LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 84TH LEGISLATIVE REGULAR SESSION

May 21, 2015

TO: Honorable Jane Nelson, Chair, Senate Committee on Finance

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: **HB2096** by Button (Relating to the temporary exemption of certain tangible personal property related to certain multi-user data centers from the sales and use tax.), **As Engrossed**

Estimated Two-year Net Impact to General Revenue Related Funds for HB2096, As Engrossed: a negative impact of ($31,200,000) through the biennium ending August 31, 2017.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2016	($10,900,000)
2017	($20,300,000)
2018	($29,100,000)
2019	($37,900,000)
2020	($39,300,000)

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue (Loss) from *General Revenue Fund* 1
2016	($10,900,000)
2017	($20,300,000)
2018	($29,100,000)
2019	($37,900,000)
2020	($39,300,000)

Fiscal Analysis

The bill would add a new Section 151.3591 to the Tax Code, relating to certain multi-user data centers that may qualify for exemption of certain items from sales and use tax.

"Multi-user data center" would be defined to mean all or part of a new or redeveloped facility that: is located in this state and is composed of one or more buildings and related improvements located on a parcel of land or parcels of land in close proximity; is specifically constructed or refurbished, repaired, restored, remodeled, or otherwise modified and actually used primarily to house servers and related equipment and support staff for the processing, storage, and distribution of data; is designed for use by one or more qualifying occupants; is not used primarily by a telecommunications provider to deliver telecommunications services; and has an uninterruptible power source, generator backup power, a fire suppression and prevention system, and certain physical security characteristics.

A qualifying multi-user data center would be required to create at least five jobs that will exist for at least three years and pay at least 120 percent of the county average wage in the county in which the job is based, and to make or agree to make, on or after September 1, 2015, a capital investment of at least $100 million in that particular multi-user data center over a 10 year period. The capital investment must exclusively serve qualifying occupants that execute contracts on or after September 1, 2015, and who were not under contract with the qualified owner or operator before then.

A "qualifying occupant" would be someone who contracts for at least 1,000 kilowatts of critical IT load per month for a period of at least two years.

The bill would exempt from tax tangible personal property that is necessary and essential to the operation of a qualifying center if the property is purchased for installation at, incorporation into, or in the case of electricity for use in, a qualifying multi-user data center if the tangible personal property is: electricity; an electrical system; a cooling system; an emergency generator; hardware or a distributed mainframe computer or server; a data storage device; network connectivity equipment; a rack, cabinet, and raised floor system; a peripheral component or system; software; a mechanical, electrical, or plumbing system necessary to operate the foregoing property; any other item of equipment or system necessary to operate any of the foregoing, including a fixture; and a component part of any of the foregoing. Excluded from exemption would be: office equipment or supplies; maintenance or janitorial supplies or equipment; equipment or supplies used primarily in sales activities or in transportation activities; property for which a refund may be received under Section 151.429 (tax refunds for enterprise projects); tangible personal property not otherwise exempted that is incorporated into real estate or an improvement of real estate; tangible personal property that is rented or leased for a term of one year or less; or notwithstanding Section 151.3111, a taxable service that is performed on tangible personal property exempted under Section 151.3591.

The exemption would expire on the tenth anniversary of the date a multi-user data center was certified as qualifying by the Comptroller if the 10 year capital investment in the data center is at least $100 million but less than $150 million, or on the fifteenth anniversary if the capital investment is $150 million or more.

The exemption would not apply to local sales and use taxes imposed under Chapters 321, 322, or 323, Tax Code, but an exception would be provided for a municipality with a population of 35,000 or less to provide by ordinance that the exemption does apply to taxes imposed by that municipality under Chapter 321.

A registration number would have to be obtained from the Comptroller for each person eligible to claim the exemption and must be stated on the exemption certificate provided by the purchaser to the seller of tangible personal property eligible for the exemption. All registration numbers issued in connection with a qualifying data center would be revocable by the Comptroller upon determination that the requirements for qualification were not met, and each person whose registration number was revoked would be liable for taxes, including penalty and interest from the date of purchase, on purchases for which the person claimed exemption.

Provision would be made for refunds of tax paid by a qualifying owner, operator, or occupant before certification by the Comptroller that a data center is a qualifying data center.

A data center that was certified as a qualifying data center under Section 151.359 during calendar year 2014 would be allowed to elect, on written notice to the Comptroller, to become a certified multi-user data center subject to the provisions of new Section 151.3591. Jobs created and capital investment made prior to September 1, 2015 would be considered in determining whether the data center meets the qualifications for certification as a multi-user data center, and the date on which the data center was certified as a qualifying data center under Section 151.359 would be considered the date of certification as a qualifying multi-user data center under Section 151.3591.

An entity issued a registration number under the new section would not be eligible to receive a limitation on appraised value under Chapter 313, Tax Code.

The bill would take effect September 1, 2015.

Methodology

The LinkedIn Richardson Texas Data Center was certified under Section 151.359 as a qualifying data center on February 20, 2014. Upon its election to be a qualifying multi-user data center under provisions of this bill, it would be subject to the minimum capital investment requirement of $100 million over a 10 year period under Section 151.3591 rather than the minimum of $200 million over a five year period under Section 151.359. To the extent that this qualifying data center may have become subject to registration revocation and liable for taxes for failure to meet the $200 million capital investment requirement under Section 151.359, there would be a reduction in state tax revenue; however, that potential amount cannot be determined.

Because the proposed Section 151.3591 would apply for single-user enterprise data centers as well as multi-tenant data centers and the terms of the proposed section with respect to the standards for qualification are less restrictive than under current law Section 151.359 - the capital investment requirement under the proposed section would be $100 million over 10 years versus $200 million over five years under current law, the job creation requirement would be for five jobs rather than 20, and a single user could qualify space that was already in use as a data center - it is expected that the proposed Section 151.3591 would effectively supersede current Section 151.359 for the qualification of single-user enterprise data centers for exemption. A substantial increase in the volume of data center expenditures that would occur under current law without exemption, whether in an enterprise or multi-tenant configuration, will qualify for exemption from state sales and use tax. The 10 year period provided by the proposed section during which capital investment may serve to qualify a data center for exemption will allow more capital expenditures for server refreshes to count toward the investment requirement, with the result that more facilities with lesser megawatt capacity are likely to qualify than under current law.

Data obtained from industry sources on the composition of data center expenditures on infrastructure and electricity costs, as well as the recent volume of deal activity in the multi-tenant data center market for tenants contracting for one megawatt or more of capacity, was used to model expected annual expenditures by data centers that would be subject to tax under current law but would be exempt under provisions of the bill. The estimate below is based on an assumption of 40 megawatts of new commitments for capacity per year, in both single-user enterprise and multi-tenant configurations, that could meet the $100 million capital investment requirement over a 10 year period subject to the one megawatt minimum capacity requirement.

While it is probable that the exemption policy proposed in this bill would foster more data center development in the state, the incremental state sales tax revenues from the additional centers would be limited for the most part to tax on building materials for the shell and some gains from nonqualifying investment by users below the one megawatt threshold, while there would be significant reductions in state sales tax revenues from expenditures on power and communications equipment, servers, and electricity pursuant to data center demand that would occur without the exemption.

Additional data center development might also result in significant increments to school property tax bases; however, the extent to which that may result in savings to the state in costs for the Foundation School Program is not estimated in this fiscal note and would have to be recognized in the appropriations process.

Local Government Impact

No significant fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: UP, KK, SD