

MEMORANDUM

To: Ellen Clark, Senior Planner
CC: Steven Hakim
From: Walter Kieser and Ashleigh Kanat
Subject: Mammoth Creek Inn Feasibility Evaluation; EPS #121131
Date: December 10, 2012

The Economics of Land Use



Mammoth Creek Inn is a 26-room hotel in the Town of Mammoth Lakes that is proposing to expand its room inventory by 12 rooms. The 12 rooms consist of 6 x 1-bedroom rooms and 3 x 2-bedroom rooms (per the Town's interpretation of a "room"). This proposed expansion exceeds the Town's maximum density allowance of 40 rooms per acre by seven rooms. The property owner is, therefore, requesting a density bonus, which triggers the requirements of the Town's Community Benefits/Incentive Zoning (CBIZ) policy.

Economic & Planning Systems, Inc. (EPS) was asked to review the financial analysis prepared by the property owner and to assist in evaluating the feasibility and value of the expansion. In this analysis, EPS is focused on estimating the value conferred by the seven rooms that exceed the base density allowance, rather than the full 12 rooms that are proposed. This memorandum is intended to communicate our independent assessment of the financial feasibility of the expansion and provide an estimate of the value of the density bonus request, which can then be used as the basis for negotiating the appropriate level of Community Benefits the property owner will be asked to provide.

Methodology and Approach

EPS's evaluation is based on an independent review, assessment, and adjustments to the property owner's pro forma analysis and related assumptions. The review uses price points and revenue and expense assumptions in the pro forma that are consistent with industry standards, EPS's experience with similar projects and pro forma analysis, and our knowledge of the current market conditions and trends in the Mammoth Lakes area. The results of our review are displayed on **Tables 1** through **6** which summarize the project description, provide revenue and development cost assumptions, reveal estimated net financial returns and estimate fiscal benefits. It should be noted that EPS has not conducted an independent, detailed market analysis of the pricing assumptions used.

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Project Feasibility

It is our opinion that the Mammoth Creek Inn expansion represents a feasible development opportunity with a projected return to the property owner of 10 percent (cash-on-cash). Though the net return is positive, it is at the low end of such industry-standard returns.

The limited financial return of the Mammoth Creek Inn expansion project is not surprising as most standard hotel projects in resort settings require private sector cross-subsidies (e.g., condo sales) or public assistance of one form or another to be financially feasible. This project is feasible because the property owner already owns the land and is expanding an already existing operation. Moreover, this result is consistent with the general observation that standard hotel developments typically generate lower land value per acre (residual value) than other types of development (e.g., residential) but have similar or even higher development costs.

There has been some discussion about the proposed new units being built as condominium units, wherein the property owner would develop the Project and operate the units as lodging units as proposed but then have the option to sell the units, rather than to continue renting them as hotel rooms. If the units were to be sold post-construction, it would have some effect on the financial performance of the Project as it would alter key assumptions (e.g., financing, sales values). However, the property owner has indicated that he would not sell the units for several years or until the condominium market has improved further, which results in no significant change to the development economics estimated in this analysis. There could be a change to the fiscal benefits to the Town insofar as the new units would no longer be in the rental pool.

Fiscal Benefits

Fiscal benefits are a key public benefit of the proposed project. EPS estimates that this project (the seven rooms) will generate approximately \$25,000 in transient occupancy taxes (TOT) per year, once the project achieves a stabilized occupancy rate. If the new units are sold as condominium units, it would reduce their use as rental units and a proportionate reduction in TOT would occur. Additional property taxes will be approximately \$722 per year, and utility taxes are estimated to be approximately \$8,000 per year. The full 12-room project will generate proportionately more. Though sales taxes resulting from the additional visitor-days in Mammoth Lakes are not estimated, visitor spending will generate sales tax revenues to the Town from food, beverage, and other retail sales.

In addition to the positive tax flows that the project will generate, the merit of the proposed project lies in its furtherance of the Town's General Plan objectives, which include providing a diversity of lodging types, remaining competitive, and achieving its full market potential as a destination resort. To do so, the Town must upgrade and expand its lodging sector, as Mammoth Creek Inn is proposing.

Community Benefits

In its September 27, 2012 memo to the property owner's architect, the Town noted several potential Community Benefits that would be acceptable in exchange for the density bonus that is being sought. Of the Community Benefits listed, it is our understanding that the property owner is most interested in helping to fund a new or improved transit facility, such as a bus stop/shelter along Old Mammoth Road in the vicinity of the Project.

The precise level of Community Benefits that the property owner should be expected to contribute will need to be negotiated between the property owner and the Town. However, in EPS's opinion, the 10 percent return to the property owner that our pro forma yields is at the low end of generally acceptable rates of return, and there does not appear to be sufficient margin to request Community Benefits exceeding five percent of the net return shown for this project (approximately \$6,000). It should be noted that the amount of Community Benefits being requested of the property owner are *in addition to* the fiscal and economic benefits the Town will realize from granting this density bonus to the Mammoth Creek Inn.

Table 1
Mammoth Creek Inn Project Parameters
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Amount
Parcel Size	33,976.80 sq.ft.
(in Acres)	0.78 acres
Existing Number of Rooms	26.00 rooms
Existing Density	33.33 rooms/acre
Proposed New Rooms	12.00 rooms
Proposed Total Rooms	38.00 rooms
Proposed Total Density	48.72 rooms/acre
(Rounded)	49.00 rooms/acre
Base Density Allowed	40.00 rooms/acre
Base Number of Rooms Allowed	31.20 rooms
Room Increase (above Base)	6.80 rooms
(Rounded)	7.00 rooms
Density Increase (above Base)	22.50%

Sources: Mammoth Creek Inn; Town of Mammoth Lakes; Economic & Planning Systems, Inc.

Table 2
Average Room Revenue Calculation
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Amount
Hotel Expansion	
1-Bedroom Rooms	6.0
Average Daily Room Rate [1]	\$150
Average Occupancy Rate	60%
Annual Room Rental Revenue	\$197,100
2-Bedroom Rooms	3.0
Average Daily Room Rate [1]	\$250
Average Occupancy Rate	50%
Annual Room Rental Revenue	\$136,875
Total	\$333,975
Number of "Rooms" per Town Definition	12.0
Average Annual Per Room Rental Revenue	\$27,831

[1] Room rates do not include Transient Occupancy Tax.

Sources: Mammoth Creek Inn; Economic & Planning Systems, Inc.

Table 3
Pro Forma (in 2012 dollars)
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Assumption	1st Year of Stabilized Operations
Hotel Expansion		
Number of Rooms [1]		7.0
Annual Room Rental Revenue	\$27,831	\$194,819
(less) Expenses [2]	\$8,000	<u>\$56,000</u>
Hotel, Annual Net Revenue		\$138,819
Other Income [3]		\$0
Gross Operating Revenue		\$194,819
NOI Before Overhead and Fixed Expenses		\$138,819
Variable Overhead Expenses [4]		
Administration & General	9.5%	\$18,508
Sales & Marketing	2.4%	\$4,676
Property Operation and Maintenance	5.6%	<u>\$10,910</u>
Total, Variable Overhead Expenses	17.5%	\$34,093
NOI Before Fixed Expenses		\$104,725
Fixed Charges and Other Expenses [5]		
Additional Property Taxes		\$12,040
Net Operating Income		\$92,685
Capitalized Value of Hotel Expansion [6]	7.0%	\$1,324,078

[1] Analysis is based on seven rooms - the difference between the number of rooms proposed (38) and the allowable number of rooms under the base density allowance (31.2, rounded down to 31).

[2] Expense is per room and provided by owner based on actual operations. Expenses include food (complementary morning breakfast, utilities and housekeeping - labor).

[3] Other income includes pet fees, movie fees, and mini-bar snacks and beverages. Revenue from these items is factored into the daily room rate estimate.

[4] Variable Overhead Expenses are based on assumptions EPS has used in previous hotel feasibility analyses for the Town of Mammoth Lakes with reference to PKF reported industry norms.

[5] With the exception of property taxes, fixed charges (e.g., snow removal, etc.) are not expected to change significantly with the addition of seven new rooms.

[6] The capitalization rate of 7.0% is based on sales that the owner is familiar with as well as prior EPS experience in the Town of Mammoth Lakes.

Sources: Mammoth Creek Inn; PKF Hospitality Research Consulting TRENDS, 2006; Economic & Planning Systems, Inc.

Table 4
Summary of Development Costs
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Development Costs	Per Room Costs	Per Room Costs Applied to Rooms Requiring Density Bonus [1]
Site and Due Diligence [2]	\$0	\$0	\$0
Construction Hard Costs [3]	\$1,560,000	\$130,000	\$910,000
Permitting and Professional Fees	\$108,000	\$9,000	\$63,000
Hotel FF&E	\$156,000	\$13,000	\$91,000
Striping and Surface Parking	\$60,000	\$5,000	\$35,000
Under Structure Parking Area	\$180,000	\$15,000	\$105,000
Total Project Costs	\$2,064,000	\$172,000	\$1,204,000

[1] Applied to 7 rooms.

[2] No land acquisition costs associated with this Project.

[3] EPS adjustment reflects a per square foot cost of \$130. This estimate is lower than what EPS has seen in Mammoth Lakes because owner is able to provide "in-house" general contracting.

Source: Mammoth Creek Inn; Economic & Planning Systems, Inc.

Table 5
Net Return Analysis
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Amount
Capitalized Value of Hotel Expansion Project [1]	\$1,324,078
Less Total Development Costs [2]	\$1,204,000
Net Return	\$120,078
per room [3]	\$17,154
per sq.ft. [4]	\$60.04
as a % of Project Cost [5]	10.0%

[1] Based on increase above base allowable density. Assumes a 7.0% cap rate.

[2] See Table 4.

[3] Assumes 7 rooms.

[4] Assumes 7,000 developable square feet.

[5] Profit as a percentage of project cost typically ranges from 12 to 20 percent depending on the risk associated with the investment. Though for a project that proposes to expand an existing property, the risk is reduced and a lower rate of return may be acceptable.

Sources: Mammoth Creek Inn; Economic & Planning Systems, Inc.

Table 6
Estimate of Annual Tax Revenues to the TOML [1]
Mammoth Creek Inn CBIZ Evaluation; EPS #121131

Item	Amount
Transient Occupancy Tax	
Room Revenue	\$194,819
TOT (at 13%)	\$25,326
Total, Transient Occupancy Tax	\$25,326
Property Tax	
Project Cost (Expansion Only)	\$1,204,000
Property Tax (at 1.0%)	\$12,040
Town Share (6% of 1%)	\$722
Total, Property Tax	\$722
Utility Tax	
Utilities [1]	\$321,015
Utility Tax (at 2.5%)	\$8,025
Total, Utility Tax	\$8,025
Total TOML Tax Revenue	\$34,074

[1] Each room is assumed to generate annual utility bills of \$1,500. Estimate based on prior work in the Town of Mammoth Lakes.

Sources: Economic & Planning Systems, Inc.