

**CALIFORNIA ALTERNATIVE ENERGY AND
ADVANCED TRANSPORTATION FINANCING AUTHORITY**

Request to Approve Project for SB 71 Sales and Use Tax Exclusion¹

**Gallo Cattle Company
Application No. 10-SM005**

Wednesday, November 17, 2010

Prepared By: *Deana Carrillo*

SUMMARY

Applicant – Gallo Cattle Company

Location – Atwater, Merced County

Industry – Dairy and Cheese Plant

Project – New Biogas Production Facility for an Existing Dairy

Value of Qualified Property – \$1,245,000

Estimated Sales and Use Tax Exclusion Amount² – \$113,295

Application Score –

| | |
|---------------------------------------|--------------|
| Fiscal Benefits Points: | 1,151 |
| <u>Environmental Benefits Points:</u> | <u>6,990</u> |
| Net Benefits Score: | 8,141 |

| | |
|------------------------------------|--------------|
| <u>Additional Benefits Points:</u> | <u>60</u> |
| Total Score: | 8,201 |

Staff Recommendation – Approval

THE APPLICANT

Gallo Cattle Company (“Gallo” or the “Applicant”) is a California limited partnership. Gallo has been a family farm since 1946, which has grown to include cattle and its own line of premium all natural cheese.

¹ All capitalized terms not defined in this document are defined in the Program’s statute and regulations.

² This amount is calculated based off of the average statewide sales tax rate of 9.1%.

The owners of Gallo Cattle Company are:

| | |
|---|--------------------|
| Western Assets LLC, General Partner | 1.000000% |
| Michael Gallo, Limited Partner | 31.236500% |
| Linda Jelacich, Limited Partner | 31.1451625% |
| Michael Gallo Exempt Children's Trust, Limited Partner | 8.457000% |
| Linda Jelacich Exempt Children's Trust, Limited Partner | 8.457000% |
| Micah Gallo, Limited Partner | 3.522700% |
| Tiffanie Gallo, Limited Partner | 3.522700% |
| Peter Gallo, Limited Partner | 3.522700% |
| Ann Marie Jelacich, Limited Partner | 8.135000% |
| Western Marketing and Sales LLC, Limited Partner | <u>1.000000%</u> |
| | <u>100.000000%</u> |

THE PROJECT

The Gallo Cattle Company Renewable Energy Plant (the “Facility”) on the Santa Rita Dairy is scheduled to begin construction in November 2010. The project consists of the installation of a lagoon style anaerobic digester system designed by Williams Engineering and California Bioenergy LLC (CalBio). The biogas destruction unit will convert the methane to electricity and heat, which will be used at the Company’s cheese plant. The electricity will be used to power the plant refrigeration, equipment, pumps and lighting. The heat will be used primarily to pasteurize the milk for the cheese.

The process consists of four main steps: waste collection, digestion, biogas treatment and transfer, and green energy production (this last step is not part of this Application). These activities are integrated into the dairy’s current operations, providing minimum disruption and maximum value to the dairy and cheese plant while also benefiting the environment.

The Gallo Cattle Company Santa Rita Dairy is a freestall dairy with flush lanes located in Atwater, California. There are 3,500 lactating cows housed in freestall barns consisting of flushed feed aprons and freestall lanes. The flushed manure from the flushed lanes, along with the milking parlor wastewater, flow by gravity into a sump. From there, the flushed manure is pumped over an inclined screen separator. The solids are removed for composting or other use, and the liquids from the screen separator flow to a covered lagoon digester. Biogas produced in this digester is treated and then piped to the cheese plant to fuel an internal combustion engine generator and cogen system. Treated water flows to an existing storage lagoon and then to the ranch irrigation system.

There are two major technology components of the process; however, the sales and use tax exclusion would only be used to finance eligible Qualified Property. First, there is an anaerobic digester where dairy cow manure is digested by bacteria and releases biogas comprised of approximately 70 percent methane. This stage is eligible under the SB 71 Program, as the Qualified Property will be used to capture and produce (or condition) dairy manure biogas into a fuel grade source.

The second component, which does not qualify for the SB 71 sales and use tax exclusion, is a combined heat and power engine and generator that burns the biogas and produces electricity for use in the cheese plant and export with waste heat captured to assist in the cheese manufacturing process. The raw biogas is transported by pipeline to the gas handling and treatment equipment. The biogas is dewatered and dried in a gas chiller, processed through an iron sponge scrubber to remove hydrogen sulfide (“H₂S”) to less than 50ppm, then fed to the Greenguard engine-generators to produce electricity for the cheese plant.

ANTICIPATED COSTS OF QUALIFIED PROPERTY

The anticipated Qualified Property purchases are listed below:

| | |
|---------------------------------------|---------------------------|
| Solids Separator | \$ 50,000 |
| Digester Liner and Cover | 985,000 |
| Pipeline System | 145,000 |
| H ₂ S Scrubber | 5,000 |
| Gas Dryer | 10,000 |
| Other Equipment (pumps, blowers, etc) | 50,000 |
| Total | <u>\$1,245,000</u> |

Note: The Qualified Property purchases reported in the Application and shown here in staff's report are estimated costs. At the termination of the conveyance/reconveyance agreement a finalized project equipment list will be prepared detailing the value of the Project equipment conveyed and reconveyed and detailing the actual tax benefit realized pursuant to Revenue and Tax Code Section 6010.8. Variations from the costs shown in the Application and in this report may occur prior to the closing due to increased costs of certain components of the Project from original estimates, and other reasons. In addition, such costs may vary after closing due also to increased costs, as well as common design and equipment modifications during construction, differences in equipment due to future changes in law or regulation or for other reasons.

TIMELINE

The Gallo Cattle Company Renewable Energy Plant is scheduled to begin construction in November 2010. The project has been designed, planned, budgeted and has received its County permit. The Project is expected to be completely installed and operational the third quarter of 2012.

PROJECT EVALUATION

NET BENEFITS

The total cost of the Qualified Property purchases is anticipated at \$1,245,000 and the total net benefits are valued at \$809,038 for the Project. The Project received a Total Score of 8,141

points, which exceeds the required 1,000 point threshold and a total Environmental Benefits score of 6,990, which greatly exceeds the 100 point threshold.

- A. Fiscal Benefits (1,151 points).** The net present value of the total fiscal benefits over the lifetime of the Qualified Property is derived from the Company’s projected sales taxes, personal income taxes paid by the firms’ employees, corporation taxes on profits, property taxes and other indirect fiscal benefits of the Applicant which amounts to a value of \$130,374 resulting in a Fiscal Benefits Score of 1,151 points for the Project.
- B. Environmental Benefits (6,990 points).** The Project provides an estimated \$791,959 of total pollution benefits over the life of the Facility, resulting in an Environmental Benefits score of 6,990 points for the Project. These benefits derive from the production of dairy bio gas, which offsets the need for use of fossil methane. In addition, because the Project will trap methane (a potent greenhouse gas), it is projected the Project will reduce over 9,460 short tons of CO₂e greenhouse gas emissions every year.
- C. Additional Benefits (60 of 200 points).** Applicants may earn up to 200 additional points for their final score. The Applicant submitted information and received 60 additional points.
- 1) Permanent Jobs (0 of 40 points).** The Applicant’s Project will support a total of two (2) permanent jobs at their Facility. CAEATFA estimates that these jobs are not attributable to an approved sale and use tax exclusion. Zero points were awarded because the marginal increase in jobs created does not meet the required threshold.
- 2) Construction Jobs (20 of 20 points).** The Applicant’s Project will provide 28 construction jobs. CAEATFA estimates that of these construction jobs approximately three (3) will be created as a result of an approved sales and use tax exclusion. Therefore, the Applicant was awarded 20 points.
- 3) Unemployment (40 of 40 points).** The Applicant’s Project is located in Merced County, which has an unemployment rate of 19 percent. Since this is above 110 percent of the statewide unemployment average, the Project was awarded an additional 40 points.

STATUS OF PERMITS/OTHER REQUIRED APPROVALS

Gallo Cattle Company has received its county permit for the Facility. It anticipates receiving permits from both the San Joaquin Valley Unified Air Pollution Control District and the Regional Water Quality Control Board (“RWQCB”) in early 2011.

LEGAL QUESTIONNAIRE

Staff reviewed the Applicant’s responses to the questions contained in the Legal Status portion of the Application. The responses did not disclose any information that raises questions concerning the financial viability or legal integrity of this Applicant.

CAEATFA FEES

In accordance with CAEATFA regulations,³ the Applicant paid CAEATFA an Application Fee of \$1,073 and will pay CAEATFA an Administrative Fee of up to \$15,000 if approved for a sales and use tax exclusion.

RECOMMENDATION

Staff recommends approval of Resolution No. 10-SM005 for Gallo Cattle Company’s purchase of Qualified Property in an amount not to exceed \$1,245,000 anticipated to result in an approximate sales and use tax exclusion value of \$113,295.

³ California Code of Regulations Title 4, Division 13, Section 10036.

RESOLUTION APPROVING AND AUTHORIZING THE EXECUTION OF A TITLE
CONVEYANCE AGREEMENT WITH GALLO CATTLE COMPANY

WHEREAS, the California Alternative Energy and Advanced Transportation Financing Authority (the “Authority”) has received the Application of Gallo Cattle Company (the “Applicant”), for financial assistance in the form of a conveyance/reconveyance of title agreement (the “Agreement”) regarding tangible personal property for the design, manufacture, production or assembly of Advanced Transportation Technologies or Alternative Source products, components, or systems (“Qualified Property”) as more particularly described in the staff summary and in the Applicant’s Application to the Authority (collectively, the “Project”); and

WHEREAS, the Applicant has requested the Authority to enter into the Agreement transferring title of Project equipment with a cost not to exceed \$1,245,000 over a period of three years; and

WHEREAS, the Agreement will provide that the Applicant will, prior to any use of the Qualified Property, transfer title at no cost to the Authority from time to time as purchases of Qualified Property are made and the Authority will then transfer title back to the Applicant without having taken possession of the Qualified Property; and

WHEREAS, the Applicant believes that this form of financial assistance will enable it to avail itself of the benefits of an exclusion from sales and use taxes relative to the Qualified Property pursuant to California Revenue and Taxation Code Section 6010.8; and

WHEREAS, approval of the terms of the Agreement and authority for the Executive Director, Deputy Executive Director or Chair of the Authority, to execute the necessary documents to effectuate the Agreement is now sought.

NOW, THEREFORE, BE IT RESOLVED by the California Alternative Energy and Advanced Transportation Financing Authority, as follows:

Section 1. The Project constitutes a “project” within the meaning of Public Resources Code Section 26003(g)(2).

Section 2. The requested conveyance agreement constitutes “financial assistance” within the meaning of Public Resources Code Section 26003(e)(2).

Section 3. The Applicant is a “participating party” within the meaning of Public Resources Code Section 26003(f).

Section 4. The Executive Director, Deputy Executive Director, or Chair of the Authority (the “Authorized Signatories”) are hereby authorized for an on behalf of the Authority to approve

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any changes to the Project as the Executive Director shall deem appropriate provided that the amount of the Qualified Property to be purchased may not be increased above the amount approved by the Authority.

Section 5. The proposed form of the Agreement between the Applicant and the Authority, as filed with the Authority prior to this meeting, is hereby approved. The Authorized Signatories are hereby authorized and directed, for and on behalf and in the name of the Authority, to execute, acknowledge and deliver to the Applicant the Agreement in substantially the form filed with or approved by the Authority, with such insertions, deletions or changes therein as the officer executing the same, may require or approve, and with particular information inserted therein in substantial conformance with the staff summary and the Applicant's Application to the Authority. The Authority understands and agrees that pursuant to the terms of the Agreement, the obligations of the Applicant may, under some circumstances be carried out or assumed by a successor or assignee entity, or by an affiliate of the Applicant.

Section 6. Each of the Authorized Signatories, acting alone, is hereby authorized and directed to do any and all ministerial acts, including (without limitation) the execution and delivery of any and all documents and certificates they may deem necessary or advisable in order to consummate the Agreement and otherwise effectuate the purposes of this Resolution.

Section 7. The Applicant shall assure CAEATFA that all Qualified Property conveyed pursuant to the Agreement shall be installed, maintained and operated in compliance with all applicable local, state and federal laws.

Section 8. The Agreement shall only apply to Qualified Property that the Applicant certifies will be installed, maintained and operated at facilities within the State of California.

Section 9. The adoption by the Authority of this Resolution for the Applicant shall not be referred to in any Application before any governmental agency as evidence of the feasibility, practicality or suitability of the Project or in any application for any required permission or authority to acquire, construct or operate the Project.

Section 10. This Resolution is effective immediately and will remain in full force and effect unless the Regulatory Agreement, as defined in CAEATFA Regulations Section 10035(A), is not executed within thirty (30) days of the date of this Resolution. The Executive Director may extend the thirty days if necessary.