

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

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

**Intuitive Surgical, Inc. and its Subsidiary, Intuitive Surgical Operations, Inc.
Application No. 19-SM006**

Tuesday, February 19, 2019

Prepared By: *Xee Moua, Program Analyst*

SUMMARY

Applicant – Intuitive Surgical, Inc. and its Subsidiary, Intuitive Surgical Operations, Inc.

Location – Sunnyvale, Santa Clara County

Industry – Advanced Robotic Surgical Systems and Tools

Project – Upgrade and Expansion of Existing Advanced Robotic Surgical Systems and Instruments and Accessories Manufacturing Facility (Advanced Manufacturing)

Value of Qualified Property – \$96,875,430

Estimated Sales and Use Tax Exclusion Amount² – \$8,098,786

Application Score –

Fiscal Benefits Points:	1,678
<u>Environmental Benefits Points:</u>	<u>65</u>
Net Benefits Score:	1,743
<u>Additional Benefits Points:</u>	<u>90</u>
Total Score:	1,833

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 8.36%.

THE APPLICANT

Intuitive Surgical, Inc. (“ISI”) and its subsidiary, Intuitive Surgical Operations, Inc. (“ISO”) are requesting a sales and use tax exclusion together as Intuitive Surgical, Inc. and its Subsidiary, Intuitive Surgical Operations, Inc. (“Intuitive” or the “Applicant”) to design, manufacture, market and distribute advanced robotic surgical systems and tools used to perform gynecological, urological, general, cardiothoracic, and head and neck surgeries. Located in Sunnyvale at its centralized global headquarters, the Applicant is comprised of two Delaware corporations that are publicly traded under the symbol ISRG. According to the Applicant, ISI was founded in 1995, however for various business reasons, including limitation of liability, ISO was formed. While ISI primarily oversees marketing, selling and administrative activities, and ISO oversees R&D and manufacturing personnel and assets activities, the two entities share overlapping manufacturing and production responsibilities as it operates as one consolidated business.

According to Intuitive, its latest surgical systems are its *da Vinci Xi*, *da Vinci X*, and *da Vinci SP*, which primarily consist of a patient cart, surgeon console, and vision cart. Intuitive’s *da Vinci* systems enable surgeons to perform surgeries such as prostatectomies, hysterectomies, hernia repair, cholecystectomies, nephrectomies, and bariatric surgery—in a less invasive manner. Intuitive states that by combining computational, robotic, and immersive imaging technologies, surgeons are able to operate on patients with greater precision, control, and access, thus reducing patient recovery time.

The corporate officers of Intuitive are:

- Gary S. Guthart, President and Chief Executive Officer
- Salvatore J. Brogna, Executive Vice President and Chief Operating Officer
- Myriam J. Curet, M.D., Executive Vice President and Chief Medical Officer
- David J. Rosa, Executive Vice President and Chief Commercial Officer
- Kara Andersen Reiter, Senior Vice President, General Counsel, and Chief Compliance Officer
- Marshall L. Mohr, Senior Vice President and Chief Financial Officer

THE PROJECT

Intuitive is requesting a sales and use tax exclusion to upgrade and expand its existing design and manufacturing facility located in Sunnyvale, which it represents utilizes science, engineering, and data analytics to produce advanced robotic surgical systems and related instruments and accessories (“I&A”) (the “Project”). According to the Applicant, the Project will add approximately 600,000 square feet of facility space and a state-of-the-art logistics system to efficiently and safely move products throughout the facility, and will upgrade existing R&D, distribution, testing, and prototyping equipment and related property.

According to Intuitive, it produces its products using information technology and data analytics. For example, the Applicant uses machine learning and artificial intelligence to differentiate

different tissues in a patient’s body during surgery, allowing the product’s needle to reduce instances of damage to internal organs and other tissues inside the patient. Additionally, Intuitive states that its EndoWrist I&A include scalpels, forceps, electrocautery, staplers, scissor and other tools that are built with advanced materials that display artificial muscle behavior when small amounts of electricity are applied, providing feedback to the surgeon who is not physically in the patient’s body, and are individually programmed with memory chips that track a multitude of statistics related to usage, as each component may only be used a limited number of times. Lastly, Intuitive states that it has engineered its advanced surgical systems and I&A to work together to computationally filter out the tremors inherent to a surgeon’s hand.

According to Intuitive, the Project will result in 10% less energy consumption after incorporating higher efficiency lighting, and 20% less solid waste generation compared to previous methods due to an increased use of additive manufacturing. The Applicant represents it will also adopt precise tools that utilize algorithms within its microprocessors to carefully build the medical devices to exact specifications. For example, the Applicant’s highly sensitive assembly tools are designed to measure and track the exact amount of torque used during the production process and will alert the technician if the incorrect amount of torque is used.



Figure 1: da Vinci Xi Surgical System Patient Cart



Figure 2: da Vinci I&A

ANTICIPATED COSTS OF QUALIFIED PROPERTY

The anticipated Qualified Property purchases are listed below:

Manufacturing/Production Machinery, Equipment & Materials	\$22,000,000
Facility Buildout, Upgrades & Infrastructure Improvements	18,975,430
Logistics, Transport, Storage Systems & Related Property	8,250,000
Computers, Information Technology & Related Property	6,500,000
Design, Engineering, and R&D Property	16,900,000
Tooling Equipment & Materials	6,750,000
Production/Design Tools, Spare & Repair Parts	4,750,000
Quality Control, Testing & Prototyping	8,750,000
Lab Instruments and Devices	4,000,000
Total	<u>\$96,875,430</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

According to Intuitive, the implementation of new research, design, distribution, testing, and prototyping equipment will begin in Q2 2019 and the installation of its logistics system will be completed by Q4 2019. The Applicant states that an initial 300,000 square-foot facility buildout and expansion will be complete by Q1 2020, and a second build-out phase is expected to commence in Q2 2021.

PROJECT EVALUATION

NET BENEFITS

The Project received a Total Score of 1,833 points, which exceeds the required 1,000 point threshold, and a total Environmental Benefits Score of 65 points, which exceeds the 20 point threshold.

- A. Fiscal Benefits (1,678 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 \$13,591,326, resulting in a Fiscal Benefits score of 1,678 points for the Project.
- B. Environmental Benefits (65 points).** The Project will result in an Environmental Benefits Score of 65. The Applicant received points in the following categories:
- 1. Energy Consumption (10 of 30 points).** The Applicant represents that the Project will result in a 10 percent reduction in energy consumption compared to the Applicant’s previous manufacturing process.
 - 2. Solid Waste (20 of 30 points).** The Applicant represents that the Project will result in a 20 percent reduction in solid waste produced relative to the Applicant’s previous manufacturing process
 - 3. Hazardous Waste (5 of 30 points).** The Applicant represents that the Project will result in a 5 percent reduction in hazardous waste produced relative to the industry standard manufacturing process.
 - 4. Other Pollutants (30 of 30 points).** The Applicant represents that the Project will result in 80 percent reduction in other pollutants produced relative to the industry standard manufacturing process.
- C. Additional Benefits (90 points).** Applicants may earn additional points for their Total Score. The Applicant submitted information and received 90 additional points.
- 1. Production Jobs (40 of 75 points).** The Applicant represents that the Project will support a total of 1,178 production-related jobs at its Facility. CAEATFA estimates that approximately 31 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 40 points for the Project.
 - 2. Construction Jobs (0 of 75 points).** The Applicant represents that the Project will support a total of 94 construction jobs at its Facility. CAEATFA

estimates that approximately two of these jobs will be attributable to a marginal increase in jobs created due to the approved STE. Zero points were awarded because the marginal increase in jobs does not meet the required threshold.

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 the production process existing advanced robotic surgical systems and related instruments and accessories that is the subject of this Application.
4. **Workforce Partnerships (25 points)**. The Applicant has partnerships with Santa Clara University, San Jose State University, Stanford University, UCLA, and UCSD for the purpose of training the workers at the Facility and/or for the purposes of assisting in the training of potential future workers.

STATUS OF PERMITS/OTHER REQUIRED APPROVALS

The Applicant represents all building, operating, and installation permits for the Project have been obtained and are in good standing with the City of Sunnyvale.

LEGAL QUESTIONNAIRE

Staff has reviewed the Applicant's responses to the questions contained in the Legal Status portion of the Application. The Executive Director, in consultation with legal counsel, has determined that the legal issues disclosed do not affect the financial viability or legal integrity of the Applicant.

CAEATFA FEES

In accordance with CAEATFA Regulations,³ the Applicant has paid CAEATFA an Application Fee of \$10,000 and will pay CAEATFA an Administrative Fee of up to \$350,000.

RECOMMENDATION

Staff recommends approval of Resolution No. 19-SM006 for Intuitive Surgical, Inc.'s purchase of Qualified Property in an amount not to exceed \$96,875,430, anticipated to result in an approximate sales and use tax exclusion value of \$8,098,786.

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

**RESOLUTION APPROVING AND AUTHORIZING EXECUTION OF A MASTER
REGULATORY AGREEMENT WITH INTUITIVE SURGICAL, INC. AND ITS
SUBSIDIARY, INTUITIVE SURGICAL OPERATIONS, INC.**

February 19, 2019

WHEREAS, the California Alternative Energy and Advanced Transportation Financing Authority (the “Authority” or “CAEATFA”) has received the Application of **Intuitive Surgical, Inc. and its Subsidiary, Intuitive Surgical Operations, 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 \$96,875,430 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.

Agenda Item – 4.A.5
Resolution No. 19-SM006
Application No. 19-SM006

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.