SENATE COMMITTEE ON GOVERNANCE AND FINANCE
Senator Mike McGuire, Chair
2021 - 2022 Regular

Bill No:	AB 726	**Hearing Date:**	6/17/21
Author:	Eduardo Garcia	**Tax Levy:**	No
Version:	2/16/21	**Fiscal:**	No
Consultant:	Peterson		

CAPITAL INVESTMENT INCENTIVE PROGRAM: QUALIFIED MANUFACTURING FACILITY

Allows cities and counties to offer Capital Investment Incentive Program incentives to businesses engaged in the manufacturing of fuels, electrical parts, or components used in clean transportation or the production of alternative fuel or electric vehicles.

Background

Property tax. Article XIII of the California Constitution provides that all property is taxable at the same percentage of fair market value unless explicitly exempted by the Constitution or federal law. The Constitution limits the maximum amount of any ad valorem tax on real property at 1% of full cash value, and directs assessors to only reappraise property when newly constructed, or ownership changes (Proposition 13, 1978). Proposition 13 additionally limits any inflationary growth of the full cash value base to 2% per year.

Capital Investment Incentive Program. Under the Capital Investment Incentive Program (CIIP), counties and cities can pay a capital investment incentive amount for 15 years to a proponent of a qualified manufacturing facility (QMF) making an initial investment that exceeds $150 million. The proponent must apply to the city or county by filing a request, which must be approved by majority vote of the city or county's governing body for payments to commence. If approved, a proponent receives a payment equal to the amount of property taxes paid and received by that city or county that exceeds $150 million of the facility's value - other agencies' shares of tax revenues from that property are not affected. In return for this property tax rebate, the proponent must then pay a community service fee equal to 25% of the capital incentive amount, up to $2 million a year. The proponent must also sign a community services agreement that spells out the fee, payment conditions, a job creation plan that requires employer-sponsored health care and payment of an average wage not less than the state average, and provisions to recapture the incentive payments if the proponent fails to run the facility as agreed. Additionally, a city or special district may pay the county or city an amount equal to the amount of property tax revenue that the local government receives from the facility's property taxes paid on the facility's value over $150 million. The city or county must submit annual reports on the incentives it approves to the Governor's Office of Business and Economic Development (GO-Biz), which GO-Biz compiles into a report it submits to the Legislature.

To qualify for this tax rebate program, a QMF must be engaged in commercial production, the perfection of the manufacturing process, or the perfection of a product intended to be manufactured. The proponent of the facility must also:

- Have an initial investment in real and personal property over $150 million GO-Biz certifies;
- Be located within the county or city offering the capital incentive program; and
- Be operated by a business within specified North American Industrial Classification System (NAICS) codes, that includes firms engaged in various types of manufacturing, research and development, recovery of minerals from geothermal resources, and components related to electricity production.

The Legislature originally approved the program to help Placer County officials attract an Intel plant, but they never used the law (SB 566, Thompson, 1997). Legislators expanded the definition of a qualified manufacturing facility to include CalEnergy Company's plan to extract minerals from geothermal brine, which did not launch (SB 133, Kelley, 1999). In 2009, the Legislature further expanded the program to include other manufacturers that produce electricity using solar, wind, biomass, hydropower, or geothermal resources and shifted the responsibility to certify the investment to the Business, Transportation and Housing Agency; and sunset the program on January 1, 2017 (AB 904, V.M Perez).

In 2012, the Legislature expanded the program to (SB 1006, Committee on Budget and Fiscal Review):

- Include research and development facilities;
- Raise the threshold investment amount from $150 to $250 million;
- Lower from $150 million to $25 million the assessed valuation threshold that trigger capital investment incentive payments equivalent to property taxes paid;
- Revise eligibility criteria; and
- Shift the duty to certify investments to GO-Biz.

SB 1006 sought to entice Samsung Semiconductor to expand its manufacturing facility in San Jose; however, the facility was constructed without the incentive agreement being executed, with the company instead applying for and receiving California Competes tax credits. SB 1006 repealed all of its changes on June 30, 2013.

In 2014, the Legislature again reauthorized the program, expanded the NAICS codes to include additional manufacturers, and lowered the threshold to trigger incentive payments from $150 million in value to $25 million. The bill was part of a package of incentives to attract production of the United States Air Force's new long-range bomber to California (AB 2389, Fox, and SB 718, Roth, 2014). The specific programmatic changes sunset on January 1, 2016, thereby defaulting to the threshold investment amounts and minimum value thresholds to those the Legislature originally set in 1997. Both bills set the program to sunset entirely on January 1, 2018. However, in 2017, the Legislature extended the program from January 1, 2018, to January 1, 2019, at the request of Imperial County and ES Minerals, a firm seeking to extract lithium from a location near the Salton Sea (AB 755, E. Garcia). In 2018, the Legislature extended the program once again from January 1, 2019, to January 1, 2024 (AB 1900, Brough).

GO-Biz report. In December 2019, GO-Biz submitted a report covering plan activity under the program through June 30, 2019. The report indicated that the following cities had approved a resolution establishing a CIIP:

- The City of Palmdale entered into a 15-year agreement with the Lockheed Martin Corporation, which agreed to invest $385 million in new facilities if it secured the Department of Defense (DOD) contract to manufacture the new strategic aircraft program. The agreement would have paid Lockheed Martin $740,000 annually, with a Community Service Fee of an unspecified amount.
- The County of Los Angeles entered into a 15-year agreement with the Lockheed Martin Corporation if it secured the same contract. The agreement would have paid Lockheed Martin $3.08 million annually, with a community services fee of $1.02 million.

However, DOD awarded the contract to another bidder, so no payments were made. The County of Los Angeles and the City of Long Beach entered into an agreement with Weber Metals, Inc., where the county entered into a 15-year agreement to make a payment of $1.04 million and the city makes one of $709,000, in exchange for annual community service fees of $348,607 and $265,000, respectively. GO-Biz indicated that the facility is currently under construction, so no payments have yet been made. If GO-Biz certifies the investment, it would become the first time the program has been used in its 24-year life. GO-Biz has not received notifications of new CIIP agreements from local governments since 2015, despite receiving several inquiries from local governments and interested manufacturer proponents.

Alternative fuels and electric vehicles. On September 23, 2020, Governor Newsom issued Executive Order N-79-20, which states, "It shall be a goal of the State that 100 percent of in-state sales of new passenger cars and trucks will be zero-emission by 2035. It shall be a further goal of the State that 100 percent of medium- and heavy-duty vehicles in the State be zero-emission by 2045 for all operations where feasible and by 2035 for drayage trucks. It shall be further a goal of the State to transition to 100 percent zero-emission off-road vehicles and equipment by 2035 where feasible." To meet this goal, the order requires various state agencies to develop and implement strategies to encourage the adoption of such vehicles. One of the key challenges in reaching these goals is the development of the fuels, electrical parts, or components these technologies need to function, such as lithium and other components batteries use.

According to the California Energy Commission (CEC), as much as 1/3 of the world's current lithium deposits are in California, and deposits in the Imperial Valley could produce up to $860 million annually. AB 1657 (E. Garcia, 2020) authorized CEC to convene a Blue-Ribbon Commission on Lithium Extraction (Lithium Valley Commission) to analyze lithium extraction issues in state, which will submit a report to the Legislature on or before October 1, 2022. CEC has also issued grants through its Electric Program Investment Charge (EPIC) program for lithium extraction, including $6 million to BHER Minerals, LLC for a demonstration project at an existing geothermal power facility in Calipatria, a city in Imperial County, to cost-effectively process at least 100 gallons of geothermal brine per minute to produce battery-grade lithium carbonate.

To encourage more lithium production and other related facilities to locate in California, the author wants to allow CIIP incentives to create incentives for manufacturers of certain alternative fuel or electric vehicle parts to locate in California.

<u>Proposed Law</u>

Assembly Bill 726 allows cities and counties to offer Capital Investment Incentive Program (CIIP) incentives to businesses engaged in the manufacturing of fuels, electrical parts, or components used in the field of clean transportation or the production of alternative fuel vehicles or electric vehicles.

State Revenue Impact

No estimate.

Comments

1. Purpose of the bill. According to the author, "The Imperial County, recently coined as The Lithium Valley due to its significant amount of underground lithium deposits, has a unique opportunity to attract battery manufacturers as a result of this natural resource as well as an opportunity to develop other renewable and clean transportation projects. In the past, the County has additionally looked to the CIIP program to attract a significant number of jobs to the region in a county with the highest unemployment rate in the nation. However, currently the CIIP does not incentivize the investment of these clean transportation projects. In order to expand on possible investments into local regions of California and to help meet our clean transportation and air quality goals, the CIIP program needs to include incentives for the manufacturing of fuels, electrical parts, or components in the field of clean transportation or the production of alternative fuel vehicles or electric vehicles."

2. Right way? AB 726 expands CIIP to additional manufacturers, which allows cities and counties to refund property taxes received solely by that jurisdiction to specified firms, under the assumption that the net economic benefits to that city or county exceed the amounts refunded. The state foregoes almost $75 billion annually in tax expenditures, some for economic development purposes. The CIIP program gives local agencies the option to do so as well. Without the revenue diverted for these incentive payments, local agencies have less funding to pay for important public services such as public health safety. AB 726 expands the program in the hopes that the economic benefits outweigh the foregone revenue. However, these incentives may reward some manufacturers that planned to locate their facility in a particular jurisdiction regardless of the incentive. In these instances, the local agency receives no marginal benefit, and provides a windfall benefit to the manufacturer. No state tax expenditure has yet conclusively demonstrated that its benefits outweigh its costs. Is there any reason to believe that when local agencies offer the incentives, the benefits will prove more conclusive? The Committee may wish to consider the general effectiveness of property tax rebates toward creating economic development.

3. How does this work? If a city council or county board of supervisors approves the proponent's request, he or she pays their property tax as they would normally under current law. The local agency approving the request then sends a payment equal to the amount of the share of the property tax they received on the value of the facility that exceeds $150 million less the community service fee. A firm that constructs a facility valued at $200 million pays $2 million in tax at a 1% rate. If the local agency approving the request receives a 15% share of the allocated property tax for that property in that specific tax rate area, the payment is $75,000 ($200 million - $150 million = $50 million x 1% rate x the 15% share), less the $18,750 (25%) community service fee, for a net payment of $56,250 annually for up to 15 years. The Committee may wish to consider whether AB 726 will sufficiently influence manufacturers' decisions regarding where to locate their facilities.

4. Sure, but will it work? Since CIIP's creation in 1997, various local agencies have sought to use the program, but none have done so successfully. According to GO-Biz, while some local agencies and companies have expressed interest, the office has not received notifications of new CIIP agreements from local governments since 2015. Despite the program's challenges, AB 726 expands the program to cover additional manufacturers. The bill's supporters note that Imperial Valley has come close to executive a successful CIIP program in the past, and that companies have already expressed interest in locating lithium facilities in the Imperial Valley if these incentives materialize. Will expanding CIIP to additional manufacturers make the program more effective?

5. Subsidies and schools. In addition to counties and cities, special districts can also make incentive payments to manufacturers under the program. However, the underlying law is unclear regarding whether the definition of special districts also includes school districts. If the measure allows school districts to do so, why should school districts shift funds from education purposes to pay for economic development incentives? While current law prohibits special districts from paying the actual property tax allocation to the recipient, likely nullifying any state Proposition 98 backfill for a school district from the state General Fund, the Committee may wish to consider amending the measure to preclude school districts from making incentive payments.

6. Sunset. CIIP sunsets in 2024. As such, local governments would have two years to offer these incentives before requiring further legislative action.

7. Related legislation. AB 983 (Eduardo Garcia, 2021) authorizes a public entity to use, enter into, or require contractors to enter into, a community workforce agreement (CWA) for construction projects related to battery manufacturing and lithium-based technology. This bill is currently pending in the Senate Governmental Organization Committee. Additionally, the Committee approved AB 1248 (Eduardo Garcia, 2019) on a vote of 5 to 0 to allow cities and counties to offer CIIP incentives to small and mid-size manufacturers. This bill was subsequently amended to relate to a different subject.

Assembly Actions

Assembly Local Government Committee:	8-0
Assembly Floor:	74-0

Support and Opposition (6/14/21)

Support: Energy Source; Imperial Valley Economic Development Corporation

Opposition: None submitted

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