The Economics of Land Use

Report

Lower-Cost Overnight Accommodation Impacts and Mitigation Analysis for the American Tin Cannery Project

Prepared for:
City of Pacific Grove

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EPS #201045

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1. Introduction and Key Findings

Introduction

The American Tin Cannery Hotel and Commercial Project (ATC Project) is a proposed mixed-use hotel and retail development located in the Coastal Zone in the City of Pacific Grove (City). The ATC Project will include 225 hotel rooms and approximately 17,000 square feet of retail space. As part of the Project's Coastal Development Permit (CDP) process, the City's Local Coastal Program (LCP) requires an analysis of the impacts of the Project on lower-cost overnight accommodations (LCOA) in the City, and of the financial implications to the Project of required impact mitigation measures. This Report contains the required analysis, and has been prepared by Economic & Planning Systems (EPS) for the City at the request of the Project's developer, Comstock Homes (Developer).

The City's LCP implements the provisions and policies of the California Coastal Act (CCA) at the local level and serves as the standard of review for development permitting in the Coastal Zone. On the topic of LCOA, the CCA states in Section 30213: "Lower cost visitor and recreational facilities shall be protected, encouraged, and, where feasible, provided. Developments providing public recreational opportunities are preferred." In order to address this provision, the California Coastal Commission (CCC), which is charged with enforcing the CCA, has required cities to make provisions in their LCPs and accompanying Implementation Plans (IP) to protect and provide LCOA in the Coastal Zone.

The City's LCP, certified in March 2020, fulfills this objective by requiring analyses for "any application involving the expansion, reduction, redevelopment, demolition, conversion, closure, cessation, or new development of any project involving visitor overnight accommodations, with the exception of short-term rental lodging that is within residential units:"

1) "An analysis of a development's impact on the availability of lower cost overnight visitor accommodations in the City;"
2) "An analysis of the feasibility of providing lower cost visitor accommodations;" and
3) "Specific detailed information regarding calculation and use of any required in-lieu fees as part of a mitigation program for project impacts to the availability of lower cost visitor accommodations within the City."[1]

EPS has been retained to conduct the above analyses, which are contained herein.

[1] From Section 23.90.220 C of the City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.

Key Findings

1. **Through analysis of the financial feasibility of LCOA development in the City, EPS calculated an in-lieu fee of approximately $32,000 per room.** EPS modeled the development feasibility of a prototypical LCOA project in the City, in order to determine the subsidy needed to support such a product. The calculated financial gap for developing the prototype is approximately $32,000 per room, which represents the maximum per room in-lieu fee that Pacific Grove could charge for LCOA mitigation. The analysis uses a lower-cost average daily rate (ADR) of $117, based on the ADR for economy class hotels in the Pacific Grove market area (including Pacific Grove, Pebble Beach, Carmel-by-the-Sea, Carmel Valley, and Monterey).

2. **This analysis suggests that providing on-site lower-cost rooms would likely render the development of the ATC Project financially infeasible but that payment of the in-lieu fee may be financially viable.** EPS modeled the development feasibility of the ATC Project based on input from the Developer and research on local hotel market conditions. The model was then modified to test the financial feasibility impacts of renting 25 percent of the Project's room, or 56 rooms, at the lower cost rate of $117 per night, per the requirements of the City's LCP. This analysis demonstrated that providing rooms at a lower-cost rate on-site would be financially infeasible for the Project. Additionally, EPS tested the financial feasibility of paying an in-lieu fee of $32,000 per room for the 56 required rooms, or a total fee of approximately $1.8 million. This analysis suggests that an in-lieu fee at this level, while compromising Project economics, may not render it financially infeasible.

3. **While the City's LCP specifies that in-lieu fee revenues must be used for the development of new lower-cost lodging rooms, given constraints in land availability and zoning in the City, it may be more effective to utilize potential in-lieu fee revenues to support alternative initiatives that improve access to coast.** There are several examples throughout the Coastal Zone where coastal communities partnered with developers to create and support alternative initiatives, such as educational camping programs for area youth or development of trail facilities. Additionally, the CCC has approved the use of in-lieu fee revenues to support development and expansion of campground facilities in State and County parks in and near the Coastal Zone.

Methodology and Data Sources

The methodology and data used in this Report are based on a variety of sources as documented throughout. In addition, EPS has worked closely with the Developer and City staff to confirm the approach and analytical assumptions. The documents and information sources include, without limitation:

- Smith Travel Research (STR)
- CoStar
- Real estate industry publications and data
- Local industry professionals

EPS has also relied on its professional judgement and experience with similar studies and hotel projects. Key assumptions and data sources are referenced throughout the document, as appropriate. The actual performance and outcome of the Project will depend on a variety of factors that cannot be known for certain in advance, including prevailing market demand and supply conditions and macro-economic trends, among others.

In particular, it should be noted that this analysis was prepared as the nation and world seek to address the COVID-19 pandemic, an unprecedented public health crisis. Given that the length and severity of the pandemic is still unknown, the economic implications, particularly in the hospitality industry, will depend fundamentally on how the crisis unfolds over the next year and the timing and effectiveness of various therapeutics. The current consensus is that the economic and fiscal impacts are likely to dissipate over the long-term, although the exact pace and timeframe for recovery remains unclear.

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2. Lower Costs Rates and Mitigation

This chapter defines LCOA per CCC guidance, and summarizes the methodology used to establish the lower-cost room rate for Pacific Grove. It also identifies the LCOA mitigation measures required for the ATC Project per the City's LCP.

Lower Cost Rates

Definition of Lower Cost Rates for Overnight Accommodations

The CCC generally divides overnight accommodations into three cost categories—"lower," "moderate," and "higher" cost. The definition of the cost categories is based on a series of per room price thresholds. Establishing these thresholds provides an understanding of the "affordability" of a city's accommodation supply, and also a target average daily rate (ADR) per room that can be utilized in formulating LCOA mitigation policies. In a report produced for one of its recent public workshops on the topic of LCOA, dated October 26, 2016, the CCC recommended that local governments determine the "lower-cost" ADR threshold per room using an approach called the simplified "Robinson" methodology. The methodology calls for cities to look at "the average ADR provided by STR [Smith Travel Research] for the economy motel segment within the target market, and assume it represents the LC [lower cost] Rate without adjustment."[2]

Lower Cost Rates for Pacific Grove

In the City's LCP Implementing Ordinances, the lower cost rate for visitor accommodations is defined as the "annual average daily room rate of all economy hotels and motels in the City of Pacific Grove market area that have room rates that are equal to or below the Statewide average daily room rate or lower. Economy hotels and motels are AAA-rated one or two diamond hotels, or equivalent."[3] As such, the identifying the Pacific Grove "market area" is an important component of this analysis.

Typically, the market area for a LCOA analysis is focused on the jurisdiction in question. However, given the minimal number of hotel offerings in Pacific Grove, EPS, in consultation with the City staff and the Developer, elected to expand the market area to include the City of Monterey.[4] This definition reflects the interconnected nature of the two cities' hospitality economies, in which many visitors seeking hotels in one city will often

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[2] California Coastal Commission, "Staff Report—Public Workshop: Lower Cost Visitor Serving Accommodations," 26 October 2019, pages 29-30.

[3] Section 23.90.220 C.1.a, City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.

[4] The need to expand the market area beyond Pacific Grove is also required by data availability. Specifically, STR, the primary data source used in this analysis, does not include any "economy" hotels in Pacific Grove in its survey.

find comparable accommodations in the other, as well as the close proximity of the primary tourism attractions in the two cities.

Once the market area was established, EPS requested data from STR on economy hotels in the market area. Among the two jurisdictions, STR collects data on 11 economy class hotels, all within the City of Monterey.[5] The 2019 total year ADR for these hotels was **$116.91**. EPS rounded this rate to $117 per night, and used as the lower cost rate for Pacific Grove in the analyses in this report. EPS used the 2019 total year ADR because it represents a full year of data, and because it was not impacted by the drop in hotel demand and associated decrease in room rates that have occurred in response to the COVID-19 pandemic.

Project Impacts and Required Mitigation

The City's LCP Implementing Ordinances require "an analysis of a development's impact on the availability of lower cost overnight visitor accommodations in the City"[6] for any development that involves the redevelopment of existing accommodations or the development of new accommodations. Impacts are defined as "any loss in the available supply of existing lower cost visitor accommodations, or… [failure] to provide lower costs rooms where new accommodations are proposed."[7] The latter clause is relevant to the ATC Project, as the Project does not eliminate any existing LCOAs but rather the Developer does not intend to provide new rooms at the lower cost rate described above. The feasibility constraints limiting the Developer's ability to provide these lower cost rooms on-site are detailed in the following chapter of this report.

Given that the ATC Project will impact the availability of LCOA per the definition cited above, it will be subject to commensurate mitigation measures. For projects that provide new higher or moderate cost accommodations[8] (but do not remove or replace existing LCOA), the available mitigation measures are to provide lower cost rooms on-site, equivalent to at least 25 percent of the number of non-lower cost rooms; or to provide a combination of on-site and off-site lower cost rooms and in-lieu fee payments equivalent to the required number of lower cost rooms. As the ATC Project proposes to provide 225 new higher cost rooms, the Developer would be required to provide at least **56** lower cost rooms or the equivalent as mitigation for the Project's impacts on LCOA.

[5] It should be noted that not all hotels participate in STR surveys. In Pacific Grove specifically, STR surveys six hotels. However, the City's Chamber Commerce identifies 18 hotels and motels in the City.

[6] Section 23.90.220 C.4, City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.

[7] Section 23.90.220 C.5, City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.

[8] The LCP defines high cost as "120 percent of Statewide average daily room rate or greater," and moderate cost as "between low cost and high cost."

3. Feasibility Analysis

This chapter includes EPS's analysis of the ATC Project's development feasibility under three scenarios: without any LCOA mitigation; with mitigation through on-site lower-cost rooms; and with mitigation through the payment of an in-lieu fee. The chapter also includes EPS's calculation of a maximum allowable in-lieu fee that the City could charge for LCOA mitigation, based on a prototypical LCOA project.

Methodology

EPS's technical analysis to determine the impacts of LCOA mitigation on the ATC Project, as well as a maximum allowable LCOA mitigation in-lieu fee, relies on well-accepted "static" developer pro forma financial feasibility models. In particular, EPS developed financial models that simulate the development economics associated with the ATC Project, as well as with a prototypical LCOA development. Model inputs include development costs (e.g. land and construction), operating costs (e.g. labor and supplies) and operating revenues (e.g. room revenues and vacancy). The specific assumptions for each models' inputs are described in the following sections.

Feasibility is determined based on a comparison between the project's development costs and its value, based on annual net income divided by a yield rate.[9] If the value is less than the development costs, the project will have a financial gap and be considered infeasible. If value is greater than development costs, the project has a financial surplus and is considered financially feasible.

The analyses utilized in this chapter are designed to provide a general indication of the feasibility of developing the ATC Project, both with and without mitigation measures, as well as the feasibility of developing a prototypical LCOA project. The conclusions are based on readily available information and standard assumptions. The actual performance and outcome of the ATC Project, as well as a future LCOA project, will depend on a variety of factors that cannot be known for certain in advance, including actual development costs, financing terms, market demand and supply, and macro-economic trends.

[9] The yield rate (also known as rate of return) represents the percentage of the project's total cost represented by its annual net income. This metric of financial return is one factor that developers consider in their investment making process. EPS, in discussion with the Developer, utilized a yield rate that would typically be required in order to solicit developer interest

ATC Project Description and Feasibility

Project Description

The ATC Project involves the redevelopment of a 5.59-acre site in the City's Coastal Zone. The existing building on the site is a former American Can Company factory that was redeveloped into the American Tin Cannery Outlet mall. The Project will replace the existing 165,000 square foot building and adjacent parking lot with 344,000 square feet of hotel and retail space. This will include 225 hotel rooms with connected amenities, approximately 17,000 square feet of street retail space, and 304 surface and underground parking spaces. Of the rooms, 121 will be located in a Group/Family Wing and 104 will be located in an Executive Wing.

The development program details for the ATC Project are shown in **Table 1**. For the purposes of the feasibility analyses, EPS did not include the costs and revenues associated with the street retail portion of the ATC Project, or the associated parking that would serve that retail, as these elements of the development do not impact lodging supply in the City.

Table 1 ATC Project Development Program (Excl. Street Retail)

Item	Assumption	Total
DEVELOPMENT PROGRAM		
Total Project Site Area (acres)		5.593
Total Project Site Area (sq. ft.)		243,635
Gross Building Area (sq. ft.)		255,458
Floors		4
Square Feet Per Floor		63,865
Hotel Room Size (sq. ft.)		498
Number of Rooms		225
Executive Wing Rooms		104
Group/Family Wing Rooms		121
Other Uses (Sq. Ft.)		
Hotel Public Uses [1]		58,665
Back of House, Core and Circulation		84,743
Parking (Sq. Ft.)	325 sq. ft./space	86,125
Number of Structured Spaces		261
Number of Surface Spaces		4
Parking Uses		
Hotel Spaces	1 space/room	*225*
Employee Spaces		*40*

[1] Includes lobby, meeting/ballroom, rest/bar, fitness club, pool area
[2] Based on comparable rates and vacancies in Pacific Grove market area.
[3] Includes revenue from food and beverage, meeting/ballroom rentals, and other add-on services.
[4] EPS Estimate.
[5] Provided by Comstock Homes

ATC Project Feasibility

In order to analyze the feasibility impacts of LCOA mitigation measures on the ATC Project, EPS first created a baseline pro forma model that assessed the feasibility of the Project without any mitigation measures. The model utilized the following assumptions:

Room Rates

EPS set a room rate of $250/night for the ATC Project's Group/Family Wing rooms and $400/night for the Executive Wing rooms. These rates were determined based on EPS research on rates for comparable lodging establishments in the market area, as well as feedback from local industry professionals.

Vacancy

EPS assumed a vacancy rate of 20 percent for the ATC Project. This is slightly below the vacancy rate of 25 percent reported by STR for the market area. However, given that the ATC Project will be among the highest-end hotels in Pacific Grove and will have facilities for meetings and events, it is likely that it will achieve a higher than average occupancy rate for the area.

Net Operating Revenue

In real estate, the net operating revenue is calculated by subtracting operating costs from the building's effective revenues.[10] Operating costs for the ATC Project are assumed to be 65 percent of gross room revenue. This assumption is based on industry standards for full-service hotels, as reported by CBRE.

Parking Revenue

Operating revenues also include daily rates for parking by hotel guests. Of the 304 spaces planned for the Project, EPS assumes that 225 spaces will be reserved for hotel guests—a rate of one space per room. The daily rate of $20 is in line with the rate charged by other similar establishments in the market. The revenue calculation assumes that 85 percent of guests would drive and require parking at the hotel.

Other Operating Revenue

Other operating revenues include a percentage of adjusted gross revenue (25 percent) to reflect additional revenue sources included in the Project program, such as food and beverage, meeting room and ballroom space rentals, and other add-on services.

Yield

Private real estate development projects require capital investors in order to finance project costs (e.g. land acquisition, site improvement, vertical development, etc.). These investors (which can include private individuals and investment funds) will require a threshold level of return in order to consider making such an investment. This required return is represented in this analysis as a yield rate (also known as rate of return), and is represented as the project's annual net income divided by the project's total costs. The

[10] Effective revenues are total revenues from rooms adjusted for the estimated vacancy rate.

modeled yield rate of 7 percent is based on standard industry thresholds and was confirmed with the Developer.

Costs

All development cost assumptions for the ATC Project were provided by the Developer. However, EPS reviewed these cost assumptions against standard per unit factors typical for hotel projects of this nature, and consulted with the Developer to reconcile any assumptions that appeared to deviate substantially from industry norms.

Using the above set of assumptions, EPS calculated the development feasibility for the ATC Project. **Table 2** shows the pro forma model, which demonstrates a financial surplus of approximately $1.9 million for the Project. This result indicates that the ATC Project, given current assumptions, would be financially feasible.

Table 2 ATC Project Pro Forma Financial Feasibility Model

Item	Assumption		Per Room	Total
REVENUE ASSUMPTIONS [1]				
Executive Wing Room Rate	$400	/room per night		$15,184,000
Group/Family Wing Room Rate	$250	/room per night		$11,041,250
(less) Vacancy	20%			($5,245,050)
Adjusted Gross Revenue				$20,980,200
(less) Operating Expenses	65%	of adjusted gross (excludes TOT)		($13,637,130)
Subtotal				$7,343,070
Parking Revenue	$20	/space		$1,116,900
Other Operating Revenue [2]	25%	of adjusted gross		$5,245,050
Net Annual Operating Revenues			$60,911	$13,705,020
Threshold Value [3]	7.0%	yield	**$870,160**	**$195,786,000**
DEVELOPMENT COSTS [4]				
Direct Costs				
Building Construction Cost	$335	/building sq. ft.	$380,846	$85,690,316
FF&E, OS&E, IT	14.7%	of direct costs	$55,917	$12,581,425
Building Sub-total (excludes parking)			*$197,333*	*$98,271,741*
Parking Structure	$33,095	/parking space	$38,390	$8,637,850
Surface Spaces	$8,289	/parking space		$33,156
Site Work and Landscaping	$86.66	/land sq. ft.	$93,840	$21,114,019
LEED Gold Standard			$10,569	$2,377,948
Contingency	10%	of construction costs (excl. FF&E)	$52,843	$11,889,739
Total Direct Costs			***$632,553***	***$142,324,453***
Development Impact Fees	***3.8%***	***of direct costs***	***$23,824***	***$5,360,414***
Land Acquisition	***$446,980***	***/acre***	***$11,111***	***$2,500,000***
Other Costs				
Master Developer/Entitlement Cost	2%	of direct costs	$14,390	$3,237,777
Development Costs	6%	of direct costs	$39,301	$8,842,752
Other Soft Costs	13%	of direct costs	$84,131	$18,929,455
Hotel Pre-Opening & Working Capital	2%	of direct costs	$15,022	$3,380,000
Developer Management Fee	5%	of direct costs	$30,326	$6,823,397
Option and Land Lease	2%	of direct costs	$11,244	$2,530,000
Total Other Costs	***31%***	***of direct costs***	***$194,415***	***$43,743,381***
Total Costs			**$861,903**	**$193,928,248**
SURPLUS/(GAP)			**$8,258**	**$1,858,000**
Per Land Square Foot				**$8**

[1] Based on comparable rates and vacancies in Pacific Grove market area.
[2] Includes revenue from food and beverage, meeting/ballroom rentals, and other add-on services.
[3] EPS Estimate.
[4] Provided by Comstock Homes

In-Lieu Fee Calculation

The City's LCP defines in-lieu fees for LCOA mitigation as an amount "adequate to cover the cost of mitigation proportionate to the impact of the development."[11] Recent recommendations from the CCC related to the calculation of in-lieu fees have suggested that the "adequate" level should be determined using financial feasibility analyses for developing lower-cost rooms in the local market. Therefore, using the same methodology described above, EPS created a pro forma model to test the development feasibility of a prototypical LCOA establishment in the City. Any financing gap identified through this analysis would represent the subsidy needed to support development of low-cost rooms and, therefore, would be the maximum allowable fee level that the City could charge for LCOA mitigation.

While the methodology for analyzing the development feasibility of the LCOA prototype is the same as that used for the ATC Project, EPS used distinct assumptions as follows:

LCOA Project Description

EPS assumed that the prototype LCOA establishment would include 56 rooms, equal to the number of lower-cost rooms that the ATC Project is required to provide as mitigation. The prototype rooms are 325 square feet, which is an industry standard size. EPS also assumed that the prototype project would include 56 surface parking spaces and would have common space equal to 30 percent of the floor area represented by the rooms. In order to accommodate parking and keep the building at four stories, the prototype project is assumed to be built on a 27,000 square foot (.56 acre) site, with a floor-to-area ratio of 0.9. The development program details for the prototype are shown in **Table 3**.

Table 3 Lower-Cost Overnight Accommodation Prototype Development Program

Item	Assumption		Total
DEVELOPMENT PROGRAM			
Total Project Site Area (acres)			0.620
Total Project Site Area (sq. ft.)			27,000
Gross Building Area (sq. ft.)			23,660
Floors			4
Square Feet Per Floor			5,915
Hotel Rooms	423	sq.ft./ room (including common area)	56
Common Area Square Footage	30%	of total	7,098
Room Square Footage	325	sq.ft./ room (excluding common area)	18,200
Total Surface Parking Spaces	1.00	parking space per room	56

[11] From Section 23.90.220 C of the City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.

Revenue Assumptions

Room Rates

The room rate of $117/night is the lower-cost room rate determined for Pacific Grove based on STR data, as described in **Chapter 2**.

Vacancy

EPS assumed the same vacancy rate of 20 percent as for the ATC Project. Given the demand for lower room rates assumed for the prototype, it is likely that such a project could achieve a higher than average occupancy rate for the area.

Net Operating Revenue

Operating costs for the LCOA prototype are assumed to be 60 percent of gross revenue for the prototypes. This assumption is based on industry standards for limited service hotels, as reported by CBRE.

Parking Revenue

EPS assumed the same daily parking rate of $20 for the LCOA prototype, given market conditions. As with the ATC project, the parking revenue calculation assumes that 85 percent of guests would drive and require parking at the hotel.

Other Operating Revenue

It is assumed that the LCOA project would not include the level of amenities and event space found in the ATC Project. Therefore, other operating revenues include a small percentage of adjusted gross revenue (5 percent) to reflect additional revenue sources such as a snack bar.

Yield

The yield rate of 8 percent was based on standard industry thresholds. The required yield for the LCOA prototype is higher than that assumed for the ATC Project. Industry data suggests that developers require higher yields from economy class lodging projects, as they are considered an inferior asset class to a midscale or luxury class lodging project and also represent greater risk in the case of a market downturn

Cost Assumptions

Land Acquisition

In order to estimate the cost of land acquisition, EPS looked at data on property sales in Pacific Grove over the past five years. The analysis filtered out any sites smaller than 0.6 acres, to best represent the type of site needed for the prototype project. EPS also adjusted the sale prices to 2020 dollars, assuming a two percent annual inflation rate. The average land price of these comparable sales, approximately $6 million per acre, was used in the prototype model.

Building Construction

EPS looked at estimates from RSMeans, a construction cost estimating database, for the cost of a four-story hotel building in the Salinas metropolitan area. The provided estimate was $210 per square foot. Given Pacific Grove's position as a higher-end community within the metropolitan area, EPS assumed a slight premium on building costs, and used an assumption of $250 per square foot in the model.

Other Building and Site Costs

Furniture, fixtures, and equipment costs are set at 10 percent of building's construction costs, which is reflective of estimates for economy hotel renovation provided by JN+A and HVS Design.

A generalized average cost of $35 per land square foot was assumed for site work, based on EPS's experience with other development projects in the state.

Parking

Cost to develop surface parking spaces was estimated at $8,000 per space, in line with the assumption for surface parking costs provided for the ATC Project.

Impact Fees

The ATC Project costs include impact fees equal to approximately 3.8 percent of direct costs. EPS applied the same proportion to estimate the potential fees for the LCOA prototype.

Indirect Costs and Contingency

In addition to fees and permits, the project would incur other indirect costs (aka "soft costs"), including legal fees, architectural design and engineering services, builder's fees, general and administrative expenses, and financing expenses. These estimates are calculated as 22 percent of direct costs, reflecting standard assumptions in the real estate industry. The model also includes a 10 percent contingency cost as a buffer against future increases in fees, direct, and indirect costs.

Fee Calculation

Using the above set of assumptions, EPS calculated the development feasibility gap for the LCOA prototype. **Table 4** shows the full pro forma model, which resulted in a gap of approximately **$32,000 per room.** This gap represents the in-lieu fee that the City can charge for LCOA mitigation.

Table 4 Lower-Cost Overnight Accommodation Prototype Pro Forma Financial Feasibility Model

Item	Assumption		Per Room	Total
REVENUE ASSUMPTIONS				
Room Rate [1]	$117	/room per night		$2,391,480
(less) Vacancy	20%			($478,296)
Adjusted Gross Revenue				$1,913,184
(less) Operating Expenses [2]	60%	of adjusted gross (excludes TOT)		($1,147,910)
Subtotal				$765,274
Parking Revenue	$20	/space		$277,984
Other Operating Revenue [3]	5%	of adjusted gross		$95,659
Net Annual Operating Revenues			$20,338	$1,138,917
Threshold Value [4]	8.0%	yield	**$254,223**	**$14,236,460**
DEVELOPMENT COSTS				
Direct Costs				
Land Acquisition [5]	$6,000,000	/acre	$66,411	$3,719,008
Building Construction Cost [6]	$250	/building sq. ft.	$105,625	$5,915,000
Furniture, Fixtures, & Equipment [7]	10.0%	of direct costs	$10,563	$591,500
Building Sub-total (excludes parking)			$182,598	$10,225,508
Surface Parking	$8,000	/parking space	$8,000	$448,000
Site Work	$35.00	/land sq. ft.	$16,875.00	$945,000
Total Direct Costs			**$207,473**	**$11,618,508**
Development Fees				
Impact Fees [8]	3.8%	of direct costs	$7,884	$441,503
Total Development Fees			**$7,884**	**$441,503**
Indirect Costs				
Total Indirect Costs [9]	22%	of direct costs	**$45,644**	**$2,556,072**
Subtotal, Development Fees, Direct and Indirect Costs			**$261,001**	**$14,616,083**
Contingency (% of subtotal)	10%	of total costs excluding fees	$25,312	$1,417,458
Total Costs			**$286,313**	**$16,033,541**
SURPLUS/(GAP)			**($32,089)**	**($1,797,000)**
Per Land Square Foot				**($67)**

[1] ADR for economy hotels in Pacific Grove as reported by Smith Travel Research
[2] Based on operating expenses for limited service hotels, per CBRE
[3] Includes food and beverage.
[4] EPS Estimate.
[5] Based on recent property sales in Pacific Grove, per CoStar
[6] Based on data from RSMeans for construction costs in the Salinas metropolitan area
[7] Based on data from JN+A and HVS Design.
[8] Based on proportion of direct costs represented by impact fees for ATC Project.
[9] Includes estimated costs for architecture and engineering, other professional services, general & administrative costs, property tax during construction, financing costs, and developer fee.

Analysis of LCOA Mitigation Scenarios

EPS created pro forma feasibility models to assess two scenarios under which the ATC Project would mitigate its impacts on LCOA. The first scenario includes the development of the required 56 lower-cost rooms on-site as part of the Project. The second scenario assumes the payment of an in-lieu fee equivalent to the subsidy needed to develop the required 56 lower-cost rooms as part of a separate project. These scenarios were modeled in order to demonstrate whether or not it is financially feasible for the ATC Project to undertake either of these mitigation measures.

Scenario 1: On-Site Lower-Cost Rooms

To model the feasibility impacts of on-site mitigation, EPS made the following adjustments to the baseline pro forma model created for the ATC Project (**Table 2**):

- The number of Group/Family Wing rooms is reduced from 121 to 65 rooms, and the remaining 56 rooms are assigned as Lower Cost rooms.
- The rate for the Lower Cost rooms is set at $117 per night, the lower-cost room rate for Pacific Grove (see **Chapter 2**).
- Other operating revenues are based on 25 percent of the adjusted gross room revenues for the baseline scenario (**Table 2**). This reflects an assumption that the provision of lower-cost rooms will not impact the revenues generated from other sources such as food and beverage and meeting and event space rentals.

Table 5 shows the pro forma model for the on-site lower-cost rooms mitigation scenario. As shown in the model, the provision of 56 lower-cost rooms at the lower-cost rate for Pacific Grove would result in a financial gap of approximately $9 million, meaning that on-site mitigation would make the ATC Project financially infeasible.

Scenario 2: In-Lieu Fee Payment

To model the feasibility impacts of paying an in-lieu fee, EPS utilized with the baseline pro forma model created for the ATC Project (**Table 2**). All assumptions from that model were maintained. On the costs side of the model, EPS added a Low Cost Rooms In-Lieu Fee line item. The maximum allowable in-lieu fee is calculated as $32,000 (the per room subsidy required to support the development of lower-cost rooms, calculated in **Table 4**) multiplied by the 56 required lower-cost rooms. This equates to a total maximum allowable in-lieu fee of approximately $1.8 million.

Table 6 shows the pro forma model for the in-lieu fee mitigation scenario. As shown in the model, payment of the maximum allowable in-lieu fee would result in a financial surplus of $53,000. This would mean that the Project is marginally feasible under this scenario, leaving little room to accommodate project risk (e.g. changes in development program, costs, or market performance, etc).

Table 5 On-Site Lower-Cost Rooms Mitigation Pro Forma Financial Feasibility Model

Item	Assumption		Per Room	Total
REVENUE ASSUMPTIONS [1]				
Executive Wing Room Rate	$400	/room per night		$15,184,000
Group/Family Wing Room Rate	$250	/room per night		$5,908,438
Low Cost Room Rate [2]	$117	/room per night		$2,402,156
(less) Vacancy	20%			($4,698,919)
Adjusted Gross Revenue				$18,795,675
(less) Operating Expenses	65%	of adjusted gross (excludes TOT)		($12,217,189)
Subtotal				$6,578,486
Parking Revenue	$20	/space		$1,116,900
Other Operating Revenue [3]	25%	of adjusted gross with full rate rooms		$5,245,050
Net Annual Operating Revenues			$57,513	$12,940,436
Threshold Value [4]	7.0%	yield	**$821,615**	**$184,863,375**
DEVELOPMENT COSTS [5]				
Direct Costs				
Building Construction Cost	$335	/building sq. ft.	$380,846	$85,690,316
FF&E, OS&E, IT	14.7%	of direct costs	$55,917	$12,581,425
Building Sub-total (excludes parking)			*$436,763*	*$98,271,741*
Parking Structure	$33,095	/parking space	$38,390	$8,637,850
Surface Spaces	$8,289	/parking space		$33,156
Site Work and Landscaping	$86.66	/land sq. ft.	$93,840	$21,114,019
LEED Gold Standard			$10,569	$2,377,948
Contingency	10%	of construction costs (excl. FF&E)	$52,843	$11,889,739
Total Direct Costs			***$632,553***	***$142,324,453***
Development Impact Fees	***3.8%***	***of direct costs***	***$23,824***	***$5,360,414***
Land Acquisition	***$446,980***	***/acre***	***$11,111***	***$2,500,000***
Other Costs				
Master Developer/Entitlement Cost	2%	of direct costs	$14,390	$3,237,777
Development Costs	6%	of direct costs	$39,301	$8,842,752
Other Soft Costs	13%	of direct costs	$84,131	$18,929,455
Hotel Pre-Opening & Working Capital	2%	of direct costs	$15,022	$3,380,000
Developer Management Fee	5%	of direct costs	$30,326	$6,823,397
Option and Land Lease	2%	of direct costs	$11,244	$2,530,000
Total Other Costs	***31%***	***of direct costs***	***$194,415***	***$43,743,381***
Total Costs			**$861,903**	**$193,928,248**
SURPLUS/(GAP)			**($40,289)**	**($9,065,000)**
Per Land Square Foot				**($37)**

[1] Based on comparable rates and vacancies in Pacific Grove market area.

[2] ADR for economy hotels in Pacific Grove as reported by Smith Travel Research. Number of low-cost rooms equal to 25 percent of total rooms.

[3] Includes revenue from food and beverage, meeting/ballroom rentals, and other add-on services. Based on adjusted gross revenue from all market-rate rooms scenario.

[4] EPS Estimate.

[5] Provided by Comstock Homes

Table 6 In-Lieu Fee Mitigation Pro Forma Financial Feasibility Model

Item	Assumption		Per Room	Total
REVENUE ASSUMPTIONS [1]				
Executive Wing Room Rate	$400	/room per night		$15,184,000
Group/Family Wing Room Rate	$250	/room per night		$11,041,250
(less) Vacancy	20%			($5,245,050)
Adjusted Gross Revenue				$20,980,200
(less) Operating Expenses	65%	of adjusted gross (excludes TOT)		($13,637,130)
Subtotal				$7,343,070
Parking Revenue	$20	/space		$1,116,900
Other Operating Revenue [2]	25%	of adjusted gross		$5,245,050
Net Annual Operating Revenues			$60,911	$13,705,020
Threshold Value [3]	7.0%	yield	**$870,160**	**$195,786,000**
DEVELOPMENT COSTS [4]				
Direct Costs				
Building Construction Cost	$335	/building sq. ft.	$380,846	$85,690,316
FF&E, OS&E, IT	14.7%	of direct costs	$55,917	$12,581,425
Building Sub-total (excludes parking)			*$436,763*	*$98,271,741*
Parking Structure	$33,095	/parking space	$38,390	$8,637,850
Surface Spaces	$8,289	/parking space		$33,156
Site Work and Landscaping	$86.66	/land sq. ft.	$93,840	$21,114,019
LEED Gold Standard			$10,569	$2,377,948
Contingency	10%	of construction costs (excl. FF&E)	$52,843	$11,889,739
Total Direct Costs			***$632,553***	***$142,324,453***
Development Impact Fees	***3.8%***	***of direct costs***	***$23,824***	***$5,360,414***
Low Cost Rooms In-Lieu Fee [5]	***$32,089***	***/req. rooms***	***$8,022***	***$1,805,022***
Land Acquisition	***$446,980***	***/acre***	***$11,111***	***$2,500,000***
Other Costs				
Master Developer/Entitlement Cost	2%	of direct costs	$14,390	$3,237,777
Development Costs	6%	of direct costs	$39,301	$8,842,752
Other Soft Costs	13%	of direct costs	$84,131	$18,929,455
Hotel Pre-Opening & Working Capital	2%	of direct costs	$15,022	$3,380,000
Developer Management Fee	5%	of direct costs	$30,326	$6,823,397
Option and Land Lease	2%	of direct costs	$11,244	$2,530,000
Total Other Costs	***31%***	***of direct costs***	***$194,415***	***$43,743,381***
Total Costs			**$869,926**	**$195,733,271**
SURPLUS/(GAP)			**$236**	**$53,000**
Per Land Square Foot				**$0**

[1] Based on comparable rates and vacancies in Pacific Grove market area.
[2] Includes revenue from food and beverage, meeting/ballroom rentals, and other add-on services.
[3] EPS Estimate.
[4] Provided by Comstock Homes
[5] Fee per room based on subsidy needed for developing low-cost rooms. Number of required low-cost rooms equal to 25 percent of total rooms.

4. Alternative Mitigation Measures

The City's LCP specifies that in-lieu fees "shall only be used for the provision of new lower-cost overnight accommodations, within the City. Funds may be used for activities including land acquisition, construction, and/or renovation that will result in additional lower-cost visitor accommodations, as well as permitting costs."[12] However, given that there are relatively few vacant or redevelopment sites in the City, as well as other planning and zoning constraints, it may be challenging for a developer to build a new LCOA project in the City, even with the help of in-lieu fee revenue. Therefore, the City may decide to consider alternative uses of the in-lieu fees, or to work with the Developer to fund alternative initiatives, that still fulfill the mission of improving access to the coast. The following case studies provide examples of such alternative uses and partnership initiatives approved by the CCC in other coastal cities.

Lido House Hotel - Newport Beach

In October 2015, the Coastal Commission approved the Lido House Hotel, a 130-room higher cost hotel to be developed on land leased from the city of Newport Beach (the former City Hall site).[13] The applicant, R.D. Olson Development, elected to pay an in-lieu mitigation fee rather than provide lower-cost accommodations on-site, and collaborated with the City to propose an alternative mitigation strategy that would use the $1.4 million in fee revenue to establish the Fostering Interest in Nature (FiiN) program, an overnight coastal education camp for underserved youth. When the project was approved, several Coastal Commissioners expressed support for the program as an "innovative way to use funds that may otherwise be untouched for years."[14]

The Lido House Hotel opened in early 2018, and one year later, 350 fifth-graders participated in the FiiN program during its first ten-week season.[15] Once fully operational, FiiN is expected to serve up to 420 students each year. Student groups from Title 1 elementary schools in Orange County are eligible for the free four-day, three-night trip, and are hosted in tent and/or cabin facilities at the Newport Dunes Waterfront Resort. The program includes coastal-education components focusing on marine biology, conservation, and water safety, as well as recreational activities like kayaking, hiking, and surfing.[16] FiiN is administered by the Newport Bay Conservancy and the City of

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[12] From Section 23.90.220 C of the City of Pacific Grove Local Coastal Program (LCP) Implementing Ordinances.
[13] California Coastal Commission October 2015 Agenda
[14] https://www.latimes.com/socal/daily-pilot/news/tn-dpt-me-1008-lido-hotel-coastal-20151007-story.html
[15] https://rdodevelopment.com/news-posts/low-income-kids-get-a-chance-to-explore-nature-in-sleep-away-science-camp-at-newports-back-bay/
[16] California Coastal Commission Staff Report

Newport Beach, and will be funded for at least ten years by in-lieu fee revenue, after which the City plans to pursue additional grant funding.

The Ranch at Laguna Beach

In May 2014, the Laguna Beach Planning Commission issued a local coastal development permit for the Laguna Beach Golf and Bungalow Village.[17] The applicant planned to renovate the 64-room Aliso Creek Inn and Golf Course by expanding amenities on the 84-acre property and adding 33 new hotel rooms. This would require converting 32 of the existing one-bedroom suites to 64 standard hotel rooms and replacing a residential unit with a penthouse suite, resulting in the loss of 32 lower cost units and the creation of 33 higher cost units, for a total of 97 units. The Coastal Commission determined that the Project would have to mitigate the loss of affordable overnight accommodations and other impacts on public access.[18]

In January 2015, the Coastal Commission approved a final mitigation plan for the project, which was rebranded as The Ranch at Laguna Beach. Debate at the Commission meeting touched on the relative affordability of the proposed units compared to units at nearby luxury hotels, and the significance of the project for the city of Laguna Beach. The mitigation plan included the following:[19]

- An in-lieu fee payment to be used to design and permit a pedestrian and cycling trail. Remaining funds could be used for trail construction and/or maintenance.
- Dedication and management of a floating trail easement.
- Hosting at least 12 overnight small group camping experiences (40 person maximum) at the project's on-site Scout Camp each year for nonprofit groups.
- Inclusion of sleeper sofas in at least 32 of the 97 rooms in order to accommodate 4 or more guests, and microwaves in all 97 rooms.

Campground Support

There are several examples of the CCC authorizing the use of LCOA in-lieu fees for campground development and expansion in state and county parks near the new development. These include:

- Demolition of the 23-room Seal Beach Inn in Seal Beach and construction of six single family homes was approved in May 2006 pending the payment of an in-lieu fee to mitigate the loss of visitor-serving uses on the site. The fee, in the amount of $87,810, funded the creation of a 40-person group campsite at Doheny State Beach in Dana Point, which was completed in 2008.[20]

[17] http://lagunabeachcity.granicus.com/MetaViewer.php?view_id=3&clip_id=420&meta_id=32176
[18] https://documents.coastal.ca.gov/reports/2014/7/W15a-7-2014.pdf
[19] https://documents.coastal.ca.gov/reports/2015/4/w14a-4-2015.pdf
[20] https://documents.coastal.ca.gov/reports/2006/5/W18e-5-2006.pdf

- In 2015, the Coastal Commission approved a plan to develop five single family homes on a 24-acre waterfront property in Malibu, known as Malibu Coast Estates. The applicant paid an in-lieu fee of $4,000,000 to mitigate the loss of visitor-serving coastal access. Fee revenue is currently held by the Mountains Recreation and Conservation Authority (MRCA) and will partially fund a camp facility at Puerco Canyon in Malibu that will serve foster children and their families, with additional spaces available for the general public.[21]

- The ongoing renovation of the Hotel Del Coronado in the City of Coronado includes the addition of 144 new higher-cost hotel rooms, which required a mitigation fee of $1,080,000 as a condition of approval in 2010.[22] In 2019, the Coastal Commission authorized the use of the funds ($1,890,363 with interest) for the construction of the Tijuana River Valley Regional Park Campground in San Diego County. The campground will include 63 campsites, 16 yurts, a nature education center, and day use facilities, including an equestrian center.[23]

[21] https://documents.coastal.ca.gov/reports/2016/7/w6a-7-2016.pdf
[22] http://www.coronadonewsca.com/news/coronado_home_and_business/construction-for-hotel-del-coronado-master-plan-to-begin-in-early-2019/article_f1f49dde-7bc8-11e8-8e93-0beff9952e45.html
[23] https://scc.ca.gov/webmaster/ftp/pdf/sccbb/2019/1903/20190314Board06_Tijuana_River_Valley.pdf