



## Agenda Report

20-1394

Agenda Date: 2/11/2020

### REPORT TO COUNCIL

#### SUBJECT

Discussion and Direction on the Santa Clara Tourism Improvement District (TID) Assessment Formula and Transient Occupancy Tax [Council Pillar: Promote and Enhance Economic and Housing Development]

#### BACKGROUND

A base transient occupancy tax (TOT) is charged to hotel guests when they rent accommodations in a lodging business for a period of less than 30 days. Currently, Santa Clara's base TOT rate is set at 9.5% and as a part of the City's future financial planning, it was identified that increasing the City's TOT rate could be one potential revenue enhancement area Council may wish to consider. A separate report on the February 11, 2020 Council agenda discusses the City's overall fiscal outlook and potential revenue areas.

On November 12, 2019, staff presented City Council with the Santa Clara Tourism Improvement District's (TID) request to establish the TID under the Property and Business Improvement District Law of 1994 and proposed to change the district assessment from \$1.00 per occupied room night to 2% of gross revenue (RTC 19-920). A policy consideration on the conversion of the TID formula is the overall transient occupancy tax (TOT) being charged. As an increase in the base TOT is being considered, Council approved to move forward with the establishment of the new district under the 1994 Law and requested additional comparative data on cities with similar districts and overall TOT.

This report provides information as requested by Council and other options for the TID assessment.

#### DISCUSSION

The lodging businesses within the current TID area collect a \$1.00 per occupied room night fee from hotel/motel guests. This is the same assessment formula that has been used since the TID was formed in January 2005. The lodging businesses in the TID have proposed a change the district assessment to 2% of gross revenue of short-term rentals. As the 11 TID hotels (AC Hotel Santa Clara, Avatar Hotel, Biltmore Hotel & Suites, Element Santa Clara, Embassy Suites, Hilton Santa Clara, Hyatt House, Hyatt Regency, Marriott Santa Clara, the Plaza Suites, and TownePlace Suites by Marriott), are also part of the Stadium Community Facility District (CFD), visitors who stay at a hotel in the TID area are subject to a CFD special tax of 2% of gross room revenue in addition to the \$1.00 fee and the City's base TOT rate of 9.5%. Santa Clara's base TOT plus the CFD special tax places Santa Clara's overall tax and assessment rate at 11.5%.

Based on the proposed levy for the TID of 2%, the overall tax and assessment rates would increase to 13.5% and a potential increase in the base TOT would bring Santa Clara's overall rate on par with Palo Alto's base TOT rate of 15.5% as well as many other destinations regionally and nationally.

**Table 1 - Transient Occupancy Tax by City**

City	Rate
Gilroy	9.0%
<b>Santa Clara (w/o CFD)</b>	<b>9.5%</b>
Saratoga	10.0%
Fremont	10.0%
Mountain View	10.0%
San Jose	10.0%
Morgan Hill	11.0%
Los Altos	12.0%
Campbell	12.0%
Cupertino	12.0%
Los Gatos	12.0%
Sunnyvale	12.5%
Milpitas	14.0%
Palo Alto	15.5%

**Santa Clara TID Compared to Other Local Districts**

Table 1 references the TOT rate by City previously presented to Council. The rates in Table 1 only represents the base TOT and is not reflective of the total taxes and fees paid by travelers to these cities. Of the cities listed, Saratoga, Mountain View, Los Altos, Campbell, Cupertino, Los Gatos, Sunnyvale, Milpitas do not have tourism improvement districts. Staff research discovered that Palo Alto along with several cities along the Peninsula, assess a tourism fee as part of the San Mateo County Tourism Business Improvement District. The assessment is \$0.15 to \$1.00 per occupied room night based on the projected occupancy of each hotel (smaller hotels with limited services and meeting space with lower occupancy pay less than larger, full-service hotels).

Table 2 compares Santa Clara's base TOT and proposed district assessment with Palo Alto and nine other cities in the region with similar districts. When looking at the base TOT rates only, Tri-Valley (8%) and Gilroy (9%) TOT rates are lower than Santa Clara, and Morgan Hill (11%), Richmond (10%), Concord (10%), San Jose (10%), Berkeley (12%), Oakland (14%), San Francisco (14%) and Palo Alto (15.5%) have TOT rates set higher than Santa Clara, with Palo Alto at the highest.

As a potential future increase to Santa Clara's base TOT is being considered as a City revenue source and yet to be determined, an additional 2% was used in the tables for comparison purposes and is highlighted in yellow.

**Table 2 - Comparison with Similar Assessment Districts**

District	Base TOT	District Assessment	Other Tax/ Assessment	Total on \$100 Room Rate
Tri-Valley <sup>(a)</sup>	8%	\$2.00	-	\$10.00
Gilroy	9%	2%	-	\$11.00
Richmond	10%	\$2.00-\$2.50	-	\$12-\$12.50
Morgan Hill	11%	1.5%	-	\$12.50
Santa Clara <sup>(current)</sup>	9.5%	\$1.00	2%	\$12.50
Berkeley	12%	1%	-	\$13.00
Concord	10%	3%	-	\$13.00
Santa Clara <sup>(proposed)</sup>	9.5%	2%	2%	\$13.50
Santa Clara <sup>(w/ potential TOT increase)</sup>	11.5%	2%	2%	\$15.50
Oakland	14%	\$1.50	-	\$15.50
Palo Alto <sup>(b)</sup>	15.5%	\$0.15-\$1.00	-	\$15.65-\$16.50
San Jose	10%	\$1.00-\$3.00	4%	\$15-\$17
San Francisco	14%	1.0625%-2.25%	0.3125%-1.25%	\$15.38-\$17.50

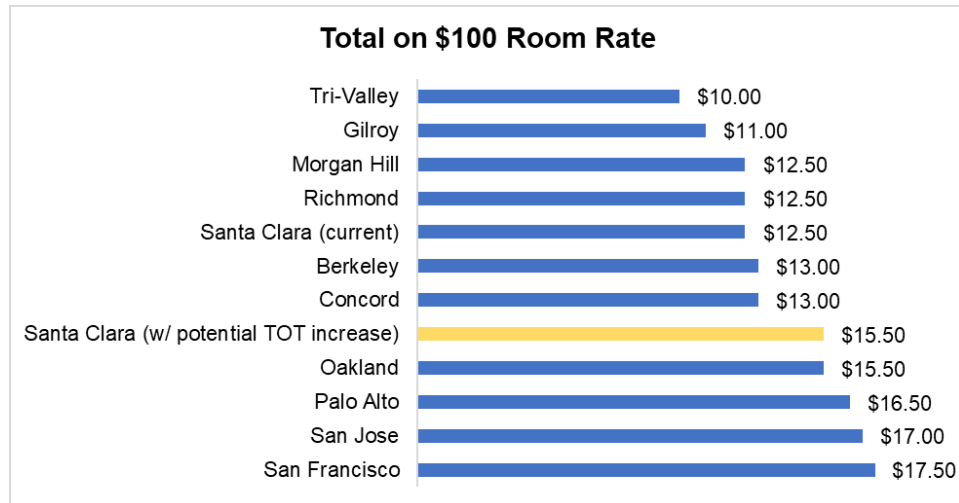
(a) Cities of Dublin, Livermore, Pleasanton and San Ramon, and town of Danville

(b) Of these fees collected by the TBID for visitor services and marketing, approximately 10% is transferred to the Palo Alto Commerce to support local visitor's bureau functions.

As shown in Table 2, the district assessments among these cities vary; half charge a fee and half charge a percentage and some cities charge an additional tax/assessment. San Jose assesses a 4% Convention Center Facilities District Tax and San Francisco assesses 0.3125%-1.25% for the Moscone Expansion District. Due to the differences in assessment methods, rather than evaluating based on overall TOT rate, the total cost on a \$100 room rate is calculated to provide a dollar for dollar comparison. This is the most accurate approach to assessing how much a traveler will ultimately pay in Santa Clara compared to others.

The last column on the right --Total on \$100 Room Rate-- shows that guests staying at a hotel in the Santa Clara TID currently pays \$12.50 on every \$100 room rate. This puts Santa Clara in the lower to mid-range of total "out-the-door" fees. The proposed 2% TID assessment would increase the total cost to \$13.50 on every \$100 and a potential 2% or 3% increase in the base TOT would bring the total fee to \$15.50 or \$16.50 on every \$100. Even with both changes, Santa Clara's out-the-door fees would still be on par with Palo Alto and less than San Jose and San Francisco. Graph 1 provides a snapshot comparison of "out-the-door" fees.

### Graph 1 - Comparison to Other Cities in the Region

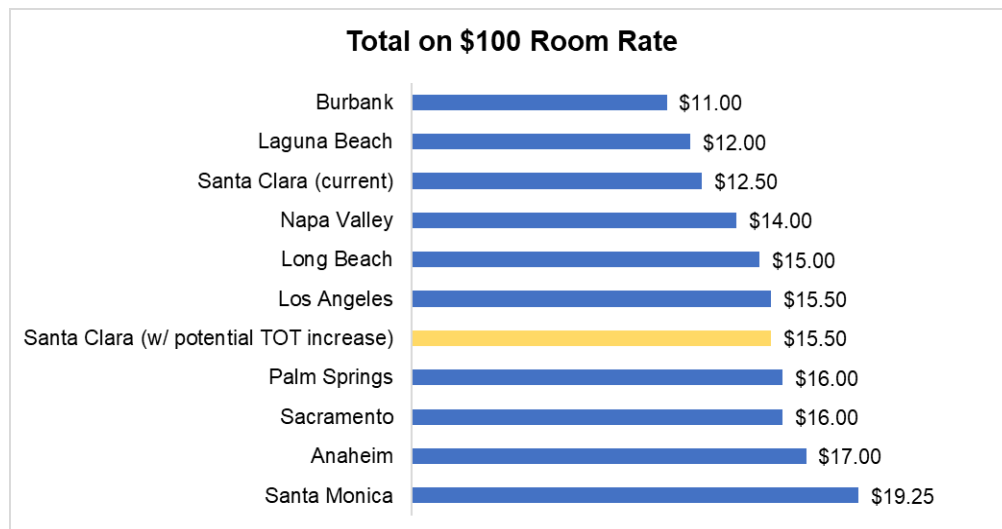


### Santa Clara Would Remain Competitive

When compared to other destinations within California and throughout the Nation, an increase in base TOT and district assessments would not impact Santa Clara as a business travel destination and Santa Clara would still be competitive with other key markets.

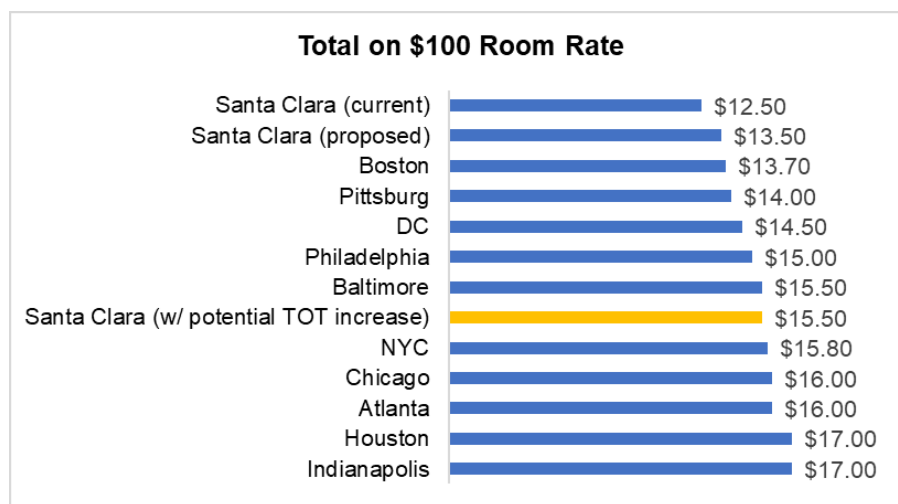
As shown in Graph 2, using the same methodology as above, when Santa Clara is compared to other California cities, Santa Clara's "out-the-door" fees still falls mid-range with Burbank at the lowest at \$11.00 on every \$100 and Santa Monica at the highest charging \$19.25 on every \$100.

**Graph 2 - Comparison to Other California Markets**



In Graph 3, Santa Clara is compared to other key markets in the country. While the comparison cities are larger than Santa Clara, they represent destinations that Santa Clara's business travelers go to frequently. Santa Clara falls in mid-range with Boston at the lowest at \$13.70 on every \$100 and Indianapolis and Houston at the highest at \$17.00 on every \$100.

**Graph 3 - Comparison to Other Key National Markets**



Primary focus customers and core travelers are those from out of the area. Many corporations use event planners that are carefully looking at costs. Corporate sales bring other business - catering, restaurants, events, sponsored experiences - all of which create additional revenue to various businesses in the City. The fact that Santa Clara would still be less out-the-door than other destinations is important for the competitiveness of Santa Clara hotels.

An increase in both the TID assessment and the base TOT could be feasible and would keep Santa Clara hotels competitive as a proposed rate increase would remain below or close to comparison cities and destinations.

#### CFD Special Tax - Future Opportunity

CFD hotel property owners voted unanimously to place a special tax on hotel room nights which took effect October 1, 2014. This special tax was pledged to finance portions of the publicly owned infrastructure for the stadium project, up to a cap of \$35M. While this is a 40-year debt ending December 31, 2054, the City is paying the debt much quicker given the higher CFD hotel collections, averaging \$2M/year for the past few years. If the City continues to pay back the debt at this rate, the debt will be paid off in 15 years (2035). If the City were to pursue an increase to the base TOT of 2% or 3% and change the TID assessment, the overall TOT rate of 15.5% or 16.5% would be temporary. With a base TOT increase of 2% or more, once the CFD debt is paid off, the 2% special tax would no longer apply, and the overall tax and assessment rates would go down by 2%. Of the 31 hotels in Santa Clara, this scenario only impacts the 11 hotels in the TID.

#### Self-Imposed Assessment

The TID assessment has no impact to local taxpayers. The TID assessment differs from the tax because it is requested, approved by, and a direct obligation of the assessed lodging businesses. The assessed lodging businesses may, at its discretion, pass the assessment on to the hotel guests which must be shown on the hotel folio and disclosed to the guest in advance when they book the room.

#### Ongoing Source of Tourism Promotion and Destination Marketing Funds

In previous years, the Santa Clara Convention Visitors Bureau (CVB) had an operating budget of approximately \$2.3M. In addition to TID revenue (approximately \$800K), the CVB received

approximately \$1.5M in City General Fund to support related visitor and tourism operations and activities. During the FY 2019/20 Operating Budget planning process, this subsidy was eliminated as it was anticipated that a combination of funds available in the Convention Center Enterprise Fund and the TID would be sufficient to fund future Destination Marketing Organization (DMO) activities and sustain future efforts.

Maintaining an ongoing source of funding at an adequate level can eliminate the need for future City General Fund support and provide the resources necessary to reintroduce and elevate Santa Clara in the convention and transient markets. Based on a 2% assessment formula, the first-year annual budget is estimated at \$3,750,000. It is important to note that revenues are cyclical and dependent upon economic activity including convention bookings, business travel and tourism. Any decrease from 2% will impact the overall estimated revenue of the TID and the DMO operating budget. The estimated budget levels at different assessment percentages are provided in Table 3.

**Table 3 - TID Assessment Options**

	Previous	Option 1	Option 2	Option 3	Option 4	Option 5
<b>TID Assessment</b>	<b>\$1/N</b>	<b>2.00%</b>	<b>1.75%</b>	<b>1.50%</b>	<b>1.25%</b>	<b>1.00%</b>
<b>TID Revenue</b>	\$ 800,000\$	3,750,000\$	3,281,250\$	2,812,500\$	2,343,750\$	1,875,000\$
<b>General Fund</b>	\$ 1,500,000\$	-	\$	-	\$	-
<b>Total CVB/DMO Funding</b>	<b>\$ 2,300,000\$</b>	<b>3,750,000\$</b>	<b>3,281,250\$</b>	<b>2,812,500\$</b>	<b>2,343,750\$</b>	<b>1,875,000\$</b>
<b>DMO PROGRAM &amp; SERVICES BUDGET</b>	<b>2.00%</b>	<b>1.75%</b>	<b>1.50%</b>	<b>1.25%</b>	<b>1.00%</b>	
Convention Sales, Incent & Svc.	50%	\$ 1,875,000\$	1,640,625\$	1,406,250\$	1,171,875\$	937,500\$
Marketing & Communications	30%	\$ 1,125,000\$	984,375\$	843,750\$	703,125\$	562,500\$
Administration	15%	\$ 562,500\$	492,188\$	421,875\$	351,563\$	281,250\$
Contingency / Reserve	3%	\$ 112,500\$	98,438\$	84,375\$	70,313\$	56,250\$
City Collection Fee	2%	\$ 75,000\$	65,625\$	56,250\$	46,875\$	37,500\$
<b>TOTAL</b>	<b>100%</b>	<b>\$ 3,750,000\$</b>	<b>3,281,250\$</b>	<b>2,812,500\$</b>	<b>2,343,750\$</b>	<b>1,875,000\$</b>

### Dedicated Funding Source

Unlike the tax, the TID assessment funds will not go into the City's General Fund. Instead, funds raised by the TID, as guided by the Management District Plan once the District is established under the 1994 Law, will be submitted to the DMO specifically for the purpose of supporting destination marketing and tourism promotion activities that directly benefit the assessed lodging businesses. DMO programs will be designed to bring in more conventions and overall visitors to the City and is projected to result in an increase in TOT collections and an increase in travel-related sales tax revenues as a result of higher hotel occupancies.

### Fairer Assessment Formula - Percentage Based

The 11 hotels in the TID offer a total of 3,069 hotel rooms with hotel rooms ranging from 107 rooms to 759 rooms. The larger hotels generally have higher average nightly rates and would proportionately pay more into the assessment than the smaller hotels. Average nightly rates vary depending on the time of year and a percentage assessment allows the fee to keep in line with hotels rates as they change.

### ***Lodging Businesses Input***

Lodging businesses in the TID are supportive of the City's efforts to identify potential revenue

strategies and opportunities for Santa Clara; however, feel strongly that a 2% assessment will create the dedicated funding stream and resources needed to put Santa Clara in a position to properly market themselves and the area through the new DMO. A successful TID would likely translate to increased revenue to the City through an increase in TOT. Additionally, increasing overnight visitation has a secondary effect wherein restaurants and other businesses would also generate additional sales tax revenue to the City.

Included as Attachment 1 is a letter to City Council from the TID hotels expressing their position on the proposed 2% TID assessment.

### ***District Formation Process***

With the current TID set to expire June 30, 2020, the process to form the new district under the 1994 Law must be immediately initiated for the new district and the new assessment to take effect July 1, 2020. The target actions and schedule are as follows:

March 17, 2020	<u>City Council - Resolution of Intention Hearing</u> Upon the submission of a written petition, signed by the business owners in the proposed district who will pay more than fifty percent (50%) of the assessments proposed to be levied, the City Council may initiate proceeding to establish a district by the adoption of a resolution expressing its intention to establish a district.
March 18, 2020	<u>Notice</u> The 1994 Law requires the City to mail written notice to the owners of all businesses proposed to be within the new district. Mailing the notice begins a mandatory forty-five (45) day period in which owners may protest the district formation.
April 14, 2020	<u>City Council - Public Meeting</u> City Council must allow public testimony on the formation of the SCTID and levy of assessments. No Council action required. The Public Meeting must be held at least 10 days after the Notice of Public Meeting/Hearing is mailed and at least seven (7) days before the Public Hearing is held.
May 19, 2020	<u>City Council - Final Public Hearing</u> The Public Hearing and Adoption of the Resolution of Formation must be held at least 45 days after the Notice is mailed.
June 30, 2020	Current district expires.
July 1, 2020	New district begins collecting new assessment.

### **ENVIRONMENTAL REVIEW**

The action being considered does not constitute a "project" within the meaning of the California Environmental Act ("CEQA") pursuant to CEQA Guidelines section 15378(b)(4) in that this is a fiscal activity that does not involved any commitment to any specific project which may result in a potential significant impact on the environment.

### **FISCAL IMPACT**

Under the current TID, the City administrative fee is \$3,000. Once established under the 1994, the City administrative fee will be equal to 2% of the assessment collected to cover administrative and collection costs.

### **COORDINATION**

This report was coordinated with the Finance Department and the City Attorney's Office.

### **PUBLIC CONTACT**

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall Council Chambers. A complete agenda packet is available on the City's website and in the City Clerk's Office at least 72 hours prior to a Regular Meeting and 24 hours prior to a Special Meeting. A hard copy of any agenda report may be requested by contacting the City Clerk's Office at (408) 615-2220, email [clerk@santaclaraca.gov](mailto:clerk@santaclaraca.gov) <<mailto:clerk@santaclaraca.gov>> or at the public information desk at any City of Santa Clara public library.

### **ALTERNATIVES**

1. Direct staff to proceed with changing the TID assessment from \$1.00 per occupied room night to 1% of gross revenue of short-term room rentals for future Council consideration.
2. Direct staff to proceed with changing the TID assessment from \$1.00 per occupied room night to 1.5% of gross revenue of short-term room rentals for future Council consideration.
3. Direct staff to proceed with changing the TID assessment from \$1.00 per occupied room night to 2% of gross revenue of short-term room rentals for future Council consideration.
4. Direct staff to commence preparatory work and return to Council to add a November 2020 ballot question which would increase the City's base transient occupancy tax by 2%.
5. Any other action as directed by Council.

### **RECOMMENDATION**

Alternatives 3 and 4

3. Direct staff to proceed with changing the TID assessment from \$1.00 per occupied room night to 2% of gross revenue of short-term room rentals for future Council consideration; and
4. Direct staff to commence preparatory work and return to Council to add a November 2020 ballot question which would increase the City's base transient occupancy tax by 2% for a new base rate of 11.5%.

Reviewed by: Ruth Mizobe Shikada, Assistant City Manager

Approved by: Deanna J. Santana, City Manager

### **ATTACHMENTS**

1. Letter from the Santa Clara TID Hotels