BRION & ASSOCIATES

MEMORANDUM

To: City of Menlo Park Planning Staff
Cc Dave Bohannon and Bohannon Planning Team

From: Joanne Brion, Brion & Associates

Subject: Response to Comments on Conley's Peer Review of Bohannon Fiscal Impact Analysis 2005; B&A #2322

Date: January 18, 2007

The following summarizes Conley Consulting Group's main comments and criticisms of the 2005 Fiscal Impact Analysis prepared by Brion & Associates of the then-proposed project at Constitution and Independence by the Bohannon Organization. Responses are provided below. At this point we are updating the 2005 study and will be preparing a new version of the analysis based on the new project description submitted recently to the City. The following provides summary statements from the Conley letter, our response, and any changes that have been made to the analysis.

Conley suggests tax revenues were overestimated in three categories:

1. ***TOT revenues** because an unidentified portion of revenues will be transferred from TOT revenues from other MP hotels*

   Since we prepared the last fiscal analysis, Marriott Hotels has become interested in the project and is proposing a completely different type of hotel concept than we had analyzed before. The Bohannon Organization has hired PKF Consulting to analyze the hotel market and to provide support for the assumptions we are using and to comment on the impact of the proposed project on existing hotels and motels.

2. ***Sales Tax revenues** due to unreliability of projections of sales taxes from businesses based solely on land use or building type information*

   The analysis we conducted for this study was a comprehensive analysis of the actual sales tax revenues by type of land use and by tenant. This analysis is the first time the

City analyzed actual revenue generated by address, building and tenant. The analysis results in average sales tax factors per sqft of office space that range from $.017 per sqft to $.05 cents per sqft. The City's prior citywide fiscal impact assumed no sales tax from office users and $.85 per sqft of R&D space. Our analysis showed that actual R&D sales tax averaged 5 to 9 cents per sqft and not 85 cents. The factors used in our analysis are based on actual performance of businesses in Menlo Park and are not unreliable as Conley suggests. Furthermore, the sales tax from office space represents a very small portion of the overall revenue of the project, estimated at about $8,800 to $26,000.

Our current model assumes the moderate sales tax factor, which we believe is reasonable and we have inflated it from 2003 dollars to 2007 dollars for our current analysis. Given the small variability of the sales tax revenue from office space on the overall performance of the project, we do not believe these scenarios are relevant at this time. We will be preparing sensitivity on the TOT revenue in our new analysis, based on the results of the PKF study.

3. ***Business License Taxes** were calculated incorrectly.*

Our previous analysis took the entire business license revenue and calculated an average revenue factor per employee of $59.57 based on our discussions with City Finance Department staff.

There are two ways to estimate business license taxes: 1) on a per employee basis; and 2) on a gross receipts basis. For office we do not know what gross receipts will be and thus use a per employee basis. For hotel and retail we do have gross revenue estimates and use approach #2. While our previous methodology was reviewed and approved by the City, we have gone ahead and revised this revenue estimate. We have taken revenue data from the Finance Department (FY 06-07) on business license revenue by industry category and sorted it into businesses that use office and R&D space and those that do not. Then we have calculated an average revenue per employee factor and applied that to the new estimate of office space or the project. For retail, gym and hotel we are using the estimated gross revenues from the three uses to estimate the businesses license tax. Our new approach results in an estimate of $108,000 instead of the prior figure of $106,000. Given the larger size of the overall project, our estimate for this revenue source has been reduced overall. The current total revenue per employee ends up at $43 per employee from the combined approaches instead of $59 per employee.

4. ***Sales Tax analysis.*** *Brion study has no analysis of whether sales tax estimates for two new development alternatives represent net new revenues to City. While Brion does provide a range of assumed sales tax generated per square foot of office space based on historic sales tax generated, it doesn't recognize that it is possible that new tenants on-site could have different sales tax-generating characteristics than the tenants who now occupy space in the area. Sales tax based solely on land use is unreliable.*

   If the project were a retail shopping center the study would include a retail market analysis to determine if the sales tax would be net new sales to the City. Given that the project includes a modest amount of retail designed to serve hotel visitors and office employees, it is pretty clear that the sales tax revenues would be new revenues. Given the lack of revenue opportunities in the M-2 District it is unlikely that the project would impact existing retailers.

   The sales tax factors developed for the office spaces represent the average overall and include business in office space that generate sales tax and those that do not generate any sales tax. The analysis found that sales tax per sqft, depending on the tenant, could range from a low of 4 cents to a high of 98 cents per sqft of space. Thus, our assumption of 5 cents on average is conservative. This approach accounts for the fact that not all office users will generate sales tax revenues for the City.

5. ***City Costs.*** *Brion likely underestimates cost of providing City services to new development because costs were calculated on a modified marginal cost basis resulting in a projected cost about $108,000 lower than what CCG feels is appropriate.*

   Our current analysis has been revised to address Conley's concerns about costs. We have removed the portion of the analysis where we assume some portion of each department costs are fixed, which is the main concern.

   Conley suggests that the reduction in City costs from 2002 to 2005 was a direct result of a loss of employment. What she does not point out is that the reduction in costs after the dot.com crash was not a result of having fewer employees in the city and thus, lower costs but a result of having less revenue and the need to reduce service levels to reduce city costs, irrespective of whether employment was reduced. Sales tax and other business revenues were significantly less and are the main factors that trigger lower service costs and not a loss of employment directly. It was a loss of business activity that impacted city revenues and in turn city costs.

Despite our disagreement with her analysis, our current cost factor per employee is higher at $201 per employee, assuming a total General Fund budget of $28.7 million, where as our prior analysis the factor was $169 per employee with a total General Fund budget of $29.9 million. So our current factor is more conservative than our prior analysis because we removed the "% fixed" portion of the calculations.

6. *CCG concludes that* ***lack of specificity of a development program*** *is a major risk to relying on the results of fiscal impact analysis in decision-making about the site and proposed development agreement would permit considerable flexibility about timing and nature of uses built on site.*

   The analysis is, and was, based on a specified proposed project, with specific estimates of office, hotel, and other uses. It is true that the zoning request is more general and that the project may change. However, the analysis would be updated and reissued for City review if the proposed project changed significantly. For example, the new project description has changed significantly from the 2005 analysis and we are in the process of updating the fiscal analysis and other analyses such as the EIR based on the new project description.

   Concerning timing, the current intent is to develop the hotel complex first and perhaps some of the office. The majority of the project revenues come from the hotel and thus, the fiscal benefits would be greater in the beginning before the other uses are development.

In summary, Conley focuses her critique on several areas where she disagrees with our approach but she fails to point out in her summary comments that there are numerous places where she agrees with our approach and assumptions, and even finds them to be conservative. The overall result is a "tone" that suggests that the analysis is flawed. But in reality, with the corrections made above, we contend that our analysis is conservative and presents the City with a general idea of the type of fiscal benefits that it can expect from the proposed Bohannon project.