

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

Request to Approve Project for Sales and Use Tax Exclusion (STE)¹

**Rolls-Royce High Temperature Composites Inc.
Application No. 15-SM012**

Tuesday, September 15, 2015

Prepared By: *James Shimp*

SUMMARY

Applicant – Rolls-Royce High Temperature Composites Inc.

Location – Huntington Beach, Orange County

Industry – Composites Manufacturing

Project – Construction of a New High Temperature Composites Facility (Advanced Manufacturing)

Value of Qualified Property – \$8,728,000

Estimated Sales and Use Tax Exclusion Amount² – \$734,898

Application Score –

Fiscal Benefits Points:	1,073
<u>Environmental Benefits Points:</u>	<u>87</u>
Net Benefits Score:	1,160
<u>Additional Benefits Points:</u>	<u>170</u>
Total Score:	1,330

Staff Recommendation – Approval



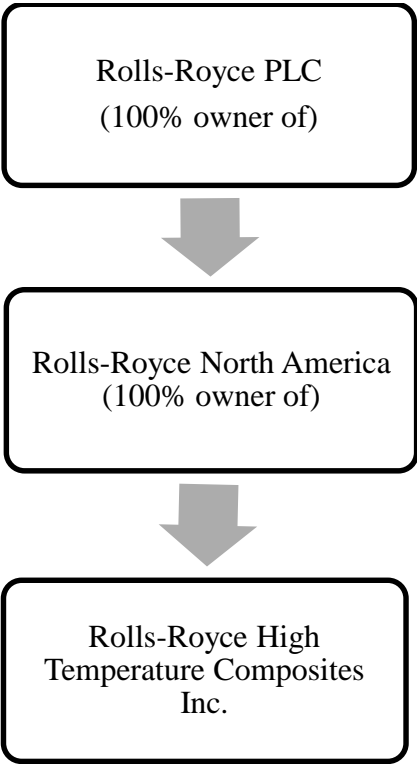
¹ All capitalized terms not defined in this document are defined in the Program’s statute and regulations.

² This amount is calculated based on the average statewide sales tax rate of 8.42%.

THE APPLICANT

Rolls-Royce High Temperature Composites Inc. (“Rolls-Royce” or the “Applicant”) is a California Corporation and wholly owned subsidiary of Rolls-Royce North America, which is a wholly owned subsidiary of Rolls-Royce PLC., which is a publicly traded company. The Applicant was formed to operate a facility in Huntington Beach that develops state-of-the-art composite materials for gas turbine engines.

The chain of ownership for Rolls-Royce High Temperature Composites Inc. is as follows:



The corporate officers of Rolls-Royce High Temperature Composites Inc. are:

- Brad Outland, Sole Director
- Andrew Lazur, President
- Michael N. Elliott, Chief Financial Officer
- William H. Walker, Vice President - Legal
- Danny Szczyrba, Vice President - Tax
- Mary S. Sullivan, Secretary

THE PROJECT

The Applicant is requesting a Sales and Use Tax Exclusion in order to build a new, high temperature composites facility at its location in Huntington Beach (the “Project”). Investment is being made in sophisticated precision machinery, including Computer Numerically Controlled (CNC) machining equipment. The new facility will produce advanced composite materials, such as ceramic matrix composites (CMCs), engineered coatings, and thermal structural components. These composites will be used in gas turbine engines, allowing the engine to run at higher temperatures and with greater efficiency. The Applicant also asserts that CMCs are typically less dense than traditional alloys, allowing for weight reductions that could potentially lead to greater fuel economy.

In addition to the installation of the CNC equipment, the Applicant intends to double its workforce and install machinery designed to reduce the environmental impact of the facility. According to the Applicant, automated cutters and dispensers will reduce solid waste by an estimated 7% and liquid ring vacuum pumps will reduce oil use by 50%.

ANTICIPATED COSTS OF QUALIFIED PROPERTY

The anticipated Qualified Property purchases are listed below:

3D Loom	\$ 500,000
Cleaning Tank and Fume Hoods	47,000
Recipe Dispenser	40,000
Attrition Mill	46,000
Fabric Rigidization system	90,000
Washer	56,000
Ultrasonic Parts Cleaner	130,000
Ultrasonic Assisted Machining Center	981,000
Slurry Removal	45,000
X-Ray Diffractor	364,000
Environmental Furnace and Frame	156,000
Chemical Vapor Infiltration Reactor	1,823,000
Melt Infiltration Furnace	1,394,000
Preform Oven	85,000
Residual Gas Analyzer	52,000
Coordinate Measuring Machine	238,000
Auto Polish	145,000
Glow Discharge Mass Spectrometry	755,000
Resist Array	41,000
Scanning Electron Microscope	400,000
Elec Test Frame	140,000
Txt Cutter	105,000
Acoustic Emission System	50,000

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High Temperature Microscope	111,000
High Definition Microscope	72,000
Digital Imagine Camera	106,000
CT Machine	485,000
Part Marker	127,000
Thermal Analysis Tools	<u>144,000</u>
Total	<u>\$8,728,000</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 master regulatory agreement a finalized project equipment list will be prepared detailing the value of the Project equipment acquired and detailing the actual tax benefit realized pursuant to Revenue and Tax Code Section 6010.8. Variance 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) over 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

Construction of the facility is currently underway, with completion anticipated in November 2015. Equipment installation will begin in early 2016, and the facility is expected to be operational in October 2016.

PROJECT EVALUATION

NET BENEFITS

The total cost of the Qualified Property purchases is anticipated to be \$8,728,000. The Project received a Total Score of 1,330 points, which exceeds the required 1,000 point threshold and a total Environmental Benefits Score of 87 points, which exceeds the 20 point threshold.

- A. Fiscal Benefits (1,073 points).** The net present value of the total fiscal benefits over the lifetime of the Qualified Property is derived from the Applicant's sales taxes, personal income taxes paid by the firm's employees, firm taxes on profits, property taxes and other indirect fiscal benefits of the Applicant which amounts to \$788,866 resulting in a Fiscal Benefits score of 1,073 points for the Project.

- B. Environmental Benefits (87 points).** The Project will result in an Environmental Benefits Score of 87. The Applicant received points in the following categories:
 - 1. Environmental Sustainability Plan (20 of 20 points).** The Applicant will implement an environmental sustainability for its Project that will result in decreases in solid waste, hazardous waste, and air pollution.

2. **Solid Waste (7 of 30 points)**. The Applicant’s manufacturing process will result in a 7% reduction in solid waste produced relative to the industry standard manufacturing process.
3. **Hazardous Waste (30 of 30 points)**. The Applicant’s manufacturing process will result in a 50% reduction in hazardous waste produced relative to the industry standard manufacturing process.
4. **Air Pollutants (30 of 30 points)**. The Applicant’s manufacturing process will result in a 50% reduction in air pollutants produced relative to the industry standard manufacturing process.

C. Additional Benefits (170 points). Applicants may earn additional points for their Total Score. The applicant submitted information and received 170 additional points.

1. **Permanent Jobs (45 of 75 points)**. The Applicant’s Project will support a total of 75 permanent jobs at its Facility. CAEATFA estimates that approximately 5 of these jobs will be attributable to a marginal increase in jobs created due to the approved STE resulting in a Permanent Jobs Score of 45 points for the Project.
2. **Construction Jobs (35 of 75 points)**. The Applicant’s Project will support a total of 30 construction jobs at its Facility. CAEATFA estimates that approximately 2 of these jobs will be attributable to a marginal increase in jobs created due to the approved STE resulting in a Construction Jobs Score of 35 points for the Project.
3. **Research and Development Facilities (25 points)**. The Applicant has verified that it has a facility located in California that performs research and development functions related to composite materials manufacturing.
4. **Workforce Partnerships (25 points)**. The Applicant has a partnership with UC Irvine School of Engineering for the purpose of for the purposes of assisting in the training of potential future workers.
5. **Industry Cluster (40 points)**. The industry associated with this Application has been identified by the Orange County Business Council as an industry cluster of the region of the Project’s location.

STATUS OF PERMITS/OTHER REQUIRED APPROVALS

Building permits have already been obtained, and all other permits, including Air Quality Permits from South Coast Air Quality Management District, will be submitted in March 2016.

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 has paid CAEATFA an Application Fee of \$4,364 and will pay CAEATFA an Administrative Fee up to \$34,912.

RECOMMENDATION

Staff recommends approval of Resolution No. 15-SM012 for Rolls-Royce High Temperature Composites Inc.'s purchase of Qualified Property in an amount not to exceed \$8,728,000 anticipated to result in an approximate sales and use tax exclusion value of \$734,898.

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

**RESOLUTION APPROVING AND AUTHORIZING EXECUTION OF A MASTER
REGULATORY AGREEMENT WITH THE ROLLS-ROYCE HIGH TEMPERATURE
COMPOSITES, INC.**

September 15, 2015

WHEREAS, the California Alternative Energy and Advanced Transportation Financing Authority (the “Authority” or “CAEATFA”) has received the Application of **Rolls-Royce High Temperature Composites Inc.** (the “Applicant”), for financial assistance in the form of a master regulatory agreement (the “Agreement”) regarding tangible personal property utilized in an Advanced Manufacturing process or 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 to acquire Project equipment with an estimated cost not to exceed \$8,728,000 over a period of three years; 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(a)(8)(B).

Section 2. The requested master regulatory agreement constitutes “financial assistance” within the meaning of Public Resources Code Section 26003(a)(6).

Section 3. The Applicant is a “participating party” within the meaning of Public Resources Code Section 26003(a)(7).

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

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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 Authorized Signatory executing the same may require or approve, and with particular information inserted therein in substantial conformance with the staff summary and in the Applicant's Application to the Authority, such approval to be conclusively evidenced by the execution and delivery thereof. 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 listed in the semi-annual reports 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.