



# SALES AND USE TAX EXCLUSION PROGRAM

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Public Workshop on STE Program Development and  
the Incorporation of Assembly Bill 199

March 16, 2016

# Agenda



- CAEATFA Overview and Legislative Background
- Existing STE Program Structure and Utilization
- Program Challenges and Proposed Modifications
- Next Steps and Process Timeline
- Q&A

# About CAEATFA



- California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA or the Authority)
  - Created in 1980 to provide credit support, access to low-cost financing through private activity tax-exempt bonds, loans, and other forms of financial assistance.
- Statutory goals include:
  - reducing greenhouse gas emissions,
  - increasing the deployment of sustainable and renewable energy sources,
  - implementing measures that increase the efficiency of the use of energy,
  - creating high quality employment opportunities, and lessening the state's dependence on fossil fuels.

# CAEATFA Board



- John Chiang, State Treasurer and Chair
- Betty T. Yee, State Controller
- Michael Cohen, Director, Department of Finance
- Dr. Robert Weisenmiller, Chair, California Energy Commission
- Michael Picker, President, California Public Utilities Commission

# About the STE Program



- In 2010, SB 71 (Padilla) was enacted, providing a targeted exclusion to projects of Alternative Source (AS) and Advanced Transportation (AT) manufacturers.
- Authority was required to notify legislature when awards exceeded \$100 MM in STE for a given calendar year, but could continue to approve applications.
- SB 1128 (Padilla) added Advanced Manufacturing (AM) as an eligible type of project to the program in 2012.
  - AM projects are eligible based on the manufacturing process utilized, rather than the product manufactured.
  - SB 1128 also set a \$100 MM cap on the amount of STE that could be awarded in a calendar year.
- AB 1269 (Dababneh, 2015) extended the sunset date of AM projects from July 1, 2016 to January 1, 2021 (the current sunset date of the entire program).
- AB 199 (Eggman, 2015) added manufacturing projects that utilize recycled feedstock (RF) to the program. Regulations to establish evaluation methods are being developed.

# Examples of potentially qualifying technologies



- **Alternative Source**
  - Solar photovoltaics
  - Energy Efficiency
    - E.g. LED Lightbulbs
  - Biogas
  - Energy Storage
- **Advanced Manufacturing**
  - Micro- and nano electronics
  - Integrated computational materials engineering
  - Nanotechnology
  - Additive Manufacturing
  - Industrial biotechnology

Common examples: Aerospace, Telecom, Pharmaceuticals
- **Advanced Transportation**
  - Electric Vehicles
  - Electric Vehicle Batteries or Components
- **Recycled Feedstock**
  - Materials Recovery Facilities (MRFs)
  - Composters
  - Tire Recyclers
  - Mattress Recyclers

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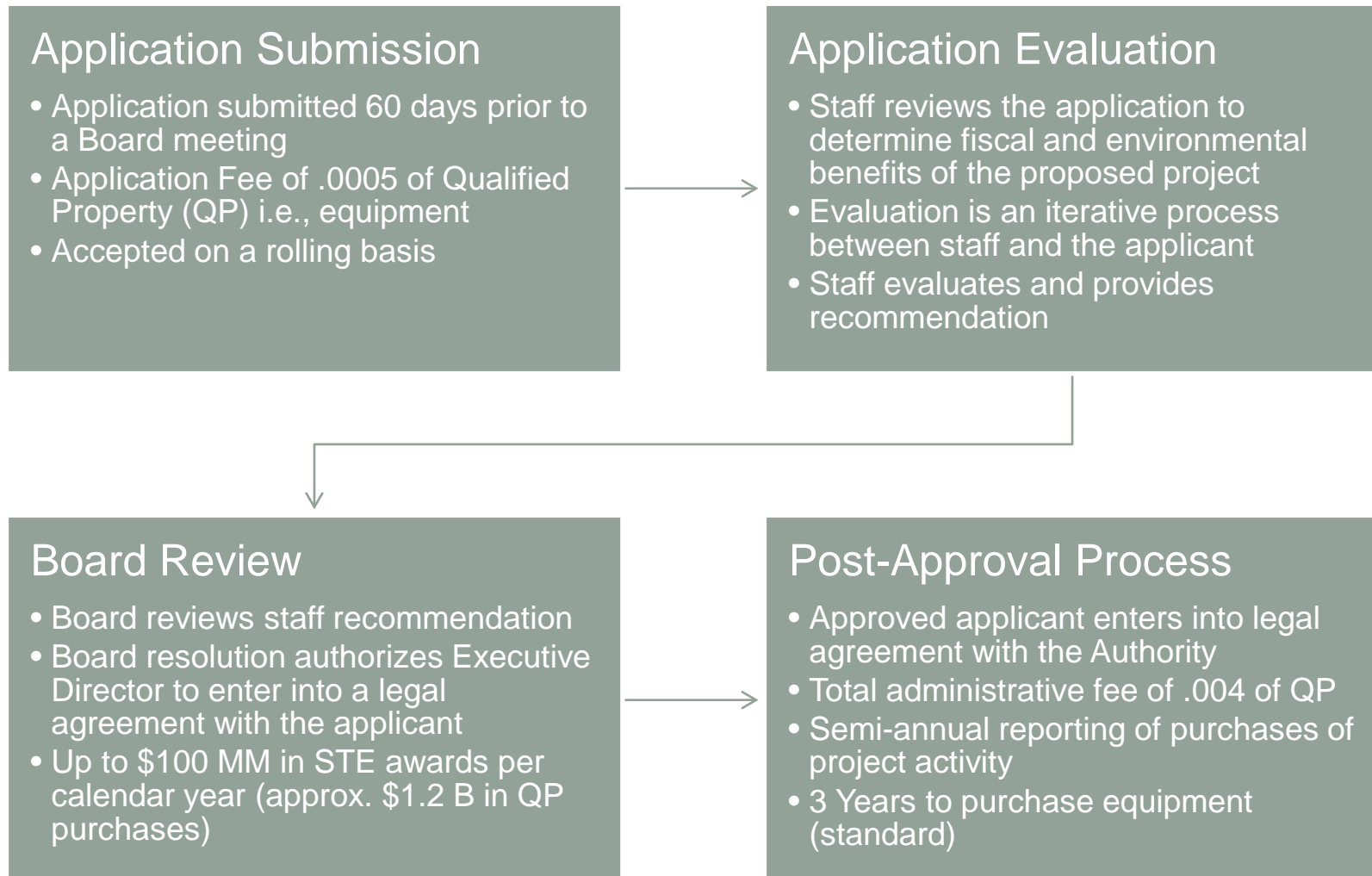
# Nature of an STE award



- CAEATFA makes a finding that the proposed facility is a “project” and that the applicant is a “participating party.” This enables the approved applicant not to pay sales and use tax on eligible equipment purchases for a project. Transaction between approved applicant and vendor is not considered a taxable “sale” under sales and use tax law. (Rev. & Tax Code § 6010.8)
- CAEATFA does not provide actual funds to applicants.
- Award is provided on the front end of projects because the STE must be used when purchasing equipment. Due to “functional use” requirement under sales and use tax law, the award cannot be provided on the back end once a project is complete.
- In some circumstances, a participating party may seek a refund of taxes paid on qualifying equipment purchased prior to Board approval of the award. Reimbursements are subject to “functional use” and other eligibility guidelines under Board of Equalization regulations.



# Overview of the application process



# Projects are evaluated by a net benefits test to estimate the benefits and costs



- Net benefits test is based on business plan data provided by the applicant and checked by staff for internal consistency and plausibility.
- The estimated marginal (rather than aggregate) increase in fiscal and environmental benefits to the state from the project are weighed against the estimated cost of the STE to the state.

## Examples of Data Requested

Specific capital equipment that will be purchased and its expected cost

Expected full time equivalent and construction jobs

Projected number of units produced per year

Expected revenue

Projected labor and material costs

Estimated annual state tax liability

Energy generation capacity (AS/AT)

Process improvements (AM)

# Net benefits result

- Analysis results in net benefits score where applicants must score a minimum of 1,000 total points. Points scale to the size of the request, i.e., 1,000 points equals the value of the STE.
- Environmental benefits thresholds are 100 for AS/AT and 20 for AM.
- Additional points are given for the marginal increase in jobs due to the STE; extent of unemployment in project area; etc.

## Net Benefits and Final Score

		Points
Fiscal Benefits (TFB)	\$502,648	999
Environmental Benefits (TPB)	\$337,905	672
Total Cost	(\$503,057)	
<b>Net Benefits</b>	<b>\$337,497</b>	

<b>Net Benefits Score</b>	<b>1,671</b>
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## Other Scoring Factors

<b>Unemployment</b>		
Facility Unemployment Rate		14%
<i>Unemployment Score</i>		20.05507474
<b>New Jobs</b>		
Total facility FTEs		9
Marginal additional jobs		1
Sales tax exclusion/job		\$799,232
<i>New Jobs Score</i>		0
<b>Construction Jobs</b>		
Total construction FTEs		19
Marginal additional jobs		1
Sales tax exclusion/job		\$367,725
<i>Construction Jobs Score</i>		0
<b>Emerging Green Industry</b>		
<i>Emerging Green Industry Score</i>		0
<b>Process Improvement</b>		
Energy Improvement		0
Water Improvement		0
Atmospheric Emissions Improvement		0
Waterborne waste improvement		0
Industrial solid waste improvement		0
Post consumer solid waste		0
<i>Process Improvement Score</i>		0
<b>Non-CA Environmental Benefits</b>		
Annual out of state pollution benefit/unit		\$0.00
Annual out of state pollution cost/unit		\$0.00
Lifetime Net out of state pollution benefit/unit		\$0.00
Total out of state pollution benefit (life of facility)		\$0.00
<i>Non-CA Environmental Benefits Score</i>		0
<b>Sub-total other factors</b>		<b>20</b>
<b>Total Additional Points</b>		<b>20</b>
<b>Final Score</b>		<b>1,691</b>

# Award compliance is established in a legal agreement



- Applicants have 3 years to use the STE, but can request extensions from the CAEATFA Board.
- Applicants must submit annual reports on the status of the project and biannual reports of purchases.
- In certain circumstances, CAEATFA may request the applicant to repay the STE or rescind the award to prevent further use.

# Without a cap increase, the program is likely to be oversubscribed in 2016 and 2017



- CAEATFA suspended acceptance of new applications in November 2015 while the regulations for AB 199 projects are developed and additional program revisions are made.
- AB 199 projects will get the first shot at remaining funds set aside (\$23 MM) by the board in December 2015, however, demand may exceed supply.

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# Proposed modifications



1. Project Cap

4. Application Streamlining

2. Award Timing

5. Compliance

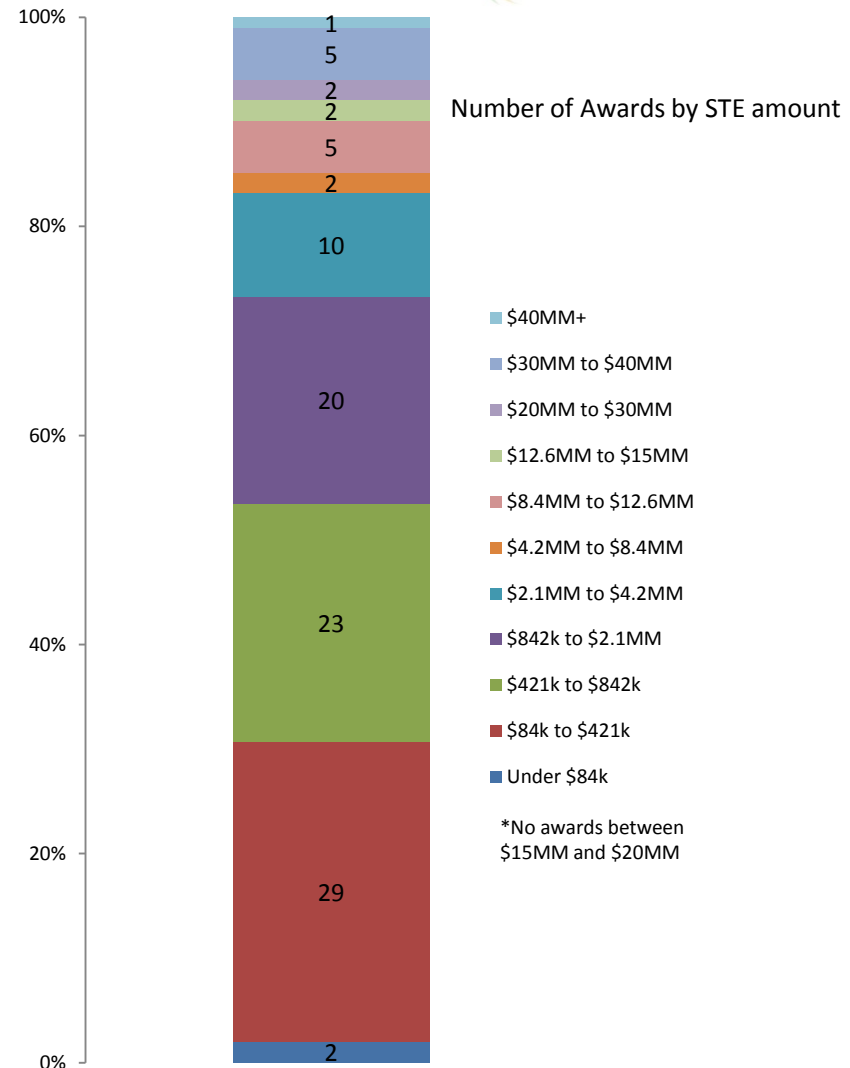
3. Ranking projects

6. AB 199 project evaluation

# Challenge: Oversubscription



- Small projects of less than \$2.1 MM in STE make up almost 75% of approved applications. However, without large projects greater than \$15 MM, CAEATFA would likely not reach cap.
- Projects are not currently capped in the amount they can request. Historically this has not been an issue.





# Proposed modification: Individual project caps



- Individual project caps set at \$20 MM of STE.
  - Provides projects with a meaningful award amount.
  - Can likely accommodate all projects with funding.
  - Reduces chances of oversubscription.
- Year-end release option to assign unallocated funds to previously approved projects that exceed \$20 MM.
  - Ensures that funds are not left on the table when there is existing demand.
  - If there are multiple requests for funding beyond \$20 MM, the remaining allocation would be split evenly.
- Large projects will undergo a one-time net benefits evaluation for their full requested amount. \$20 MM will be available in the first year and the applicant can return in subsequent years to apply for additional funding (also subject to the \$20 MM per year cap).\*
  - For the purposes of subsequent year applications, the one-time net benefits test from the first application year will be used.
  - No additional application fees incurred.

\*CAEATFA is currently looking into how this arrangement might affect functional use.

# Proposed modifications



1. Project Cap

4. Application Streamlining

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# Challenge: Award timing



- To date, CAEATFA has accepted applications on a rolling basis.
  - Provides applicants flexibility and surety to apply at a time that is convenient for business needs.
- The program originally included a readiness measure: a requirement to purchase 25% of Qualified Property within the first year.
  - Intended to encourage “shovel-ready” projects.
  - In light of program undersubscription due to the economic downturn, this requirement was often waived and was subsequently removed.
- Applicants are typically granted three years from Board approval in which to utilize the award.
  - Applicants, upon demonstrating a strong business need, may request extension of the initial term.

# Proposed modification: First come, first served with readiness requirement



- CAEATFA will continue to accept and evaluate applications on a first come, first serve basis (excepting instances of oversubscription, when objective criteria will be used).
  - Allows companies to continue submitting applications on a timeline that matches unique business needs.
- A requirement to complete 20% of qualified purchases within one year of Board approval will be added.
  - Increases the likelihood that award will be used, thereby increasing efficacy of STE allocated.
- The Board will not be able to waive this purchase requirement.
  - Encourages projects that are close to breaking ground and discourages applicants from “sitting on” an award.

# Proposed modifications



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# Challenge: Competitive ranking



- Since project types have been added piecemeal to program, many are dissimilar and cannot be compared directly to one another without disadvantaging one or more categories of applicant.
- Applicants provide best estimates on future business growth up to 3 to 5 years out from time of application consideration. However, estimates are not immediately verifiable.
- Ideal competitive criteria is objective and verifiable at the time of application.

# Proposed modification: Ranking based on objective criteria



- In the event of oversubscription, only applicants in queue that would receive at least 75% of their award request will be considered.
  - The remaining amount of an approved applicant's request will be filled in the following calendar year.
  - If more than one applicant in queue can be funded by at least 75%, points based on objective criteria will be used to rank applicants.

## Potential criteria

Unemployment rate of proposed project location

California headquarters

Small business

Prior STE awards (looking for new applicants)

Eligibility pathway/representation in prior awards

# Proposed modifications



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# Proposed modification: Reduce questions and add automation



- Application process should balance accessibility and rigor.
- Assumptions should be as reliable as possible without putting undue burden on applicants with fewer resources.

## Examples of Proposed Modifications\*

“Estimated annual California Corporation or Income Tax Liability” (formerly box D4).	Many applicants struggle with this question, and we have determined that we can prepare a reasonably accurate estimate, similar to the methodology used to estimate personal income taxes paid by facility employees.
All questions in section G ii (Manufacturing Process Improvements).	No applicants to date have been approved based on their scores in this section and it is therefore not needed.
Environmental Benefits questions (Sections F and G) for BioFuels applicants	Replaced with two questions: “Type of Biofuel produced (select from list)” and “Units of Energy Produced (select from list).”

\* The full list of proposed modifications to the application process is available in Appendix A

# Proposed modifications



1. Project Cap

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# Challenge: Reporting requirements and compliance



- Program participants are currently required to submit three reports per year: two semi-annual reports and one annual report. Reporting requirements can be onerous, but are necessary to meet legislative requirements and program maintenance needs.
  - 2019 Legislative Analyst Office report to Joint Legislative Budget Committee on program effectiveness must evaluate: (1) # of jobs created, (2) retention/attraction of businesses to CA, (3) state and local revenue and economic activity generated, (4) amount of greenhouse gas (GHG), pollution, or energy reduction.
- Semi-annual reporting (list of purchases) required to ensure project compliance.

# Proposed modification: Reduce reporting and add compliance ramification



- Second semi-annual report is combined with annual report.
  - Simplifies the reporting process by reducing the overall number of required reports, while still collecting needed information.
- Reporting deadlines pushed back to August 15<sup>th</sup> for the January to June reporting period, and February 15<sup>th</sup> for the July to December and annual report.
  - Allows more time for program participants to work on reporting and stay compliant.
- STE award is temporarily suspended while program participants are in non-compliance with reporting requirements.
  - Motivates program participants to remain compliant without going to the extreme of revoking the award.

# Proposed modifications



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# Introduction



- AB 199 (Eggman) added recycling and composting projects and projects that manufacture products with at least 50% recycled content to the types of projects eligible to apply for a CAEATFA Sales and Use Tax Exclusion (STE).
- This portion of the presentation describes the proposed project eligibility framework and evaluation criteria for AB 199 projects.

# Program changes for AB 199



- Some of the project categories included in AB 199 were already eligible under CAEATFA's existing STE program.
- Others are newly eligible due to AB 199.
- Previously eligible categories will continue to be evaluated under the existing program rules.
- Newly eligible categories will be scored with a modified evaluation system.

# Eligibility of recycling-related projects under current CAEATFA regulations



Type of Facility/Project	STE Application Pathway
Materials Recovery Facilities	New pathway under AB 199
Composting	
Specialty recyclers (e.g. tire or scrap metal)	
Manufacturing with Recycled Materials	Advanced manufacturing
Intermediate Processing of Recovered Materials	
Biogas	Alternative source



# Application information and scoring



- The new AB 199 project pathway will require the same types financial and environmental information required under the existing application requirements.
- In addition, AB 199 projects will need to indicate the type(s) of recycled materials to be produced.
- The information collected in the STE application will be used to score each project based on its estimated economic and environmental benefits in a manner very similar to the approach used currently.

# Estimating economic and fiscal benefits



- Economic and fiscal benefits of AB 199 projects will be estimated by the same method currently used for alternative source and advanced transportation projects.
- Increases in taxes paid, employment, and supplier purchases will be used to determine the impact of projects.

# Estimating environmental benefits



- Environmental benefits will be estimated based on increases in the total amount of recycled materials produced.
- Using the U.S. Environmental Protection Agency's (EPA) WARM model, which estimates the greenhouse gas benefits of recycling various waste materials, the increase in recycling will be translated into an estimated greenhouse gas (GHG) reduction.
- Greenhouse gas reductions will then be monetized based on economic estimates of the cost of each additional ton of GHG emissions.
- Only projects that increase the amount of recycled materials produced and generate sufficient environmental benefits will be eligible (e.g. replacing an existing piece of equipment with a similar new piece of equipment would likely not qualify).

# Estimating environmental benefits (continued)



- Increases in recycling due to the STE will be estimated as follows:
  - Applicants provide information about total production costs, tons of materials processed, and amount of recycled materials to be produced.
  - CAEATFA then calculates:
    - The change in production costs due to the STE.
    - The resulting increase in recycling due to the incentive effect of the STE based on supply and demand characteristics of the relevant recycling market.
    - The reduction in GHG emissions from the EPA WARM model.
    - The economic benefit from the reduction in GHGs.

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# Next steps for the STE program



- Regulatory Modifications
  - Review feedback from workshop to inform draft regulations (March/April).
  - Draft regulations will be presented to the public for comment (April).
  - Draft regulations to be brought before the Board (May).
  - Complete the regulatory process and open the application process to qualifying AB 199 projects (June).
- Legislative Proposals by the STO
  - Raise Program Cap.
  - Create Roll-over function for un-awarded funds.
  - Make language regarding contractors and subcontractors consistent with the BOE partial exemption program.

# Process Timeline



**March 16: Public workshop**



**March 25: Public comments due**



**April: Workshop to discuss and seek feedback on regulations**



**May 17: Board consideration of proposed regulations**



**June: Authority begins accepting applications from AB 199 eligible projects**



**August: First AB 199 projects go before the Board. Authority resumes accepting applications from all other project types**



**October: First Board meeting at which non-AB 199 projects are heard**

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# Questions for stakeholders



- Are there other indicators of readiness that CAEATFA should consider?
- Are there other objective criteria that CAEATFA could use to rank projects?
- Are there any potential AB 199 applicants who would be willing to do a mock application to help calibrate the scoring?

# Public comment



- All comments must be submitted in writing to [CAEATFA@treasurer.ca.gov](mailto:CAEATFA@treasurer.ca.gov)
- or by mail to:  
CAEATFA  
Attn: AB 199 Program Development  
915 Capitol Mall, Room 457  
Sacramento, CA 95814
- For questions, please contact (916) 651-8157
- Please subscribe to [CAEATFA's listserv](#) or visit the [AB 199 Program Development Page](#)

# Appendix A: Proposed modifications to the application



- CAEATFA proposes eliminating the following questions for all applicant types:
  - “Brief Description of Qualified Property to be purchased” (formerly C1). A description is already provided in the application narrative and on the Qualified Property (QP) Tab.
  - “Estimated Cost of Qualified Property” (formerly C2). The amount of QP is already calculated on the QP Tab.
  - “Estimated Useful Lifespan of the Qualified Property” (formerly C3). This information is already provided on the QP Tab.
  - “Estimated percent of time the QP will be used” (formerly C4). This information is already provided on the QP Tab.
  - “Estimated annual California Corporation or Income Tax Liability” (formerly D4). Many applicants struggled with this question, and we have determined that we can prepare a reasonably accurate estimate, similar to the methodology used to estimate personal income taxes paid by facility employees.
  - “NAICS Code” (formerly E2). This information is inconsistently entered by Applicants and is not used by CAEATFA.
  - “Total facility sales in dollars” (formerly E5). This value is simply the product of per unit price and number of units and can therefore be calculated automatically.
  - All questions in section G ii (Manufacturing Process Improvements). No applicants have been approved based on their scores in this section and it is therefore not needed.
  - Remove the applicant explanation boxes except in cases where such an explanation is mandatory or most commonly utilized by applicants and CAEATFA.

# Appendix A: Proposed modifications to the application (continued)



- CAEATFA also proposes eliminating the following questions for BioFuels and Advanced Manufacturing Applicants:
  - “Expected useful life of product, in years” (formerly E9). This value is always 1 for Biofuels applicants and is not relevant for Advanced Manufacturing Applicants.
  - “Is the product a sub-component of a Qualified Product?” (formerly E11). Biofuels are always end of supply chain products and this question is not relevant for Advanced Manufacturing Applicants.
  - “What is the total value of the efficiency or energy generation component of the end of supply chain product?” (formerly E12). Biofuels are always end of supply chain products and this question is not relevant for Advanced Manufacturing Applicants.
  - “Estimated percent of total end of supply chain product sales in California?” (Formerly E14). Biofuels are always end of supply chain products and this question is not relevant for Advanced Manufacturing Applicants.
  - In addition, we replaced all former Environmental Benefits questions (Sections F and G) for BioFuels applicants with two questions: “Type of Biofuel produced (select from list)” and “Units of Energy Produced (select from list).”
  - Eliminating these questions does not alter the calculation of net benefits. The questions listed above were either redundant (for certain applicant types) or asked applicants to enter values that we are able to estimate or calculate on their behalf.

# Appendix A: Proposed modifications to the application (continued)



- Other proposed changes to the application include:
  - Update the numbering of questions (to reflect the elimination and reordering of questions).
  - “Application Type” question moved from the “Environmental Benefits” (section F tab) to the “Application Information” tab.
  - Re-order the worksheets. After the Application Information tab, the applicant fills out the qualified property worksheet, and then moves to the customized tab for their application type.
  - Add navigational links throughout the workbook. After identifying the application type, an applicant is redirected to the appropriate tab if they go to the incorrect tab.
  - For the environmental benefits questions for applicants identified as “Alternative Energy” and “Energy Efficiency,” energy units changed from requiring all applicants to use MWh to allow the applicant to select the energy unit.