



January 19, 2016

Mr. Greg Blodgett
Senior Project Manager
Ms. Grace Lee
Sr. Economic Development Specialist
City of Garden Grove | Economic Development Division
11222 Acacia Parkway
Garden Grove, CA 92840

RE: AAA Oil, Inc. (Dba California Fuels and Lubricants)
AB 562 - Economic Development Strategy
Job Retention, Capital Investment and Sales Tax Sharing

Dear Mr. Blodgett and Ms. Lee:

The City of Garden Grove (City) has commissioned Tierra West Advisors, Inc. (Tierra West) to mediate, review, analyze and prepare a report pertaining to an Amended and Restated Operating Covenant Agreement, between the City and AAA Oil, Inc. Dba California Fuels and Lubricants (CFL). The Amended and Restated Operating Covenant Agreement and terms are based upon the City's economic development strategy and in compliance with the newly enacted public reporting requirements of Assembly Bill 562 (AB 562)The State Legislature and Governor Brown, due to the elimination of Redevelopment addressed the loud outcry by cities, counties and communities for the need to legislatively assist local agencies, as well as the State, to encourage employment, retain jobs and companies in local communities. The loss of redevelopment has left the City of Garden Grove with a loss of local resources to encourage economic development. In response to this financial loss, the City of Garden Grove is developing an economic development strategy and considering an economic development subsidy that will comply with the continued public reporting provisions mandated by AB 562.

CFL, located in Garden Grove, is proposing to maintain its primary office location within the City for the next 20 years and four (4) months maintain the City as the Point of Sales for all

2616 East 3rd Street
Los Angeles California 90033
T 323/265 4400
F 323/261 8676
W tierrawestadvisors.com

REAL ESTATE & DEVELOPMENT
STRATEGISTS

taxable sales. In order to remain competitive and promote expansion, CFL and the City are proposing to enter into the Amended and Restated Operating Covenant Agreement which includes a revenue sharing and capital investment arrangement as part of the City's Economic Development Program.

The Amended and Restated Operating Covenant Agreement is intended to provide CFL and the City the ability to address among others:

- Decline in competitiveness due to industry consolidation
- Update the existing Operating Covenant Agreement
- Extend CFL's operations in the City
- Retain City General Fund revenues to provide needed services for residents
- Retain and capture future growth in CFL product sales (leveraging on estimated future revenue and industry price increases) Increase the economic competitiveness of Garden Grove
- Increase the City's wealth and prosperity
- Diversify the City's economic base and wage levels
- Outreach and support to existing businesses
- Maintain and enhance a consistent, business-friendly environment
- Expand public-private partnership opportunities

Tierra West recognizes that the provisions of the Amended and Restated Operating Covenant Agreement and retention of CFL would not only assist CFL but also provide a strong public purpose through the City's continued expansion of economic development opportunities for businesses within the City. Simultaneously, retention of CFL in the City, will provide continued growth of the City's General Fund revenue and tax base and improve economic and physical conditions and services in the City.

Sincerely,
TIERRA WEST ADVISORS, INC.


John N. Yonai

City of Garden Grove
Economic Development (AB562)
Amended and Restated Operating Covenant Agreement
between
City of Garden Grove
and
AAA Oil, Inc.
dba California Fuels and Lubricants

The City of Garden Grove (City) in order to maintain sustainable economic development, community vitality and recovery from the annual loss of over \$5 million previously received by the City's Redevelopment Agency, is implementing economic development strategies that include the application of Assembly Bill (AB) 562. The City and AAA Oil, Inc., dba California Fuels and Lubricants, (CFL) propose to enter into an Amended and Restated Operating Covenant Agreement. The Amended and Restated Operating Covenant Agreement requires CFL to remain in operation in the City and the City will continue to provide revenue sharing with CFL.

The loss of redevelopment has left the City of Garden Grove as well as all cities Statewide with a loss of local resources to encourage economic development and maintain local services. The California Legislature and Governor Brown made the decision to terminate redevelopment and removed the single largest economic tool available to local agencies. Based upon the decision to terminate redevelopment statewide, the Governor and Legislature recognized the necessity of cities, counties and the State, to encourage employment and retain jobs and companies by giving economic subsidies to businesses and the importance of providing public input by requiring:

1. A public hearing prior to the granting of the subsidy
2. A report regarding the subsidy within the term
3. Where a subsidy has a term of more than 10 years, an additional public hearing at the conclusion of the subsidy.

The State approved AB 562, which went into effect on January 1, 2014, codifying a continued public reporting requirement for economic development subsidies.

This report includes the information required by AB 562 and the fiscal analysis necessary to determine the projected revenue generated by CFL to the City as part of the economic development strategy for business retention through an Amended and Restated Operating Covenant Agreement. The City provided information which was utilized to establish an estimated "Revenue Tax Base" of sales tax collected by the City from CFL. After the Revenue Tax Base was determined, projections of additional revenue generation from sales tax collections directly attributable to the business were developed. The projected revenue tax increase from CFL represents new resources as well as the retention of a portion of existing general fund revenues to the City of which a percentage of the revenue collected will be shared with CFL. This will avoid significant fiscal impacts to City revenues and community services.

AB562 requires a statement of public purpose for the economic development subsidies which can be satisfied by showing how the public is benefited at large with the proposed business retention. Community-wide benefits can be readily shown by the retention of revenues that will be used to provide municipal services. The City Council may choose to approve the Amended and Restated Operating Covenant Agreement in order to retain and expand jobs, maintain a local business, assist CFL to gain competitiveness within the fuel provision industry and incentivize the business owner to consider and complete upgrades and improvements. This report identifies the financial data necessary to allow the City Council to determine the value of entering into the proposed Amended and Restated Operating Covenant Agreement.

AB 562 Reporting Requirements

On and after January 1, 2014, each local agency shall, before approving any economic development subsidy within its jurisdiction, provide all of the following information in written form available to the public, and through its Internet Web site, if applicable:

1. The name and address of all corporations or any other business entities, except for sole proprietorships, that are the beneficiary of the economic development subsidy, if applicable.

AAA Oil, Inc., dba California Fuels & Lubricants – 11621 Westminster Ave, Garden Grove, CA 92843

Founded in 2004, AAA Oil, Inc., dba California Fuels and Lubricants, (CFL) is a state provider of competitively priced energy products and services. CFL delivers high-quality name brand petroleum products including but not limited to clear and dyed diesel, gasoline, all variety of lubricants, greases, DEF, propane, CNG, and LPG. CFL operates its own fleet of vehicles and provides 24/7 emergency services, fuel and lube inventory management, remote tank monitoring with a fully integrated fuel management system/fuel monitoring and tank rentals and sales. Certifications include Supplier Clearing House: Minority Business Enterprise (MBE) CPUC VON: 11090024 and National Minority Supplier Development Council (NMSDC) #SC05132.

Refined Petroleum Industry

The refined petroleum products market in the US grew 22 percent between 2006-2012 despite a sharp decline in consumption and price during the economic downturn. The local refined petroleum products industry followed similar trends, growing by an average of 6 percent per year during the 2006-2012 review period. The US refined petroleum products industry became more export-oriented with the share of exports increasing from 6 percent in 2006 to 16 percent in 2012. Strong growth is forecast for the industry as high prices and recovering volume demand will propel revenues.

2. The start and end dates and schedule, if applicable, for the economic development subsidy.

The Amended and Restated Operating Covenant, if approved, is for twenty (20) years and (4) months commencing on March 1, 2016 and ending on June 30, 2036.

Sales Tax Generation

The Bradley Burns Uniform Local Sales and Use Tax (“Bradley Burns”) applies to the sales of tangible personal property in which a percentage of California’s sales and use tax rate is distributed back to the jurisdiction where sales were generated to support local general funds. For many jurisdictions, including the City, this amount is one percent (1%). Sales tax is payable to the City from the State Board of Equalization. The calculations in this report indicate only the estimated amount of sales tax to be received by the City through the distribution formula used by the State Board of Equalization. CFL proposes to maintain and enhance existing business operations in the City. The City and CFL mutually agreed that a Sales Tax Base would be set at \$200,000 annually. Payment will be made quarterly with \$50, 000 per quarter set as the base to offset and minimize any potential decline in current general fund revenue. Therefore, the City would receive the first \$50, 000 in a quarter and revenue sharing would commence on any sales tax generated by CFL above this amount. The Annual base remains at \$200,000

Sales projections were developed based upon review of retail sales data between the years of 2011 through 2015. According to the historical sales data, CFL generated on average of \$6.93 million in revenue per quarter or \$27.72 million annually. 2014 and 2015 data indicated steady growth in revenue with an average of \$9.13 million in sales per quarter or \$36.5 million per year.

The City and CFL previously entered into an Operating Covenant Agreement in August 2013, which provides for the City to rebate to CFL 50% of the incremental additional sales tax revenue generated by CFL above the amount of sales tax revenues generated in the Fiscal Year 2012-2013 base year, for a period of 10 years (through June 20, 2023), up to an aggregate maximum of \$2,000,000 with the remaining 50% of the incremental additional sales tax revenue retained by the City. The existing Operating Covenant Agreement also calls for a minimum of \$2,000,000 capital investment by CFL in the business. Under the current Operating Covenant Agreement, CFL has already exceeded the \$2,000,000 capital investments. In addition, the City has received 99.99% of the sales tax revenue while CFL has received less than 0.01%.

3. A description of the economic development subsidy, including the estimated total amount of the expenditure of public funds by, or of revenue lost to, the local agency as a result of the economic development subsidy.

Economic Development Strategy Implementation and Business Retention

In furtherance of the City's economic development strategies, a revenue sharing agreement in the form of the Amended and Restated Operating Covenant Agreement is being proposed. Pursuant to AB562, the revenue sharing Amended and Restated Operating Covenant Agreement is defined as an Economic Development Subsidy that is an expenditure of public funds or loss of revenue to a local agency in the amount of one hundred thousand dollars (\$100,000) or more, for the purpose of stimulating economic development within the jurisdiction of a local agency, including, but not limited to, bonds, grants, loans, loan guarantees, enterprise zone or empowerment zone incentives, fee waivers, land price subsidies, matching funds, tax abatements, tax exemptions, and tax credits. The Economic Development Subsidy shall not include expenditures of public funds by, or loss of revenue to, the local agency for the purpose of providing housing affordable to persons and families of low or moderate income, as defined in Section 50093 of the Health and Safety Code. The City and CFL are currently in a revenue sharing agreement which the parties propose to amend and extend. The current Operating Covenant Agreement term began in July of 2013; the Amended and Restated Operating Covenant Agreement term will extend the current Operating Covenant Agreement by 20 years and four (4) months from March 1, 2016 and expiring on June 30, 2036.

The City is being proactive in retaining CFL as one of the major contributors to the City's general fund. The City's economic development strategies recognize the vulnerable economic recovery the Nation and City are experiencing. The potential relocation of CFL and total loss of revenue would be much more detrimental and undermine the City's delicate economic recovery and cause significant impact to its services. The City is making a significant commitment to maintain the economic momentum it has gained over the past 12 months.

The City and CFL propose to enter into an Amended and Restated Operating Covenant Agreement that would extend the commitment by CFL to remain in the City for twenty (20) years and four (4) months. The Amended and Restated Operating Covenant Agreement provides for a sales tax sharing structure that would provide CFL with up to seventy (70) percent of the sales tax revenue generated by CFL above sales tax in excess of \$200,000 generated annually, with payments distributed quarterly that are in excess of \$50,000 per quarter not to exceed two million dollars (\$2,000,000) and the City receives up to thirty (30) percent of the revenue between \$200,000 and \$2,000,000 in addition to the first \$200,000 of annual revenue which shall be paid quarterly in excess of the \$50,000. It is estimated that the Amended and Restated Operating Covenant Agreement will provide CFL with approximately \$6.6 million and the City \$6.9 million over a twenty (20) year and four (4) month period.

- The City base revenue receipts is reset to \$200,000 annually or \$50,000 quarterly

- City retains the first \$200,000 of sales tax collected annually which is accounted for in quarterly sales tax amounts of \$50,000 before sales tax sharing reimbursements commence to CFL.
- This allows the City to gradually adjust to the new terms and financial impact.
- City and CFL sharing of revenue in the Amended and Restated Operating Covenant Agreement includes the following structure:
 1. 30/70 from \$200,001 to \$2,000,000
 2. 40/60 from \$2,000,001 to \$3,000,000
 3. 50/50 from \$3,000,001 to 5,000,000
 4. 45/55 from \$5,000,001 to \$7,000,000
 5. 35/65 from \$7,000,001 and up.

In addition to the Amended and Restated Operating Covenant Agreement addressing Sales Tax sharing between the parties, CFL commits to investing \$8 million in capital assets between 2015 and 2024 as part of its growth plans within the City. CFL has already committed \$3.368 million to capital investment in 2015 as part of this Amended and Restated Operating Covenant Agreement.

4. A statement of the public purposes for the economic development subsidy.

Public Purpose

Review of the Amended and Restated Operating Covenant Agreement and proposed revenue sharing between CFL and the City is consistent with the City’s economic goals and strategies and is in the best interest of the general public.

Economic goals and strategies include the following:

- Increase the economic competitiveness of Garden Grove
- Increase the City’s wealth and prosperity
- Maximize public revenues and economic development financing options
- Diversify the City’s economic base and wage levels
- Outreach and support to existing businesses
- Maintain and enhancing a consistent, business-friendly environment
- Expand public-private partnership opportunities
- Maintain current and provide future City public Services, capital projects and maintenance

The loss of redevelopment has had significant fiscal impact on City revenues as a result of eliminating the primary local economic tool. Retaining CFL’s business operations in the City would address the need and desire to maintain revenue streams such as property and sales tax to the City. Additionally, CFL’s continued presence in the City would assist in maintaining relative balance in the local economy through indirect retail sales and employment from other local businesses that are supported by CFL’s location in the City.

The Amended and Restated Operating Agreement assists CFL in the following areas:

- Decline in competitiveness due to industry consolidation



- Update current Operating Covenant Tax Sharing Agreement Terms to allow CFL to remain competitive
- Early capture of future growth in product sales (leveraging on estimated future revenue or industry price increases)

CFL has identified multiple instances where larger competitors, created by significant consolidation of operators in the industry, have prevailed over CFL by providing prices at significantly lower than CFL product costs. In recent months there have been a number of smaller firms that have been purchased by larger companies. These acquisitions have made it difficult for many of the remaining smaller operations to submit competitive price quotes for new business contracts. Larger companies are positioned to offer lower bid prices, thus creating a challenging environment for operations similar to CFL to remain viable.

CFL and the City concur that the current Operating Covenant Agreement between the City and CFL is not reflective of the current industry standards or requirements for competitiveness. Tierra West has reviewed comparable agreements between companies and communities and noted substantial support for revenue sharing agreements of 65 percent and above. CFL, as well as, overall industry forecasts project significant growth in sales revenue over the next five (5) and ten (10) years. City staff and CFL agree that early capture or the ability of CFL to accelerate increases in revenue through the proposed Amended and Restated Operating Covenant Agreement will allow it to be more competitive with contract pricing and operations.

5. Projected tax revenue to the local agency as a result of the economic development subsidy.

Based upon the proposed Amended and Restated Operating Covenant Agreement, it is estimated that the City will receive \$3.1 million during the first ten (10) years of the Amended and Restated Operating Covenant Agreement and \$6.9 million over the course of the full term of the twenty (20) year and four (4) month Amended and Restated Operating Covenant Agreement.

6. Estimated number of jobs created by the economic development subsidy, broken down by full-time, part-time, and temporary positions.

AAA Oil, Inc., dba California Fuels and Lubricants (CFL), was founded in Garden Grove September 2004 with only 2 employees. Today they employ 44 people and are one of the City's top ten (10) highest sales tax producers.

CFL projects the addition of approximately 130 to 235 new jobs over a period of twenty (20) years and four (4) months. New jobs will include drivers, dispatchers, logistics office staff, accounting and IT positions. Job growth as proposed at this facility will be constant each year at a rate of change/growth that ranges from 12.5% in its lowest year of 2014 to 44.4% in the highest growth year of 2017. Notable growth in employment opportunities in the initial years and constant job growth throughout the twenty (20) year four (4) month period is consistent with the capital investment proposed by CFL.

Summary

AAA Oil, Inc., dba California Fuels and Lubricants (CFL) and the City have agreed that CFL remaining in Garden Grove is beneficial for both parties. The City has proposed that CFL agree to an Amended Operating Covenant Agreement to remain in Garden Grove for the next twenty (20) years. CFL and the City have mutually agreed to a revenue sharing structure and capital investment plan in exchange for the Amended and Restated Operating Covenant Agreement. The Amended and Restated Operating Covenant Agreement provides CFL a more competitive advantage in an industry that is consolidating and extremely competitive for smaller firms. The Amended and Restated Operating Covenant Agreement is the economic development subsidy that is consistent with the City's economic development implementation strategy and as prescribed in AB 562.

Assistance is provided in the form of a revenue sharing Amended and Restated Operating Covenant Agreement between CFL and the City. The Amended and Restated Operating Covenant Agreement provides for CFL receiving 50.0% to 70.0% of the sales tax revenue generated by CFL's sales operation with the balance of 30.0% to 50.0% remaining with the City. The proposed Amended and Restated Operating Covenant Agreement is for twenty (20) years and four (4) months. The estimated amount of the total subsidy or expenditure of public funds would be \$6.6 million over a twenty (20) year four (4) month period.

Based upon review of the Amended and Restated Operating Covenant Agreement, the structure is consistent with the City's economic goals and an implementation strategy is in the best interest of the general public. The Amended and Restated Operating Covenant Agreement and projections indicate the City will receive approximately \$6.9 million in sales tax revenue during the twenty (20) year four (4) month Amended and Restated Operating Covenant Agreement.

The Amended and Restated Operating Covenant Agreement serves a valid public purpose through the expansion of economic development opportunities for businesses in the City, continuing to expand the City's employment base, increasing capital investment in the CFL, increasing the property and personal property tax base, and continuing to generate sales tax revenue that the City utilizes to fund general governmental services for businesses and residents.

Recommendation

Retention of CFL in the City will continue to contribute to the economic vitality of the City, provide additional jobs within the City, expand the City's tax base and improve economic and physical conditions in the City. Loss or relocation of CFL out of the City will impact a vulnerable economic recovery and momentum that the City is achieving and reduce City services. As such, it is recommended that the Amended and Restated Operating Covenant Agreement be approved.

By its approval of the Amended and Restated Operating Covenant , the City Council of the City of Garden Grove finds and determines that the Amended and Restated Operating Covenant Agreement serves a valid public purpose through continuing to expand economic opportunities for businesses in the City, continuing to expand the City's employment base, and continuing to generate Sales Tax that the City will utilize to fund general governmental services such as police, fire, street maintenance, and parks and recreation programs.