

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

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

**Northrop Grumman Systems Corporation
Application No. 19-SM009**

April 16, 2019

Prepared By: *Matthew Parsons, Program Analyst*

SUMMARY

Applicant – Northrop Grumman Systems Corporation

Location – Palmdale, Los Angeles County

Industry – Aerospace Manufacturing

Project – Upgrade and Expansion of Existing Aerospace Manufacturing Facility (Advanced Manufacturing)

Value of Qualified Property – \$211,964,787

Estimated Sales and Use Tax Exclusion Amount² – \$17,720,256

Application Score–

Fiscal Benefits Points:	1,518
<u>Environmental Benefits Points:</u>	<u>50</u>
Net Benefits Score:	1,568
<u>Additional Benefits Points:</u>	<u>130</u>
Total Score:	1,698

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

Northrop Grumman Systems Corporation (“Northrop” or the “Applicant”) is a Delaware corporation formed in 1985. Northrop provides innovative systems, products, and solutions in autonomous systems, cyber, C4ISR (command, control, communications and computers, intelligence, surveillance, reconnaissance), space, strike, and logistics and modernization to customers worldwide. Northrop conducts most of its business with the U.S. Government, principally the Department of Defense and intelligence community.

The major shareholders (10.0% or greater) of Northrop Grumman Systems Corporation are:

Northrop Grumman Corporation (100%)

The corporate officers of Northrop Grumman Systems Corporation are:

Stephen C. Movius, President & Treasurer
Mark A. Caylor, Vice President
Christopher T. Jones, Vice President
Janis G. Pamiljans, Vice President
Shawn N. Purvis, Vice President
Talha A. Zobair, Vice President Tax
Jennifer C. McGarrey, Secretary

THE PROJECT

Northrop is requesting a sales and use tax exclusion to upgrade and expand its existing Aerospace Manufacturing facility located in Palmdale (the “Project”). The facility is dedicated to the development and production of a major classified program, as well as work on the F-35 Lightning II fuselage, RQ-4 Global Hawk, Triton, EuroHawk and various other aircraft systems, and maintenance and upgrades on the U.S. Air Force’s fleet of B-2 Spirit bombers.

According to the Applicant, the facility upgrade and expansion will enable the use of composite materials and robotic systems to produce lighter and more efficient classified aircraft, airframes, and aircraft components for Palmdale Aircraft Programs. Northrop states that it will utilize advances in programming, machining, and technology to reduce overall time and assembly costs. According to Northrop, upgrades to their environmental controls will result in a reduction in out-of-cycle downtime in their production areas caused by the inoperability of their evaporative cooling units. The Applicant states that the upgrades within their production areas will result in a reduction of 40 million gallons of water annually compared to previous practices. Northrop also represents that infrastructure upgrades are anticipated to reduce overall energy consumption by approximately 1M kWh (one million kilo watts per hour) compared to previous practices. The infrastructure upgrades include hangar lighting retrofits, light-emitting diode (LED) lighting, replacement of inefficient evaporative cooling units, and upgrades to the facility’s boiler system.

ANTICIPATED COSTS OF QUALIFIED PROPERTY

The anticipated Qualified Property purchases are listed below:

G-KD4X83 Test Articles (Classified)	\$ 126,637,630
G-KD4X73 Production Test Equipment (Classified)	40,450,000
G-KD4X74 N Tooling (Classified)	12,341,199
30-CTF Lab Requirements (Classified)	8,800,000
Execution Risk-Catastrophic, Broken, or Aged Equipment	5,924,000
FTB G-IV Aircraft Instrumental Equipment & Outfitting	2,619,611
F35 Coatings Environmental Control Modifications	3,000,000
IT Equipment, Upgrades, and Servers	3,964,800
F-35 Rate Infrastructure	1,706,507
336 Roof Upgrades	1,600,000
FoS & Lab Upgrades & Technology Refresh	1,950,000
Establish FTF Capability	1,040,000
PBX Retirement	800,000
Mobile Automated Ultrasonic Inspection System	256,000
GSL Cockpit Implementation	200,000
Distribution Center Racking Requirement	156,000
Seal Mixers	69,120
Cap Sprayers	60,000
Downdraft Tables	52,320
Freezers	40,000
Survey Capital	64,000
Clayton Sanders	64,000
911 Recorders	44,800
Vehicle Purchases	67,200
EMCS Cyber Security Compliance	57,600
Total	<u>\$211,964,787</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 the Applicant, the enhancements and updates to the Palmdale facility began in 2018, and are scheduled to be completed by 2020.

PROJECT EVALUATION

NET BENEFITS

The Project received a Total Score of 1,698 points, which exceeds the required 1,000-point threshold, and a total Environmental Benefits Score of 50 points, which exceeds the 20-point threshold.

- A. **Fiscal Benefits (1,518 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 \$26,906,447, resulting in a Fiscal Benefits score of 1,518 points for the Project.
- B. **Environmental Benefits (50 points)**. The Project will result in an Environmental Benefits Score of 50. The Applicant received points in the following categories:
 1. **Environmental Sustainability Plan (20 of 20 points)**. The Applicant will implement an environmental sustainability plan for its Project that it represents will result in a reduction in greenhouse gas emissions by 30%, a reduction in water consumption by 20%, and a reduction in solid waste by 70%.
 2. **Water Use (30 of 30 points)**. The Applicant represents that the Project will result in a 34% reduction in water use relative to the Applicant's previous manufacturing process.
- C. **Additional Benefits (130 points)**. Applicants may earn additional points for their Total Score. The Applicant submitted information and received 130 additional points.
 1. **Production Jobs (60 of 75 points)**. The Applicant represents that the Project will support a total of 4,417 production-related jobs at its Facility. CAEATFA estimates that approximately 210 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 60 points for the Project.
 2. **Construction Jobs (20 of 75 points)**. The Applicant represents that the Project will support a total of 469 construction jobs at its Facility. CAEATFA estimates that approximately 22 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 20 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 Aerospace Manufacturing.
4. **Workforce Partnerships (25 points)**. The Applicant has a partnership with Antelope Valley College for the purposes of assisting in the training of potential future workers.

STATUS OF PERMITS/OTHER REQUIRED APPROVALS

According to the Applicant, all necessary permits have either been obtained or will be obtained when required. Specifically, the Applicant anticipates amending its current Domestic Water Supply Permit by late 2019 with the California State Water Resource Control Board, and an Air Permit, issued at both the local and state level.

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-SM009 for Northrop Grumman Systems Corporation's purchase of Qualified Property in an amount not to exceed \$211,964,787, anticipated to result in an approximate sales and use tax exclusion value of \$17,720,256.

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

**RESOLUTION APPROVING AND AUTHORIZING EXECUTION OF A MASTER
REGULATORY AGREEMENT WITH NORTHROP GRUMMAN SYSTEMS
CORPORATION**

April 16, 2019

WHEREAS, the California Alternative Energy and Advanced Transportation Financing Authority (the “Authority” or “CAEATFA”) has received the Application of **Northrop Grumman Systems Corporation** (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 \$211,964,787 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.1
Resolution No. 19-SM009
Application No. 19-SM009

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.