

**CITY COUNCIL**

For City Clerk's Use:

**APPROVED**  **DENIED**

Reso No. <sup>2006</sup>2004-216R File No. 0808-40

Ord No. 2004-<sup>2006</sup>217R HOTEL

Agenda Item No.: 21  
Date: August 23, 2006

**TO:** Honorable Mayor and Members of the City Council  
**FROM:** Jack Anderson, Assistant City Manager  
**SUBJECT:** Approval of Downtown Hotel and Conference Center Project

**RECOMMENDATION:**

It is requested that Council take the following actions:

- a) Adopt Resolution 2006-217 Amending the Downtown Specific Plan's Civic Center District to allow a nine-story hotel with seven above-ground floors and related facilities; consideration of a Planned Development for a 196-room hotel and related facilities including a restaurant, health club, and administrative offices, and installation of signals and/or stop signs at three nearby intersections. The request involves the adoption of project-specific development standards for a maximum building height of 75 feet and 209 parking spaces to be built in the hotel's two underground parking levels based on studies conducted by Walker & Associates and resulting in a reduction of 75 surface parking spaces that currently exist between City Hall and the California Center for the Arts. A Planned Development application for the project is also proposed.
- b) Adopt Resolution 2006-216 Authorizing the Mayor and City Clerk to execute a Disposition and Development Agreement between the City of Escondido and Escondido Development, LLC that specifies the roles, responsibilities and financial obligations of the parties in the development and ongoing operation of the project.

**FISCAL ANALYSIS:**

This project is expected to cost a total of \$56,318,369 of which the City will contribute cash in the amount of \$16,485,489 consisting of the acquisition of an operating covenant, construction of a two-level subterranean parking structure and various site preparation requirements, as well as off-site improvements.

The City's anticipated revenue from the project calculated in net present values will be \$27,351,000. This revenue stream consists of Transient Occupancy Tax, property and sales tax receipts, and ground lease payments.

**GENERAL PLAN ANALYSIS:**

A Downtown Hotel and Conference Center Project is consistent with General Plan goals of an economically viable downtown area.

**PREVIOUS ACTION:**

- In June 2004 the Council directed negotiations take place with the Phelps/CW Clark development team for the Hotel and Conference Center project.
- In February 2005 the Council directed staff to continue negotiations with an expanded project that included a mixed use project on Public Parking Lot One; the project included residential condominiums, public parking and retail spaces.
- In May 2006 the City and the Developer agreed to eliminate the mixed use project from the expanded project and to construct only the hotel including the subterranean parking and refurbishment of the Conference Center building, with no project development to take place on Public Parking Lot One. While the City Council stated a continuing interest in the concept of additional residential development in the immediate downtown area, Council directed that the future uses of Lot One be considered as part of the Downtown Specific Plan and its environmental review. There are no agreements in place or specific plans for Parking Lot One.

**BACKGROUND:**

**Market Demand**

The City commissioned a Hotel Market Demand study in April 2003 by PKF Consulting. The study demonstrated a potential for success for a full-service hotel constructed and operated in conjunction with the existing CCAE Conference Center. During the extended time of negotiations with the development team, the 2003 study was reviewed and updated in January 2006. Subsequently, CW Clark and Sage Hospitality have provided revised assumptions regarding Average Daily Rate, occupancy and expenses relating to the hotel operations. The hotel operating projections reflected in the Keyser Marston Associates financial analysis represent the expected financial outcomes of these studies.

**Development Team**

After the completion of the initial Market Study, the City conducted a Request for Qualifications (RFQ) process, followed by a Request for Proposal (RFP) process among qualified firms. The City Council clearly stated its goal of creating a public-private partnership with a quality team that was willing to invest substantial private funds into the project. The team of CW Clark, Inc.; Phelps Program

Management, Joseph Wong Design Associates, Sage Hospitality Group and Hensel Phelps Construction were selected for the project. Negotiations have taken place with the City's negotiating team under the direction of the City Council. The City has retained consulting expertise for advice on hotel development issues, financial implications and assessments and legal support for creating the Disposition and Development Agreement.

### The Project

The project consists of a 196 room Marriott Hotel situated on city-owned property located between the City Hall and the California Center for the Arts Escondido (CCAE) and refurbishment of the existing Conference Center building. The hotel will be operated in conjunction with and physically connected to the current CCAE Conference Center building. Two levels of underground parking will be constructed under the hotel providing 209 parking spaces; the hotel will have use of the 11 surface parking spaces located adjacent to the Conference Center on its south side. This combined parking inventory represents 220 spaces for the Hotel and Conference Center project. The architectural theme of the hotel is consistent with, and complementary to the other buildings in the Civic Center complex.

### Project Changes

During the initial negotiation period, the developer team, aware of the City Council's publicly-stated goal of bringing additional residential development to the downtown area, proposed a mixed-use project of high-quality condominiums for a location across West Valley Parkway from the hotel on Public Lot One. The City's role would have been to add public parking to the project along with limited commercial spaces to create additional downtown activity along the Maple Avenue corridor connecting Grand Avenue to the CCAE. This change in the project scope added financial benefit to both the City (sale of air space above the public parking) and the Developer Team (the value of residential development to complement the hotel investment).

In response to a high level of community concern with the mixed-use portion of the project, and the concern that the height of the proposed building might negatively impact downtown, the City and the Developer Team agreed to remove the mixed-use portion of the project from the Hotel and Conference Center. The City Council continues to support the concept of residential development in the downtown, and expects the Downtown Specific Plan to consider residential mixed-use on the Public Lot One property. Such consideration will include assessment through a comprehensive environmental review process. However, the proposed Hotel and Conference Center project being considered by the City Council at this time does not include consideration of any mixed-use development in the downtown area. Moreover, there are no agreements in place or proposed, with either the developer team or any other entity, for further development on the Public Lot One property.

Although no new public parking will be constructed as part of this project, the Staff and the Downtown Business Association are continuing to work on long term parking solutions for the downtown area. These efforts will be built on the information gathered in the Walker Parking Consultants study as well as consideration of alternatives for a parking system that can be implemented with full DBA and City cooperation and coordination.

Disposition and Development Agreement

The Disposition and Development Agreement presented as part of this City Council action defines the specific responsibilities for both the CW Clark Team and the City in this project. Specifically, the parties are responsible as follows:

**The Developer will:**

- Obtain all entitlements and approvals for the Hotel and Conference Center, paying all permit fees required by the City
- Design, construct and operate a 196-room full service Hotel and Conference Center
- Refurbish the current Conference Center and upgrade to Marriott standards, and assume full responsibility for all operating and maintenance costs during the term of the lease
- Secure a twenty-year franchise agreement with Marriott International, operating the hotel to Marriott standards and quality
- Make ground lease payments to the City for the fifty-five year term of the lease as a percentage of gross revenue of Hotel and Conference Center operations
- Contribute equity and private financing to complete construction of the project
- Enter into an operating agreement between the City, the CCAE and the Hotel

**The City will:**

- Lease the Conference Center and the land under the hotel site for 55 years to the Developer
- Contribute \$6,000,000 in equity towards the development of the hotel
- Pay for the construction of two levels of subterranean parking below the hotel (209 spaces) and pay for costs to prepare the site for construction of the hotel (\$9,225,489)

- Pay for offsite costs including traffic signal improvements at West Valley Parkway/Maple Street and West Second Avenue/Maple Street and connection of the City Hall building to a new chiller system (\$1,260,000)

Financial Implications

Attached to the staff report are two reports from Keyser Marston Associates representing their assessment of the economics of the proposed project. In summary form, the information below represents Annual City revenues from this project:

|   |                    |
|---|--------------------|
| Transient Occupancy Tax:<br>(Projected at year 4)<br>(Collected immediately on hotel opening) | \$ 821,000         |
| Sales tax:<br>(Contributed by hotel guests; includes spending in Escondido)                   | \$ 294,000         |
| Property taxes:<br>(Includes Redevelopment Tax Increment)                                     | \$ 250,000         |
| Housing Set-Aside:  | <u>\$ 76,000</u>   |
| <b>Total Annual City Revenues</b>   | <b>\$1,441,000</b> |

Base Rent (Ground Lease) payments begin after 10 years of operations and are based on a percentage of gross revenues from all operations of the Hotel and Conference Center.

Net present value of all project revenues (calculated through the 55-year lease term):

|  |                     |
|--|---------------------|
| Base Rent Payments:  | \$ 7,731,000        |
| Taxes (Hotel and Property):  | \$19,620,000        |
| <b>Total Present Value of City Revenue (2006):</b><br>Discount rate 8% | <b>\$27,351,000</b> |

The transition of the Conference Center from operation by the CCAE to the lease to the Hotel operation is critically important to the City. As part of the lease, the Developer will assume full responsibility for the operations, maintenance and capital maintenance of the Conference Center building. This building is currently owned by the City and operated by the CCAE; periodic repairs and maintenance are the responsibility of the City as it contributes to the CCAE. Additionally, the City

Downtown Hotel and Conference Center

August 23, 2006

Page 6

pays the utility costs of this building. All of these costs will be the responsibility of the hotel Developer during the entire term of the lease.

California Center for the Arts Escondido

The CCAE Board conducts operations at the Center for the Arts. Their responsibility under the management agreement with the City includes operations of the theaters, Museum and the Conference Center. The City, as the owner of the CCAE buildings, has determined to separate the Conference Center building from the balance of the CCAE campus. The CCAE Board will continue its responsibility to operate the remaining CCAE venues.

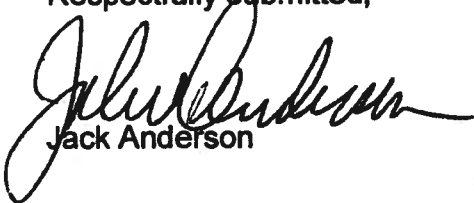
The City Council will evaluate the financial impact of the CCAE's reduced operational venues to understand levels of financial support that might need to be adjusted due to the Hotel project. Keyser Marston Associates has been retained by the City to evaluate the impact of this project on CCAE operations and revenues. The findings of the study are in final review and will serve as a basis for future City financial support of the CCAE.

Additionally, an operating agreement will be created between the CCAE, the Hotel Operator and the City to ensure that the interrelationship of the Hotel and the CCAE can be most beneficial to all parties.

SUMMARY

The Downtown Hotel Project is critical to the ongoing economic development of the City and the downtown area. The project has undergone extensive negotiations and review, and it is an outstanding example of public-private partnering for the benefit of the City and the Developer Team.

Respectfully submitted,

  
Jack Anderson



**KEYSER MARSTON ASSOCIATES**  
ADVISORS IN PUBLIC/PRIVATE REAL ESTATE DEVELOPMENT

**MEMORANDUM**

ADVISORS IN:  
REAL ESTATE  
REDEVELOPMENT  
AFFORDABLE HOUSING  
ECONOMIC DEVELOPMENT

**To:** Jack Anderson, Assistant City Manager  
City of Escondido

SAN FRANCISCO  
A. JERRY KEYSER  
TIMOTHY C. KELLY  
KATE EARLE FUNK  
DEBBIE M. KERN  
ROBERT J. WETMORE

**From:** KEYSER MARSTON ASSOCIATES, INC.

**Date:** August 17, 2006

**Subject:** Civic Center Hotel - Review of Proposed Transaction

LOS ANGELES  
CALVIN E. HOLLIS, II  
KATHLEEN H. HEAD  
JAMES A. RABE  
PAUL C. ANDERSON  
GREGORY D. SOO-HOO

**I. Introduction**

SAN DIEGO  
GERALD M. TRIMBLE  
PAUL C. MARRA

Keyser Marston Associates, Inc. (KMA) has been requested to review the proposed development transaction between the City of Escondido (City) and Escondido Development, LLC (Developer) for the development of a 196-room Marriott brand hotel (Project). The proposed development transaction is described in the proposed Disposition and Development Agreement (DDA) dated August 10, 2006.

The Project will be developed on a 2.29-acre site (Site) on the north side of West Valley Parkway adjacent to the California Center for the Arts Escondido (CCAЕ). The Developer intends to construct an approximately 118,000 square foot (SF) hotel consisting of 196 rooms, a lobby/lounge area, meeting rooms, and a restaurant. Parking for the Project will be provided in a 209-space subterranean garage with 11 surface spaces on the Site.

**II. Key Findings**

KMA's key findings related to the proposed transaction are as follows:

- The City will lease to the Developer a 2.29-acre site consisting of the existing CCAE conference center and adjacent parking lot for a period of 55 years.
- The Developer will develop a 196-room, seven-story Marriott brand hotel with 209 subterranean parking spaces, plus refurbish the conference center.

1660 HOTEL CIRCLE NORTH, SUITE 716 > SAN DIEGO, CALIFORNIA 92108 > PHONE: 619 718 9500 > FAX: 619 718 9508

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006

Page 2

- The Developer agrees to construct the hotel, and to continually use and operate the hotel for a period of 55 years.
- The total estimated development cost for the Project is estimated at \$56,318,000, inclusive of the payment of prevailing wages during construction. The total development budget can be broken out as follows:

| <b>Development Costs</b>       | <b>Total</b>        |
|--------------------------------|---------------------|
| Direct Costs                   | \$43,932,000        |
| Indirect Costs                 | \$8,358,000         |
| Financing Costs                | \$4,028,000         |
| <b>Total Development Costs</b> | <b>\$56,318,000</b> |

- The City will contribute total financial assistance toward the development costs of the hotel of \$15,226,000 (maximum). The City contribution will be provided in two forms:

| <b>Source</b>  | <b>Total</b>        |
|--|---------------------|
| City Purchase Price for Subterranean Parking (maximum) | \$9,226,000         |
| Covenant Acquisition Consideration                     | \$6,000,000         |
| <b>Total City Contribution (maximum)</b>               | <b>\$15,226,000</b> |

- The balance of the development costs, \$41,092,000, will be funded by the Developer through conventional debt and equity investment.
- KMA has extensively analyzed the Developer's projections of development costs, achievable net operating income (occupancy, room rate, other revenues, and operating expenses), debt financing assumptions, and future value of the hotel after stabilization. Based on this review, it is the KMA estimate that the Project will achieve a leveraged internal rate of return (IRR) on Developer equity on the order of 17.1%. This return reflects the allocation of costs between the City and Developer as described above.

To: Jack Anderson, Assistant City Manager  
Subject: Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 3

- Based on current industry standards, KMA believes a leveraged IRR in the mid- to high teens is an appropriate target. This target return is reflective of the risks associated with development of a high-rise hotel (Type I construction) in a pioneering location. On this basis, then, KMA concludes that the proposed City financial contribution is warranted.
- Under the terms of the proposed ground lease, the Developer will pay ground rent to the City in three principal forms:
  - Base rent
  - Additional rent
  - Additional rent in case of a capital event
- KMA estimates that the City will receive total ground rent of \$7,731,000 in present value terms (based on an 8.0% discount rate).
- KMA has also projected the anticipated stream of tax revenues to be generated by the Project. Over the term of the 55-year lease, KMA estimates that the City and/or its Redevelopment Agency will receive total tax revenues of \$19,620,000 in present value terms (based on an 8.0% discount rate).

### III. Background

#### A. City Overview

The City of Escondido (City) is located at the confluence of Interstate 15 and Highway 78. It is approximately 18 miles inland, 30 miles northeast of downtown San Diego, and has a population of about 135,000. The City's relatively small size makes it a highly desirable place to live, and offers a number of amenities including a range of housing options, parks and lakes, golf courses, art galleries, antique stores, restaurants, and wineries.

In the early 2000s, a number of developers began noticing the potential of downtown Escondido for both commercial and residential development. This trend continues in today's marketplace with several commercial projects as well as nearly 700 condominiums and townhomes being proposed in or near downtown.

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 4

**B. Recent Development Trends in Escondido**

The City has seen substantial growth over the past several years. Most recently, the City has placed an emphasis on downtown revitalization. This emphasis can be attributed to demographic changes that support "urban" housing, and an increased interest from developers to build in the City's downtown. A few of the most recently constructed, planned, and proposed projects near downtown are discussed below.

- **Signature Pavilion Complex** – The complex opened in November 2003 and was recently sold to an investment company. The complex is located directly west of the CCAE. The complex is anchored by a 16-screen Regal Cinema and surrounded by various ancillary office, retail, and restaurant uses including Starbucks, Cold Stone Creamery, Café Socrates, and Juice It Up.
- **Palomar Medical Center** – The existing facility (Palomar East) is located in downtown Escondido and will be renovated and transformed into a "specialty" hospital. The facility has approximately 370,000 SF of building area. Under the proposed renovation plan, approximately 39,000 SF will be remodeled and 15,700 SF of new building area will be constructed. The Palomar Pomerado Health District has received approval for expansion of their operations to a 40-acre site at the Escondido Research and Technology Center. The Health District plans to build the new campus in two phases and be entirely complete by 2010.
- **Lowe's Home Improvement Warehouse** – the approximately 140,000-SF warehouse will be constructed at the corner of Mission Avenue and Quince Street. The approximately 19-acre development site would also include 150 townhomes.
- **Residential** – There are several residential developments planned or proposed in the downtown area. They consist of the following:
  - Barratt American is currently under construction on City Square, a 102-unit townhome project between Centre City Parkway, Orange Street, and Second Avenue. Models are expected to be available for viewing in early 2007.
  - San Diego-based developer CityMark has proposed a 95-unit condominium development on a public parking lot at Second Avenue between Broadway and Maple Street.

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 5

- Kevin DeFreitas Architects, a San Diego design-builder, commenced construction this summer on 15 detached units near Grape Day Park.
- DR Horton is developing The Paramount, a former Barratt American project, consisting of a 122-unit condominium complex, currently under construction on the former Palomar Lanes site.

**C. California Center for the Arts, Escondido (CCAIE)**

The CCAIE opened in 1994, and is situated on a 12-acre site. The CCAIE campus is located just north of the subject Site. The CCAIE consists of a 25,000-SF conference center facility (10,000 SF of useable space) that provides a venue for various conference and performance groups on both a local and national level. The CCAIE includes the following key components:

- Concert Hall – 1,535-seat performance venue
- Center Theater – 408-seat performance venue
- Museum – contemporary art exhibition venue, including three galleries and four studios
- Conference Center – 10,000-SF of useable meeting and conference facility space

**IV. Proposed Development**

Table 1 describes the proposed hotel development. It is planned to contain approximately 118,000 SF of gross building area (GBA) on the 2.29-acre Site. The proposed development is a full-service Marriott brand hotel consisting of 196 rooms, meeting space, and a restaurant in a seven-story Type I structure. In addition, the hotel will contain 220 parking spaces, of which 209 will be provided in a two-level subterranean garage with an additional 11 surface spaces. As part of the Project, the Developer will refurbish the conference center of the CCAIE and incorporate it as part of the hotel operations.

**V. Proposed Deal Terms**

The transaction terms between the City and the Developer are included in the proposed DDA that is under consideration by the City. Key business terms include:

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 6

**A. City Contribution**

The City will contribute a total of \$15,226,000 as follows:

- The City Purchase Price for Subterranean Parking (maximum) of \$9,226,000. This amount will be contributed at the time of the City conveys a fee simple interest to the Developer in the Site to construct the hotel subterranean parking. The construction lender will submit monthly disbursement reports to the City and Developer.
- The Covenant Acquisition Consideration of \$6,000,000. The City will contribute this amount at the time the City leases the Site to the Developer as improved with the subterranean parking. This consideration is for the Developer's agreement to be bound by the covenants set forth in the DDA.

The following table itemizes the City's financial contribution to the development.

| <b>Sources</b>   | <b>Totals</b>       |
|--|---------------------|
| City Purchase Price for Subterranean Parking (maximum) | \$9,226,000         |
| Covenant Acquisition Consideration                     | \$6,000,000         |
| <b>Total City Contribution (maximum)</b>               | <b>\$15,226,000</b> |

**B. Compensation to City**

- The City will lease the Site and existing conference center to the Developer for a period of 55 years. For the first 10-year period from the date the hotel commences operation, no rent will be payable. Beginning in Year 11 the Base Rent will be one percent (1%) of hotel gross revenues and will increase one percent (1%) each year beginning in Year 12 and ending in Year 17 at a maximum of 7% for Years 17-55. The following table summarizes the rent schedule:

To: Jack Anderson, Assistant City Manager  
Subject: Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 7

| <b>Operating Year</b> | <b>Base Rent<br/>(% of Gross Revenue)</b> |
|-----------------------|---|
| 0 - 10                | 0%  |
| 11                    | 1%  |
| 12                    | 2%  |
| 13                    | 3%  |
| 14                    | 4%  |
| 15                    | 5%  |
| 16                    | 6%  |
| 17 - 55               | 7%  |

- KMA has prepared a 55-year operating cash flow for the Project and estimates that the City will receive total ground rent of \$7,731,000 in present value terms (based on a 8.0% discount rate).
- The City will receive Additional Rent for any year where actual gross revenue exceeds the pro forma gross revenues by more than one million dollars. The Additional Rent will be equal to 5.0% of the gross revenue in excess of the pro forma revenue.
- After the Developer has received repayment in full of the equity investment and a compounded 20% return, the City will receive 65% of project cash flow and net proceeds from any refinancing or sale until the earlier of the following: (1) the City has received its original contribution (\$15,226,000) plus 4% compounded interest, or (2) the 26<sup>th</sup> anniversary of the commencement of operation of the hotel.

**C. Other Transaction Terms**

- The Developer agrees to continuously use and operate the hotel for a period of 55 years from the date on which the Project commences operations.
- The Developer and any subcontractors will comply with all governmental requirements applicable to public works, including the payment of prevailing wages.
- The Developer may seek New Market Tax Credits (NMTC) to assist with financing the Project. NMTCs are Federal tax credits that are provided in connection with qualified investments in certain low-income communities in hope of effecting

economic development. In the event that the Developer receives NMTCs, it will pay to the City 25% of the NMTC proceeds. The balance of the proceeds will be used to offset the Project equity. The Developer agrees that it will not accept or utilize NMTCs in a financing structure that does not reduce the Project equity requirement.

*D. Other Revenues to the City/Agency*

- In addition to the above, the City and/or its Redevelopment Agency will receive various tax revenues from the Project, e.g., transient occupancy tax, tax increment/property tax, sales tax, etc. KMA estimates the present value of this revenue over the 55-year term of the lease to be \$19,620,000, using an 8.0% discount rate. This projection can be broken out as follows:

| <b>Tax Revenue Source</b>                   | <b>Total</b>        |
|---|---------------------|
| Transient Occupancy Tax                     | \$12,504,000        |
| Sales Tax                                   | \$4,552,000         |
| Tax Increment/Property Tax <sup>(1)</sup>   | \$1,877,000         |
| Low/Moderate Housing Set-Aside              | \$686,000           |
| <b>Total Tax Revenues <sup>(2)(3)</sup></b> | <b>\$19,620,000</b> |

(1) Net of pass-throughs to other taxing agencies and low/moderate housing set-aside.

(2) Allow for rounding error.

(3) Includes both direct and indirect tax revenues.

**VI. Financial Feasibility Analysis**

The following presents KMA's analysis of the Project's financial feasibility. The analysis takes into consideration the City's contribution toward the Project of \$15,226,000.

Tables 2 to 4 present KMA's financial analysis of the Project.

*A. Development Costs*

In calculating the direct costs of the development, KMA reviewed the pro forma submitted by the Developer in light of our experience with similar projects, and our knowledge of the industry and found them to be representative of today's market. As shown in Table 2, KMA's estimate of total costs for the Project, excluding land, are estimated at \$56,318,000, or \$475 per SF GBA. These include the following:

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 9

- Parking construction costs, consisting of site preparation, garage construction, and related indirect and financing costs, are estimated to be \$9,226,000, or nearly \$42,000 per space. These costs are inclusive of the requirement to pay prevailing wages.
- Direct construction costs, such as site preparation, shell construction, tenant improvements, conference center improvements, FF&E, and contingency, are estimated to be \$35,766,000, or \$302 per SF GBA. These costs are inclusive of the requirement to pay prevailing wages.
- Indirect costs, such as architecture and engineering, permits and fees, legal and accounting, taxes and insurance, developer fee, marketing and pre-opening expense, and contingency, are projected to be \$7,305,000, or 20.4% of direct costs.
- Financing costs, consisting of loan fees and interest during construction, are estimated to be \$4,021,000, or 11.2% of direct costs.

**B. Net Operating Income**

Table 3 presents KMA's estimate of Net Operating Income (NOI) for the Project. KMA based revenue projections on information provided by the Developer and a market study by PKF Consulting. KMA found this information to be reflective of the current marketplace for the type of hotel proposed. As shown, total stabilized annual NOI for the Project is estimated at \$3,840,000. This NOI projection is based on the following assumptions for the stabilized year (Year 4):

- An average daily rate (ADR) for the hotel of \$155 per night at a 74% occupancy rate.
- Parking revenue at \$122 per space per month.
- Other revenue, such as food and beverage, telephone revenue, and rental revenue, equal to about 70% of room revenue.
- Departmental, overhead, and fixed expenses totaling approximately 73% of gross income.

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 10

Based on the assumptions discussed above, the anticipated annual NOI for the hotel is estimated at \$3,840,000 at stabilization.

*C. Internal Rate of Return*

The Developer has indicated a target internal rate of return (IRR) for the Project of 20.0%. Based on current industry standards, KMA believes a leveraged IRR in the mid-to high teens is an appropriate target. The return requirement for the Project should consider the specific risks associated with developing a Type I high-rise hotel in a pioneering market. As indicated in Table 4, the Project is projected to yield a leveraged IRR of 17.1%, based on current estimates of development costs, revenue projections, total City contribution (\$15,226,000), and the Developer's equity investment (\$4,485,000). The Developer's indicated IRR is within today's industry standard, and therefore KMA finds that the proposed City financial contribution is warranted.

**VII. Limiting Conditions**

The estimates of value contained in this memorandum assume compliance with the following assumptions:

1. There are no soil or subsoil problems, including toxic or hazardous conditions on the site that need to be remediated in order to develop the Site.
2. The ultimate development will not vary significantly from that assumed in this analysis.
3. The title of the property is good and marketable; no title search has been made, nor have we attempted to determine the ownership of the property. The value estimates are given without regard to any questions of title, boundaries, encumbrances, liens or encroachments. It is assumed that all assessments, if any, are paid.
4. The site will be in conformance with the applicable zoning and building ordinances.
5. Information provided by such local sources as governmental agencies, financial institutions, realtors, buyers, sellers, and others was considered in light of its source, and checked by secondary means.

**To:** Jack Anderson, Assistant City Manager  
**Subject:** Civic Center Hotel - Review of Proposed Transaction

August 17, 2006  
Page 11

6. Neither the local nor national economy will experience a major recession. If an unforeseen change occurs in the economy, the conclusions contained herein may no longer be valid.
7. The development will adhere to the schedule of performance described in the DDA.
8. Both parties are well informed and well advised and each is acting prudently in what he/she considers his/her own best interest.
9. The lessor is a public agency having definite controls over the development. The Developer must contend with a series of regulations and controls of which many are not common in the conventional real estate market.
10. No assurances are provided by KMA as to the certainty of the projected tax increment revenues shown in this document. Actual revenues may be higher or lower than what has been projected and are subject to valuation changes resulting from new developments or transfers of ownership not specifically identified herein, actual resolution of outstanding appeals, future filing of appeals, or the non-payment of taxes due. The projection reflects KMA's understanding of the assessment and tax apportionment procedures employed by the County.

attachments

**TABLE 1****PROJECT DESCRIPTION  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

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**I. Site Area**

|                        |                  |
|------------------------|------------------|
| Hotel Site             | 50,094 SF        |
| Conference Center Site | <u>49,658 SF</u> |
| Total Site             | 99,752 SF        |
|                        | 2.29 Acres       |

**II. Gross Building Area**

|   |                  |              |
|---|------------------|--------------|
| Hotel Rooms   | 93,588 SF        | 79.0%        |
| Meeting Rooms   | 1,300 SF         | 1.1%         |
| Restaurant  | 2,700 SF         | 2.3%         |
| Lobby/Lounge  | 5,000 SF         | 4.2%         |
| Other Common Area/First Floor Circulation/Back of House | <u>15,900 SF</u> | <u>13.4%</u> |
| Subtotal Gross Building Area (GBA)                      | 118,488 SF       | 100.0%       |
| Floor Area Ratio (FAR)                                  | 1.2              |              |
| Conference Center (Gross SF)                            | 25,000 SF        |              |

**III. Number of Rooms**

|                            |           |
|----------------------------|-----------|
| Number of Guest Rooms      | 196 Rooms |
| Average Room Size - Net SF | 477 SF    |
| Number of Meeting Rooms    | 2 Rooms   |
| Number of Floors           | 7 Floors  |

**IV. Parking****Parking Area**

Total Parking Area 78,370 SF

**Parking**

|                          |                     |
|--------------------------|---------------------|
| Parking under Hotel      | 209 Spaces          |
| Surface Parking at Hotel | <u>11 Spaces</u>    |
| Total Parking Spaces     | 220 Spaces          |
| Average SF per Space     | 356 SF per Space    |
| Parking Ratio            | 1.1 Spaces per Room |

**TABLE 2**

**DEVELOPMENT COSTS  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

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|  | <u>Total</u>       | <u>Comments</u>                  |
|--|--------------------|----------------------------------|
| <b><u>City Parking Costs</u></b>       |                    |                                  |
| <b>I. Direct Costs (1)</b>             |                    |                                  |
| Parking under Hotel - City             | \$7,140,000        | \$34,163 Per Space - Under Hotel |
| Site Preparation                       | \$795,000          | \$3,614 Per Space                |
| Surface Parking at Hotel               | \$0                | Included Above                   |
| Contingency                            | <u>\$231,000</u>   | 2.9% of Directs                  |
| <b>Total Direct Costs</b>              | <b>\$8,166,000</b> | <b>\$37,118 Per Space</b>        |
| <b>II. Indirect Costs</b>              |                    |                                  |
| Architecture & Engineering             | \$280,000          | 3.4% of Directs                  |
| Permits & Fees (2)                     | \$259,000          | \$3 Per SF GBA                   |
| Legal & Accounting                     | \$37,000           | 0.5% of Directs                  |
| Taxes & Insurance                      | \$160,000          | 2.0% of Directs                  |
| Marketing/Pre-Opening Expense          | \$11,000           | 0.1% of Directs                  |
| Developer Fee                          | <u>\$306,000</u>   | 3.7% of Directs                  |
| <b>Total Indirect Costs</b>            | <b>\$1,053,000</b> | <b>12.9% of Directs</b>          |
| <b>III. Financing Costs</b>            |                    |                                  |
| Interest During Construction/Loan Fees | <u>\$7,000</u>     | 0.1% of Directs                  |
| <b>Total City Parking Costs</b>        | <b>\$9,226,000</b> | <b>\$41,936 Per Space</b>        |

(1) Reflects the payment of prevailing wages.

(2) Per Developer. Not verified by KMA or City.

**TABLE 2**

**DEVELOPMENT COSTS  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

|                                      | <u>Total</u>        | <u>Comments</u>         |
|--------------------------------------|---------------------|-------------------------|
| <b><u>Developer Costs</u></b>        |                     |                         |
| <b>I. Direct Costs (1)</b>           |                     |                         |
| Off-Sites                            | \$255,000           | \$5 Per SF Hotel Site   |
| On-Sites                             | \$1,747,000         | \$35 Per SF Hotel Site  |
| Relocate Generator/Cooling Tower     |                     | Assumed w/ City         |
| Shell Construction - Hotel (2)       | \$24,588,000        | \$208 Per SF GBA        |
|                                      |                     | \$125,449 Per Room      |
| Conference Center Improvements       | \$802,000           | \$32 Per SF - Center    |
| FF&E                                 | \$7,197,000         | \$36,719 Per Room       |
| Contingency                          | <u>\$1,177,000</u>  | 3.4% of Directs         |
| Total Direct Costs                   | \$35,766,000        | \$302 Per SF GBA        |
|                                      |                     | \$182,480 Per Room      |
| <b>II. Indirect Costs</b>            |                     |                         |
| Architecture & Engineering           | \$1,691,000         | 4.7% of Directs         |
| Permits & Fees (3)                   | \$1,168,000         | \$10 Per SF GBA         |
| Legal & Accounting                   | \$188,000           | 0.5% of Directs         |
| Taxes & Insurance                    | \$1,069,000         | 3.0% of Directs         |
| Marketing/Pre-Opening Expense        | \$1,397,000         | \$7,128 Per Room        |
| Developer Fee                        | \$1,792,000         | 5.0% of Directs         |
| Contingency                          | <u>\$0</u>          | Included Above          |
| Total Indirect Costs                 | \$7,305,000         | 20.4% of Directs        |
| <b>III. Financing Costs</b>          |                     |                         |
| Interest During Construction         | \$2,159,000         | 6.0% of Directs         |
| Loan Fees                            | \$712,000           | 2.0% of Directs         |
| Operating Deficit Reserves           | <u>\$1,150,000</u>  | 3.2% of Directs         |
| Total Financing Costs                | \$4,021,000         | 11.2% of Directs        |
| <b>IV. Total Development Costs</b>   |                     |                         |
|                                      | <b>\$47,092,000</b> | <b>\$397 Per SF GBA</b> |
| <hr/>                                |                     |                         |
| <b>Grand Total Development Costs</b> | <b>\$56,318,000</b> | <b>\$475 Per SF GBA</b> |

(1) Reflects the payment of prevailing wages.

(2) Includes Developer portion of site excavation and building foundation.

(3) Per Developer. Not verified by KMA or City.



TABLE 1

**PROPOSED FINANCING SOURCES AND USES  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

| Proposed Uses       | Proposed Sources                             |
|---------------------|--|
| Land Acquisition    | Construction Loan                            |
| Direct Costs        | Developer Equity                             |
| Indirect Costs      | Covenant Acquisition Consideration           |
| Financing Costs     | City Purchase Price for Subterranean Parking |
| <b>Total Uses</b>   | <b>Total Sources</b>                         |
| \$0                 | \$36,607,000                                 |
| \$43,932,000        | \$4,485,000                                  |
| \$8,358,000         | \$6,000,000                                  |
| <u>\$4,028,000</u>  | <u>\$9,226,000</u>                           |
| <b>\$56,318,000</b> | <b>\$56,318,000</b>                          |

| Itemization of City Financial Contribution   | Estimated Cost      |
|--|---------------------|
| Covenant Acquisition Consideration           | \$6,000,000         |
| City Purchase Price for Subterranean Parking | <u>\$9,226,000</u>  |
| <b>Subtotal City Contribution</b>            | <b>\$15,226,000</b> |
| Add: Off-site Infrastructure Related Costs   | <u>\$1,260,000</u>  |
| <b>Total City Contribution</b>               | <b>\$16,486,000</b> |

**TABLE 2**

**SUMMARY OF ECONOMIC BENEFITS  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

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| <b>Estimated Annual Tax Revenue to City/Redevelopment Agency (1)<br/>Stabilized Year 4</b> |                    |
|--|--------------------|
| <b><u>Revenue Sources</u></b>  |                    |
| Property Tax / Tax Increment (2)   | \$250,000          |
| Housing Set-Aside  | \$76,000           |
| Transient Occupancy Tax (TOT)  | \$821,000          |
| Sales Tax  | <u>\$137,000</u>   |
| <b>Total Hotel Sources</b>   | <b>\$1,284,000</b> |

(1) Figures have been rounded.

(2) Proceeds to the City/Agency net of pass-through agreements and housing set-aside. Assumes that method of site conveyance will trigger a fee-equivalent Assessed Value based on the income approach to value.

Prepared by: Keyser Marston Associates, Inc.

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TABLE 3

**PROJECTION OF ANNUAL REVENUE TO CITY/CDC  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

| <u>Year (1)</u> | <u>Ground Lease<br/>Payment</u> | <u>Taxes (2)</u> | <u>Total</u> |
|-----------------|---------------------------------|------------------|--------------|
| 2006            | \$0                             | \$0              | \$0          |
| 2007            | \$0                             | \$0              | \$0          |
| 2008            | \$0                             | \$1,059,000      | \$1,059,000  |
| 2009            | \$0                             | \$1,172,000      | \$1,172,000  |
| 2010            | \$0                             | \$1,256,000      | \$1,256,000  |
| 2011            | \$0                             | \$1,284,000      | \$1,284,000  |
| 2012            | \$0                             | \$1,306,000      | \$1,306,000  |
| 2013            | \$0                             | \$1,217,000 (3)  | \$1,217,000  |
| 2014            | \$0                             | \$1,252,000      | \$1,252,000  |
| 2015            | \$0                             | \$1,288,000      | \$1,288,000  |
| 2016            | \$0                             | \$1,324,000      | \$1,324,000  |
| 2017            | \$0                             | \$1,362,000      | \$1,362,000  |
| 2018            | \$174,000                       | \$1,401,000      | \$1,575,000  |
| 2019            | \$358,000                       | \$1,440,000      | \$1,798,000  |
| 2020            | \$553,000                       | \$1,481,000      | \$2,034,000  |
| 2021            | \$759,000                       | \$1,522,000      | \$2,281,000  |
| 2022            | \$978,000                       | \$1,565,000      | \$2,543,000  |
| 2023            | \$1,208,000                     | \$1,609,000      | \$2,817,000  |
| 2024            | \$1,452,000                     | \$1,655,000      | \$3,107,000  |
| 2025            | \$1,496,000                     | \$1,503,000 (4)  | \$2,999,000  |
| 2026            | \$1,541,000                     | \$1,548,000      | \$3,089,000  |
| 2027            | \$1,587,000                     | \$1,593,000      | \$3,180,000  |
| 2028            | \$1,634,000                     | \$1,640,000      | \$3,274,000  |
| 2029            | \$1,683,000                     | \$1,689,000      | \$3,372,000  |
| 2030            | \$1,734,000                     | \$1,738,000      | \$3,472,000  |
| 2031            | \$1,786,000                     | \$1,789,000      | \$3,575,000  |
| 2032            | \$1,840,000                     | \$1,842,000      | \$3,682,000  |
| 2033            | \$1,895,000                     | \$1,897,000      | \$3,792,000  |
| 2034            | \$1,952,000                     | \$1,954,000      | \$3,906,000  |
| 2035            | \$2,010,000                     | \$2,011,000      | \$4,021,000  |
| 2036            | \$2,070,000                     | \$2,071,000      | \$4,141,000  |
| 2037            | \$2,133,000                     | \$2,132,000      | \$4,265,000  |
| 2038            | \$2,197,000                     | \$2,184,000      | \$4,391,000  |
| 2039            | \$2,262,000                     | \$2,260,000      | \$4,522,000  |
| 2040            | \$2,330,000                     | \$2,327,000      | \$4,657,000  |
| 2041            | \$2,400,000                     | \$2,396,000      | \$4,796,000  |
| 2042            | \$2,472,000                     | \$2,466,000      | \$4,938,000  |
| 2043            | \$2,546,000                     | \$2,539,000      | \$5,085,000  |
| 2044            | \$2,623,000                     | \$2,614,000      | \$5,237,000  |
| 2045            | \$2,701,000                     | \$2,691,000      | \$5,392,000  |
| 2046            | \$2,782,000                     | \$2,771,000      | \$5,553,000  |
| 2047            | \$2,866,000                     | \$2,853,000      | \$5,719,000  |
| 2048            | \$2,952,000                     | \$2,937,000      | \$5,889,000  |
| 2049            | \$3,040,000                     | \$3,025,000      | \$6,065,000  |
| 2050            | \$3,132,000                     | \$3,115,000      | \$6,247,000  |
| 2051            | \$3,226,000                     | \$3,207,000      | \$6,433,000  |
| 2052            | \$3,322,000                     | \$3,302,000      | \$6,624,000  |
| 2053            | \$3,422,000                     | \$3,399,000      | \$6,821,000  |
| 2054            | \$3,525,000                     | \$3,500,000      | \$7,025,000  |

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**TABLE 3**

**PROJECTION OF ANNUAL REVENUE TO CITY/CDC  
CIVIC CENTER HOTEL  
CITY OF ESCONDIDO**

---

| <u>Year (1)</u>             | <u>Ground Lease<br/>Payment</u> | <u>Taxes (2)</u>     | <u>Total</u>         |
|-----------------------------|---------------------------------|----------------------|----------------------|
| 2055                        | \$3,631,000                     | \$3,604,000          | \$7,235,000          |
| 2056                        | \$3,739,000                     | \$3,710,000          | \$7,449,000          |
| 2057                        | \$3,852,000                     | \$3,821,000          | \$7,673,000          |
| 2058                        | \$3,967,000                     | \$3,934,000          | \$7,901,000          |
| 2059                        | \$4,086,000                     | \$4,051,000          | \$8,137,000          |
| 2060                        | \$4,209,000                     | \$4,170,000          | \$8,379,000          |
| <hr/>                       |                                 |                      |                      |
| <b>Future Value</b>         | <b>\$100,125,000</b>            | <b>\$117,486,000</b> | <b>\$217,611,000</b> |
| <b>Present Value (2006)</b> | <b>\$7,731,000</b>              | <b>\$17,187,000</b>  | <b>\$24,918,000</b>  |
| <b>Discount Rate 8.0%</b>   |                                 |                      |                      |

(1) 55-year ground lease, i.e., two years of construction and 53 years of operations.

(2) No assurances are provided by KMA as to the certainty of the projected tax revenues shown in this document. The projection reflects KMA's understanding of the assessment and tax apportionment procedures employed by the County.

(3) Pass-throughs to other taxing agencies assumed to commence in 2013.

(4) Redevelopment Plan expires in 2024. City receives 14.46% of the 1.0% property tax beginning in 2025.

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