



City of Morgan Hill

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CITY COUNCIL STAFF REPORT

MEETING DATE: JANUARY 18, 2017

PREPARED BY: John Lang, Economic Development Coordinator/Community Development
 APPROVED BY: City Manager

INCENTIVE AGREEMENT WITH MORGAN HILL REAL ESTATE LLC, FOR THE ESTABLISHMENT OF A NEW AUTOMOBILE AGENCY AT THE AUTO MALL PLANNED DEVELOPMENT SITE ON CONDIT ROAD

RECOMMENDATION(S)

Adopt resolution authorizing the City Manager to execute an Incentive Agreement, consistent with the Auto Dealer Economic Development Strategy, with Morgan Hill Real Estate LLC for a new automobile dealership at the Auto Mall Planned Development Site on Condit Road; and make findings of consistency with Section 53083(a)(6)(b) of the Government Code (AB 562).

COUNCIL PRIORITIES, GOALS & STRATEGIES:

Ongoing Priorities

Maintaining fiscal responsibility

2016 Focus Areas

Developing Our Community
 Planning Our Community

REPORT NARRATIVE:

In February of 2002, the City Council authorized an auto dealer assistance program as part of an Auto Dealer Economic Development Strategy. The strategy sought to take a proactive role to identify and entitle appropriate locations for new auto dealerships, as well as marketing and attracting new car sales agencies to the City. A component of the "Strategy" offers auto dealers incentives to locate and or expand in Morgan Hill if it can be demonstrated that there is a need for assistance and a significant benefit to the community. Building partnerships with the private development community has always been at the core of the City's auto strategy to advance development plans.

In 2003, the City utilized this program to provide assistance to the Ford Store. The 2003 agreement with the Ford Store was satisfied in 2013. The Ford Store exceeded all previous sales tax expectations and remains one of Morgan Hill's top sales tax generators. In 2005, Morgan Hill went further to secure the City's future as a regional location for auto dealer sales by adopting a Planned Development Zone, pre-zoning and annexing 19.87 acres of land north of the Ford Store, along Condit Road to plan for future auto users. In 2013, the Ford Store was granted additional assistance to facilitate the acquisition of 2.53 acres to provide for the expansion of the facility. That expansion project was completed in early 2015.

In 2014, the Auto Incentive program was used to aide in the acquisition of land and facilitate the expansion of Honda of Morgan Hill. The incentive agreement is currently in place and Honda has been exceeding estimated sales targets and thus receiving rebates.

In 2016, the City of Morgan Hill began conversations with Morgan Hill Real Estate LLC about the possibility of locating a new Chrysler, Dodge, Jeep or Ram dealership in Morgan Hill. After conducting due diligence on the property adjacent to the Ford Store, Morgan Hill Real Estate LLC has received approval from Chrysler to move forward with a new dealership in Morgan Hill.

Morgan Hill Real Estate LLC is in process to purchase six acres of land, to the north of the Ford Store, from South Valley Mushroom Farm (owned by Omura and Sons) to develop a Chrysler, Dodge, Jeep or Ram branded dealership.

This report requests the authority to execute an incentive agreement with Morgan Hill Real Estate LLC which would rebate up to \$780,000 in sales tax revenue to offset the costs of impact fees, mitigation, habitat conservation fees and offsite improvements for a new automobile agency.

Because auto dealerships require so much land to store, display, and service their products, and purchase inventory and trade-in stock, dealerships outside of huge population centers are very expensive to develop. Impact fees, the lack of improved roads, and agricultural mitigation costs severely restrict the feasibility of this use in Morgan Hill. The City's Auto Dealer Strategy and the partnership it creates, makes the decision to locate in Morgan Hill possible.

New automobile dealerships are economic engines that support and sustain critical city services for years to come. Morgan Hill Real Estate LLC will require an investment of about \$14 million to acquire and develop the site. It is anticipated that 180 new jobs (including construction jobs) will result from the dealership. The estimate for impact fees, HCP fees, and agricultural mitigation is \$780,000.

Consistent with the Auto Dealer Policy, proposed is an incentive agreement that includes:

- Morgan Hill Real Estate LLC would receive up to a maximum of \$780,000 over a ten (10) year period in sales tax rebates. The tax sharing arrangement terminates at the end of ten years

regardless if the maximum of \$780,000 has been paid to the dealer.

- The City would share 50% of the sales tax revenue collected above \$50,000 for the first year of operation based on total taxable sales of \$5 million.
- The City would share 50% of the sales tax revenue collected above \$100,000 for the second year of operations based on total taxable sales of \$10 million.
- The City would share 50% of the sale tax revenue collected above \$200,000 for each year thereafter based on total taxable sales of \$20 million.
- The City would make payments twice a year. If the dealer did not exceed the baseline threshold for a year, it would not receive any payment for the year.
- In exchange for assistance, the dealer agrees to operate an automobile dealership for 20 years. In the event of default, the dealer would be required to reimburse the City per the agreement.

Similar to the transactions crafted for the developments of the Ford Store and Honda of Morgan Hill, and consistent with the Auto Dealer Policy, this incentive program provides a lower baseline amount in the first two years to allow the dealer to build its business. The baseline amount for the subsequent years was first established using average annual sales a dealership of similar brands in Northern California typically produces. The baseline was then modified downward by approximately 50 percent reflecting a conservative approach when anticipating a challenging entry into a strong Chrysler, Dodge, Jeep Ram market in South County and to advance Morgan Hill’s economic development efforts.

The baseline amount can, reward the dealership for being better than average and creates an incentive for the dealer to far exceed \$20 million in sales each year.

Within Santa Clara County, Chrysler, Dodge and Jeep represent about 5 percent of the new car market share. According to the Silicon Valley Auto Dealers, Dodge and Jeep car and light trucks are the preferred brands within the County.

COMMUNITY ENGAGEMENT: Inform

The table below addresses the requirements set forth in the State of California AB 562 (Government Code 53083) for publication of information related to an economic development subsidy and public hearing.

| | |
|--|---|
| Name/address of beneficiary of the subsidy: | Morgan Hill Real Estate LLC 6520 Centennial Center Blvd Las Vegas, NV 89149 |
| Start and end dates, schedule for the subsidy | The incentive agreement will not start any earlier than the first year after full operation. The subsidy will reimburse 50% of the sales tax revenue received by the City of Morgan Hill over an established baseline for the next ten years or until \$780,000 has been paid, whichever comes first. |

| | |
|---|--|
| <p>Describe the subsidy, estimated total amount of expenditure of public funds or revenue lost</p> | <p>The City will reimburse 50% of new sales tax revenue received from the new Chrysler/Dodge dealership over an escalating baseline up to \$780,000 or ten years which ever occurs first. The baseline for year one is \$5 million. The baseline for year two is \$10 million. The baseline for year three through year ten is \$20 million.</p> |
| <p>Statement of public purpose</p> | <p>Expand and enhance economic opportunities for businesses in the City, continue to expand the City's employment base, and continue to generate hereinafter defined Sales Tax that the City can utilize to fund general governmental services such as police, fire, street maintenance, and parks and recreation programs.</p> |
| <p>Projected Tax revenue</p> | <p>It is estimated that the investment into the property will increase property tax revenue received by the City by \$150,000 over 10 years. It is also anticipated that over the 10 years of the agreement the City will conservatively receive approximately \$825,000 in net sales tax revenue. If the dealership performs at the upper range of highest performing Chrysler Dealerships in California, the City of Morgan Hill could receive up to \$1.9 million over ten years.</p> |
| <p>Estimated number of jobs created by the subsidy</p> | <p>It is estimated the dealership will employ between 40-50 employees people when fully operational. Full time and part time occupations will range from managers, mechanics, service technicians, and sales people.</p> |

ALTERNATIVE ACTIONS:

The alternative would be to not consider the agreement. However, the developer may not build which would mean the City would lose the opportunity to generate between \$975,000 and \$2.05 million in new revenue to the General Fund over the course of the next ten years.

PRIOR CITY COUNCIL AND COMMISSION ACTIONS:

City Council and the Planning Commission have not taken any specific action related to this project to date. City Council has approved three incentive agreements under the Auto Dealer Economic Development Strategy.

In March 2004, City Council approved a development agreement with Morgan Hill Land, LLC (dba Ford Store Morgan Hill) to construct a new car dealership.

On September 11 2013, City Council approved an incentive agreement with Morgan Hill Land, LLC for the expansion of the Ford Store Morgan Hill.

On July 2, 2014, City Council approved an incentive agreement with Theodore Stevens Revocable Trust Dated April 24, 2000 and Stavridis, Inc. (dba Honda of Morgan Hill) for the expansion of the Honda of Morgan Hill Store.

FISCAL AND RESOURCE IMPACT:

Over a ten year period, the City may share up to \$780,000 in sales tax revenue with Morgan Hill Real Estate, LLC. Based upon straight line revenue forecasts, the City would net approximately \$825,000 in new sales tax revenue. After 10 years the City would receive the full 1% of sales tax revenue with no additional rebates.

CEQA (California Environmental Quality Act):

Not a Project

This incentive agreement is exempted from environmental review under Section 15061(b)(3) of the State CEQA Guidelines. The incentive agreement is covered by the general rule that CEQA applies only to projects which have the potential for causing a significant effect on the environment. Where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment, the activity is not subject to CEQA. The incentive agreement will not result in any direct impact upon the physical environment. Any development that occurs in the future will be subject to development standards of the zone district and will undergo an independent analysis pursuant to the requirements of CEQA.

LINKS/ATTACHMENTS:

Exhibit A: Resolution

Exhibit B: Incentive Agreement