastructure Boeing demands, while at the same time giving major tax breaks, is by borrowing from the future.

In Washington state, the tax incentives given Boeing in 2003 will continue until July 1, 2024. The Washington Research Council, a non-partisan research organization, calculated that the value of the tax incentives would grow each year until then, increasing from about \$50 million in Fiscal Year 2007 to \$144 million in FY2010 and \$291 million in FY2023.<sup>55</sup>

In South Carolina, the incentives given in 2009 last various time periods. The largest property tax breaks extend for 30 years. Others incentives are to last ten years and fifteen years. And if certain conditions are met, "some of the property tax breaks could remain in force beyond 2060," the Charleston Post and Courier reported.

In Kansas, Boeing continues to have a property tax abatement and sales tax exemption based on its use of Industrial Revenue Bonds (IRBs). The bonds first appeared on Boeing's 10-K report for 2004 and the incentives are in place for ten years.

An unusual feature of these Kansas bonds is that Boeing borrowed the money even though it had no need to. That's clear from the fact that Boeing itself bought the bonds, thereby providing the very cash that Boeing itself was borrowing. As Boeing's 10-K states, "We have also purchased the IRBs and therefore are the bondholders as well as the borrower/lessee of the property purchased with the IRB proceeds."

Why did Boeing loan money to itself? Because issuing an IRB through the city of Wichita enabled Boeing to win a long-term property tax abatement and sales tax exemption on everything connected with the property it borrowed money to build. Boeing reported \$2.9 billion worth of Kansas IRBs in 2004, an enormous property value on which to be tax-exempt. Boeing also reported a small but similar arrangement in Georgia, in which it received a partial property tax abatement after being the purchaser of IRB bonds which provided funding for itself.

Are these states and communities in strong enough financial condition to manage while giving Boeing large tax breaks? No. Especially with the recession battering state and local budgets across the country, the communities in which Boeing is receiving large tax breaks are struggling to maintain services while balancing their budgets.

Consider South Carolina, where the tax incentives have just begun. The state is running an anticipated deficit of \$1.2 billion for fiscal year 2010, or 20% of its total budget, and \$1.3 billion in fiscal year 2011, according to the Washington, D.C.-based Center on Budget and Policy Priorities (CBPP). Its projected deficit for fiscal year 2011 is \$1.3 billion.<sup>56</sup>

The state is dealing with these deficits in the customary way: by slashing programs. South Carolina has already cut programs in public health, education at all levels from pre-school through K-12 to higher education, workforce development (except for Boeing) and service for the elderly and those with disabilities. The governor is further proposing to cap the state's children's health insurance package.<sup>57</sup>

On top of that, changes in federal health care law will mean an additional half million people eligible for the state's Medicaid program. A state official determined that "it will cost \$914 million in state funds over a decade to cover them."<sup>58</sup> Coincidentally, that's just about the amount of tax breaks going to Boeing over that same time period.

Similar stories can be told about Washington and Kansas. In Washington, the expected deficit for fiscal year 2010 is \$6.2 billion, or 27% of the general fund budget. In Kansas, the expected deficit is \$1.8 billion, or 30% of the budget. These deficits are expected to run well into the future. To deal with the troubled budgets, Washington has already cut programs in public health, K-12, pre-school, and higher education, workforce development (except for Boeing) and service for the elderly and those with disabilities. Kansas has made similar cuts, though so far it has exempted public health programs. A recent headline noted, "Kansas' model parole program collapses with state budget cuts."<sup>59</sup>

In Kansas, the experience with tax breaks for Boeing and other firms has led to some rethinking of the practice of tax giveaways. In 2008, the Legislature's audit bureau conducted a Performance Audit Report on the state's economic development strategies. Its conclusion: "Most reviews of economic development assistance find few results are achieved – a theme that audits in Kansas and other states commonly find, as well."<sup>60</sup> Problems include:

- Promised jobs weren't created;
- Return on investment is low or negative;
- And incentives offered weren't a determining factor in site selection.

The dilemma, auditors noted, is that although "incentives don't have a significant impact on economic growth...states have to continue offering such incentives to remain competitive." It went on to say: "Because so many states offer economic development assistance, many business officials have come to view these incentives as an entitlement – they expect to be offered an incentive package."

But there is a severe price paid for these incentives, auditors noted: "One downside to offering public assistance to so many businesses is that it may cause less state funding to [be] available for public services." These are the very public services that provide the framework for a strong middle class and a stable community.

### *The global economic development wars*

While pressing state and local governments from coast to coast for major tax concessions, Boeing has also waged an international legal battle with the help of Senators, Congressmen and the US government, accusing its competitor Airbus with – of all things – relying too heavily on government assistance. In March 2010, Boeing won the latest round at the World Trade Organization (WTO), with a ruling that about \$20 billion in European government aid to Airbus constituted an illegal export subsidy.<sup>61</sup>

The case is far from over. The Europeans are expected to appeal. Airbus' counterclaim about Boeing's incentives is expected to be decided in coming months. Even the consequences of guilty verdicts are not clear. They could include anything from repayments of incentives to prohibitions against future incentives to the establishment of import tariffs to an international trade war.

But the sparse public documentation of the cases makes it abundantly clear that the tax incentives urged at the Savannah conference are worldwide in scope. Just as the Airbus complaint against Boeing cites the tax breaks in Washington, Kansas and Illinois (South Carolina had not yet happened) – as well as federal aid – the Boeing complaint against Airbus cites economic development incentives given to Airbus in a number of European countries, including France, Germany, Spain, Italy and the United Kingdom.<sup>62</sup> Boeing has its own economic development incentives in Italy for factories that supply the 787. And Japan's national and local governments have provided at least \$2 billion worth of help to the three Japanese firms doing contract work on the 787.<sup>63</sup>

The problem is that the greater the competition for the kind of work involved in technologically advanced design and production, the swifter the race to the bottom. When companies like Boeing conduct competitions to locate a new facility, new kinds of incentives are invented and old kinds of incentives are expanded.

When local governments here and abroad are forced to give up tax revenues to attract a new factory, when workers are forced to accept reduced wages, when communities must build expensive roads and ports and high-quality educational programs, something must suffer. What suffers is the ability of communities to maintain a durable middle class and the systems needed for ongoing economic growth.

## *Summary and Conclusion*

Boeing has positioned itself to be a model for the global corporation of the 21<sup>st</sup> century. This model pressures state and local governments to reduce taxes and provide lavish financial incentives to come and stay in any given locality. In addition, the Boeing model wants governmental sanction and support to offer lower wages and benefits for the same work with no-cost human resource services and training. On top of these, the new model demands that government provide extensive financing and infrastructure to support operations. The Boeing model uses sophisticated marketing, heavy-handed relationships with key decision makers and the fear of job loss to enforce its agenda.

Boeing and those who follow its lead drain resources from employees and governments while demanding investment in roads, sewers, and supplementary systems to facilitate expansion. The multiple demands leave state and local governments incapable of maintaining the intricate network of programs that are vital for communities to thrive. This also erodes the public sector framework for growing and maintaining a strong middle class – education, public health and safety, transportation, housing and investments in technology.

This is the bottom line for Boeing's 'cash cow' approach to local government. The combination of demands for low taxes, low wages and high-cost infrastructure is unsustainable. In 2004, a review of state taxes by the University of Kansas summarized the consequences clearly: "Low business costs generally translate into low wages and low tax revenues. Low wages generally translate into low incomes, and low tax revenues generally translate into low levels of educational expenditure and other government services. And low income and low services generally translate into a low quality of life."<sup>64</sup>

That's not how the company sees it, of course. Boeing and its top executives are self-consciously bold, buoyant, futuristic, optimistic. That's why it calls the new 787 aircraft the Dreamliner. But Boeing's 'dream' scenario clashes with the realities of how it conducts business. Boeing makes impossible demands of communities that simply cannot be satisfied in a world of shared prosperity. The only way that states and communities can satisfy Boeing's insatiable demands is by disassembling its prize public structures and borrowing unsustainably into the future.

In the long run, Boeing's model for the new global corporation is a recipe for an America without a middle class.

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