Date of Hearing: July 3, 2012

ASSEMBLY COMMITTEE ON JOBS, ECONOMIC DEVELOPMENT AND THE ECONOMY
V. Manuel Pérez, Chair
SB 1128 (Padilla) – As Amended: June 18, 2012

SENATE VOTE: 38-0

SUBJECT: Energy: alternative energy financing

SUMMARY: Revises and recasts the provisions of the California Alternative Energy and Advanced Transportation Financing Authority (Finance Authority) and extends financing authority to provide sales and use tax exclusion (SUTE) for projects that promote the utilization of advanced manufacturing. Specifically, this bill:

1) Updates Finance Authority legislative intent to more proactively address issues of sustainable renewable energy sources and advanced transportation technologies.

2) Expands the SUTE Program to include "advanced manufacturing" and defines it through an extended multipart definition to mean, among other things, that the manufacturing improves existing, or creates new, materials, products, and processes through the use of science, engineering, or information technologies, high-precision tools and methods, a high-performance workforce, and innovative business or organizational models for certain technology areas, as follows:
   a) Micro- and nanoelectronics, including semiconductors;
   b) Advanced materials;
   c) Integrated computational materials engineers;
   d) Nanotechnology;
   e) Addictive manufacturing; and
   f) Industrial manufacturing.

3) Excludes from the definition of "advanced manufacturing" technologies and "advanced transportation technologies," those technologies that are required to be undertaken pursuant to state or federal law, regulations, as specified.

4) Revises the definition of "alternative sources" to align with the Renewable Portfolio Standards definition of "renewable electrical generation facilities." Further, the bill adds combined heat and power to the definition, which is consistent with the definition in Waste and Heat and Carbon Emission Reduction Act.

5) Excludes from the definition of financial assistance, contribution of property, labor, or other items of value, and qualifies the terms "insurance" and "guarantees" to only include bond insurance and loan guarantees. The reference to "any other type of assistance the authority deems appropriate" is also removed.

6) Harmonizes the definition of "participating party" with the definition of "pubic agency."

7) Consolidates the Finance Authority's rule making authority.

8) Changes a notice requirement for awarding more than $100 million in SUTE in a year to a limit of $100 million per year.

9) Requires the Finance Authority to study and report by January 1, 2017 on the efficacy and cost benefits of the sales SUTE as it relates to advanced manufacturing including the number of jobs created, the costs of each job, and the annual salary of each job. The study is required to also consider a dynamic analysis of the economic output to the state that would occur without the sales and use tax exemption.

10) Requires the Finance Authority to work with the Legislative Analyst's Office (LAO) to determine the most efficient and cost-effective way for the state to create jobs in advanced manufacturing.

11) Requires, prior to January 1, 2014, and within six months of any significant change to the net benefit test, the Finance Authority to work with the University of California or the California State University to perform a peer review of the net benefits test currently used in evaluating applications.

12) Requires the Finance Authority to study and provide an interim report by January 1, 2015 on the efficacy of the overall program including recommendations on how to increase the program's efficacy in creating permanent and temporary jobs, and whether eligibility for the program should be extended or narrowed to other manufacturing types. The Finance Authority is authorized to work with the LAO in preparing the report and its recommendations.

13) Limits the term of the advanced manufacturing component of the SUTE to July 1, 2016, which is four and one half years less than the overall SUTE program.

14) Repeals specific language that states that in carrying out the provisions of this division, funds may only come from those funds provided under the division. The Legislature has added similar language to other financing authorities as a means to indicate that the program or activity is not backed by the full faith and credit of the state and therefore has no claim to moneys in the General Fund.

15) Repeals a range of programmatic authorities and requirements the Treasurer's Office says have not been used or for which funding has not been provided in a number of years including those related to financing hydroelectric facilities, providing common bond reserve funds for bonds issued by small businesses, and a renewable energy finance program.

16) Makes a series of changes to statute to bring, according to the Treasurer's Office, conformity with state law and business practices concerning conduit bond financing.

17) Moves the Property Tax Assessed Clean Energy (PACE) and Clean Energy Financing Program from Division 16.2 (commencing with Section 26100 of the Public Resources Code) to related sections under the Finance Authority with conforming and harmonizing changes.

18) Makes other technical and conforming changes to the operations of the Finance Authority.

EXISTING LAW:

1) Creates the Finance Authority for the purpose of promoting the development and utilization of alternative energy sources and the development and commercialization of advanced transportation technologies.

2) Authorizes the Finance Authority to administer a state and local sales tax exclusion program (SUTE Program) for tangible personal property that is used for the design, manufacture, production, or assembly of advanced transportation technologies or alternative source products, components or systems. Alternative source products, components or systems include cogeneration technology, energy conservation, solar, biomass, wind, geothermal, specified hydro-electric, or any other energy efficient technologies that reduce the use of fossil and nuclear fuels. Alternative sources would also include advanced electric distributive generation technology and energy storage technology.

3) Requires the Finance Authority to evaluate the SUTE Program project applications based on the extent to which: (a) the project develops manufacturing facilities or purchases equipment in California; (b) the benefits of the project to the state equal or exceed the benefits to the project applicant and other participants; (c) the project creates new permanent jobs in California; (d) the project results in a reduction in greenhouse gases, a reduction in air or water pollution, an increase in energy efficiency, or a reduction in energy consumption, beyond what is required by state or federal law; (e) unemployment exists in the area in which the proposed project is to be located; and (f) any other factors deemed appropriate.

4) Establishes a renewable portfolio goal of 33% of total retail sales of electricity by December 31, 2020.

FISCAL EFFECT: Unknown

COMMENTS:

1) Purpose of the Bill: According to the Author, "Last summer President Obama launched the Advanced Manufacturing Partnership, to 'invest in the emerging technologies that will create high quality manufacturing jobs.' The program directs more than $1billion to promoting advanced manufacturing. The Advanced Manufacturing Partnership offers new opportunities for California to draw down federal dollars, attract new investment, and employ our workforce. States such as Massachusetts, Michigan and Georgia are creating collaborative centers between industry and government to attract advanced manufactures and draw down the federal dollars. California must act to remain competitive.

   The California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is an existing authority within the Office of the State Treasurer that can attract and retain manufacturers. In the first year alone the program approved 26 projects which generated $950 million in investments in California. These investments are projected to create an estimated 6,027 jobs; 3,936 permanent jobs and 2,091 construction jobs. CAEATFA is a successful model for leveraging state dollars to create new jobs and investments. SB 1128 will expand the success of the program by adding “Advanced

Manufacturing" as one of the top priority criteria CAEATFA will use to determine the allocation of exemptions."

2) Double Referral: This bill was double referred to the Assembly Committee on Revenue and Taxation (R&T) and the Assembly Committee on Jobs, Economic Development, and the Economy (JEDE). The R&T hearing is scheduled for July 2, 2012 and JEDE will hear the bill on July 3, 2012.

3) Background on the Finance Authority: The Finance Authority was established in 1980 for the purpose of providing capital for facilities utilizing alternative methods and sources of energy and facilities needed for the development and commercialization of advanced transportation technologies. The Finance Authority overs a range of financial products including conduit bond and revenue bond financings, loan guarantees, loan loss reserve accounts among other financial products that support the development and commercialization of technologies that conserve energy, reduce air pollution, and promote economic development and jobs.

   Examples of some of the Finance Authority's more unique financial products include $381 million in Qualified Energy Conservation Bonds authorized under the federal American Recovery and Reinvestment Act and the SB 77 Property Assessed Clean Energy (PACE) Bond Program. Governor Arnold Schwarzenegger, as another example, used the Finance Authority to assist a joint venture between Tesla Motors and Toyota Motors to purchase the Nummi assembly plant in Fremont, California where the two companies focus on manufacturing hybrid and electric vehicles, including the TESLA brand.

   Most recently, the role of the Finance Authority was expanded to include administration of a state sales and use tax exclusion for property used in the "design, manufacture, production, or assembly" of either advanced transportation technologies or alternative energy source products, components or systems [SB 71 (Padilla), Chapter 10, Statutes of 2010]. The intent of the SUTE Program is to promote the creation of California-based manufacturing, California-based jobs, and the reduction of greenhouse gases, air and water pollution, or energy consumption. Interest in the program was high at the program's inception but has since tapered off, as indicated by the fact that approximately 60% of the projects were approved within the first eight months of the program.

   The Finance Authority is overseen by a five-member board of directors comprised of the Treasurer (chair), Controller, Director of Finance, Chairperson of the Energy Commission, and President of the Public Utilities Commission. The Finance Authority meets on a monthly basis and members of the board serve without compensation. The day-to-day activities of the Finance Authority are overseen by an executive director, who serves at the pleasure of the board.

4) Sustainable Change May Require More Balance: SB 1128 prohibits SUTE financing of advanced manufacturing and advanced transportation technologies that are required to be undertaken pursuant to state or federal law. Concerns have been raised that this change could effectively remove a growing number of emerging technologies, such as fuel cells and advanced microturbines, which have already demonstrated meaningful levels of greenhouse gas emission reductions and air quality benefits. Further, the bill specifically allows financing of combined heat and power technologies even though these technologies are not necessarily powered by renewable fuel sources.

With California businesses continuing to face significant challenges in accessing capital, even profitable companies find it difficult to finance the retooling and upgrading of production lines. Many of these challenges remain substantively out of the control of the business including the effect of reduced revenues resulting from lower consumer demand, reductions in the real estate value of collateral that could be used to access new debt, a growing ability of cleantech capital to flow globally rather than remain in California, and stricter federal regulations on the balance sheets of traditional sources of capital, such as banks. While it is a laudable goal for the state to support manufacturers that produce technologies that only result in higher than mandated environmental standards, it may be premature to restrict state resources in this manner.

New and more flexible sources of capital are necessary to the extent that California wants to leverage California-grown R&D, expand manufacturing of products that result in a cleaner environment, and increase quality jobs, while still improving air quality and producing less greenhouse gas emissions. State policies will need to reflect sustainable values whereby programs are socially, environmentally and economically viable.

5) Updating Statute without Public or Stakeholder Engagement: Amendments taken on June 19, 2012 propose to modernize the Finance Authority statute in order to better meet the changing needs of California businesses. Generally, when these types of comprehensive updates are undertaken, the amendments are placed in a bill well before the final policy hearing of the session, a stakeholder working group might be formed, the sponsoring government body may hold a hearing to vet the changes among program users, or, at a minimum, a draft of the changes would be circulated among interested parties to solicit written comments. In the case of SB 1128, committee staff is unaware that any of these types of actions occurred.

   Although the language has only been in print for one week, several affected industry groups have expressed concerns that the most recent amendments go beyond technical and include significant policy shifts for the Finance Authority. Other language proposes to remove programs because they have not been funded for a number of years. Examples of eliminated programs include the common bond reserve fund program targeted to small businesses and a renewable energy finance program.

   While some of these changes may be appropriate, full discussion and adequate time for public input on modernization changes is very important. Sometimes concerns can be resolved through discourse, while others may require amendments or removal from a technical clean-up bill.

6) Purpose of the Finance Authority: The State Treasurer serves as the Chairperson for a number of state financing authorities including, but not limited to, the:

   a) California Pollution Control Financing Authority;
   b) California Educational Facilities Financing Authority;
   c) California Health Facilities Financing Authority;
   d) California Industrial Development Financing Advisory Committee;

e) California School Finance Authority; and
f) California Transportation Finance Authority.

While most of these financing entities have specific and distinct areas of expertise, several have overlapping missions and programs. The finance authority which has, perhaps, the least clear mission is the subject of this measure. New programs have been added, without a clear understanding of why a clean technology project would go to one of the financing entities rather than another. Alternatively, why do several of the financing entities operate loss reserve account or loan guarantee programs? While this may be too broad of an issue for the Committee to consider at the last policy hearing of the 2011-12 legislative session - SB 1128 brings this long lingering issue to a head for one financing entity.

7) Manufacturing in California: Manufacturing is one of the state's top five private industry sectors, responsible for employing 1.24 million workers (8.9%) and contributing over $206.2 billion to the state's $1.9 trillion GDP. Manufacturing employment is sometimes referred to as the gold standard because it pays high wages (usually with benefits), supports the state's access to the broader global market and provides a key link in the extended network of small- and medium-sized businesses that participate in the production, distribution and retail supply chain. Further, the Milken Institute estimates that every job created in manufacturing supports 2.5 jobs in other sectors. In some industry sectors, such as the electronic computer manufacturing, the multiplier effect is 16 to one.

   Manufacturing in California, however, even prior to the current economic recession, faced many challenges maintaining global and domestic competitiveness, including accessing a skilled workforce to support the changing needs of manufacturing and goods movement and maintaining cost-effective productivity in the face of lower safety and wage standards in emerging foreign markets.

   The California Manufacturers and Technology Association estimate that California lost 613,000 manufacturing jobs from its peak in January 2001 to September 2011. While part of this reduction reflects the loss of high-tech jobs in 2001 and 2002 and the current recession, the industry as a whole is suffering. California's loss of manufacturing jobs is not unusual among Western states. It is, however, more severe with California's loss reported to be -34% between 2001 to 2010, as compared to Arizona (-30%), Nevada (-12%), Oregon (-29%) and Texas (-21%).

   Similar findings were made in a June 2010 report by the Milken Institute, "Manufacturing 2.0: A More Prosperous California," which also found that California's competitive position is losing ground to other states and nations based on its regulatory climate, tax burden and reputation as a difficult and costly place to do business.

8) Manufacturing Incentives in other States: California communities are in competition to attract and retain manufacturers. Many states have developed economic development programs that target manufacturing generally, while others focus on sub-industry and sub-subindustry sections such as energy generation, information technology, biotechnology and food processing. As an example, the U.S. Department of Energy has taken a closer look at state incentives related to attracting renewable energy production and manufacturing and reports that 24 states have tax credits, 28 states authorize property assessed clean energy

(PACE) programs, and 38 states offer property tax-based incentives. Below are examples of three nationally recognized state initiatives:

a) *Michigan SmartZones*: Michigan's 15 SmartZones include technology business accelerators and incubators that provide the critical entrepreneurial and commercialization support services essential to growing start-up ventures. The program consists of collaborations among universities, industry, research organizations, government and other local institutions and has resulted in regionally based high-tech zones which target growth in a specific economic sector that fits the geographic region's strengths and needs, creating clusters of high-skilled, high-paying jobs.

b) *Arizona Clean Technology Property Tax Reduction and Tax Credit*: The goal of the program (enacted in 2009) is to encourage business investment that will produce high quality employment opportunities and enhance Arizona's position as a center for production and use of renewable energy products. The program offers two benefits: up to a 10% refundable income tax credit and up to a 75% reduction on property taxes for 10 years, for companies that are primarily engaged in manufacturing or have headquarters for producing systems and components that are used or useful in manufacturing renewable energy equipment. To be eligible for these benefits, companies must meet and maintain certain requirements, including paying wages above the state's annual median wage, paying certain health care costs and making annual investments in equipment.

c) *Missouri TechLaunch*: The Missouri Technology Corporation (MTC) is a public-private partnership created by the Missouri Legislature to "promote entrepreneurship and foster the growth of new and emerging high-tech companies." One MTC initiative is the Missouri TechLaunch which offers pre-seed funding to start-ups for intellectual property development and evaluation, including in-depth market analysis, competitive analysis, proof of concept, and prototype design and development. Individual awards cannot exceed $100,000 and may be in the form of equity or convertible debt.

9) Technical Issues: Whenever a measure proposes to revise and recast significant portions of law, it is not unusual for there to be a variety of technical issues. It is suggested that the Committee direct staff to work with the author and the Finance Authority to make a number of technical changes including, but not limited to, correcting cross references, harmonizing potentially repetitive studies, codifying the net benefit test, inserting a statement that limits exposure of the General Fund to the Finance Authority activities, and redirecting economic development studies away from the Finance Authority and the LAO to the Governor's Office of Business and Economic Development.

10) Related Legislation: Below is a list of related bills from the current and previous sessions.

a) *AB 231 (V. Manuel Pérez and Alejo) Enterprise Zone Reforms*: This bill makes a number of key changes to the enterprise zone program to make it more accountable and effective in reducing poverty and strengthening the economies of lower income communities. Among other reforms, the bill increases the value of the hire credit for manufacturing jobs from 150% of minimum wage to 202%. Status: The bill was retained with the Assembly Committee on Jobs, Economic Development and the Economy, January 2012. The compromise will be included in AB 1411 (V. Manuel Pérez and Alejo).

b) *AB 894 (V. Manuel Pérez) California Manufacturing Act of 2011*: This bill would have authorized the establishment of the California Manufacturing Competitiveness Act of 2011 for the purpose of supporting the retooling and expansion of California's manufacturing facilities, enhancing the state's logistics network, and retaining and creating jobs. Status: The bill was vetoed by the Governor in October 2011.

c) *AB 904 (V. Manuel Pérez) Capital Investment Incentive*: This bill expands the definition of a qualified manufacturing facility eligible for local capital investment incentive payments to include a facility operated by a business engaged in the manufacturing of parts or components related to the production of electricity using solar, wind, biomass, hydropower, or geothermal resources on or after July 1, 2010. Under this program, manufacturers that make capital investments of over $150 million are eligible for a specified property tax rebate. Status: The bill was signed by the Governor, Chapter 486, Statutes of 2009.

d) *AB 2437 (V. Manuel Pérez) California Manufacturing Competitiveness Act of 2010*: This bill would have authorized the establishment of the California Manufacturing Competitiveness Act of 2011 for the purpose of supporting the retooling and expansion of California's manufacturing facilities, enhancing the state's logistics network, and retaining and creating jobs. Status: The bill was vetoed by the Governor in October 2010.

e) *SB 71 (Padilla) Sales and Use Tax Exemption*: This bill authorizes the Finance Authority to administer a state and local sales tax exclusion program for tangible personal property that is used for the design, manufacture, production, or assembly of advanced transportation technologies or alternative source products, components or systems. Status: The bill was signed by the Governor, Chapter 10, Statues of 2010.

REGISTERED SUPPORT / OPPOSITION:

Support

Applied Materials
BayBio
Boeing
Boehringer-Ingelheim
California Health Care Institute
Pharmaceutical Research and Manufacturers of America

Opposition

None received

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