APPLIED ECONOMICS

ECONOMIC AND REVENUE IMPACTS OF 5TH AND CONGRESS ON THE CITY OF TUCSON

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1.0 INTRODUCTION

Applied Economics was retained by the City of Tucson to perform an economic impact analysis of the 5th and Congress mixed use development. The development includes a 147 room boutique hotel, 5,400 square feet of neighborhood and specialty retail and 10,050 square feet of restaurant space with three new restaurants. The retail and restaurants would be located on the ground floor of the hotel. There would also be 3,000 square feet of roof space that would be developed to accommodate a commercial business.

The project would be eligible for a Government Property Lease Excise Tax (GPLET) agreement which would result in the abatement of all real property taxes and lease excise taxes during the first eight years following construction. This analysis is intended to provide a framework for understanding the economic and revenue impacts the project would have on the city.

1.1 Project Description

The proposed hotel development would include 200,000 square feet with 147 rooms (Figure 1). This boutique downtown hotel would be owned and operated a major hotel brand. Occupancy rates are projected to increase from 63 percent in the first year of operations to a long term rate of 72 percent as the hotel gains market share. The project will provide much needed downtown hotel space for major events. In addition, it will include three restaurants with combined taxable sales of $5.6 million per year, 5,400 square feet of street level retail space with taxable sales of $2.4 million per year, and 3,000 square feet of additional roof space with $1.7 million in annual taxable sales. All total, the project would create an estimated 219 new jobs and $16.1 million in annual taxable sales. *Note that these estimates exclude the parking garage which would be owned by the Rio Nuevo District and is not part of the GPLET application.*

FIGURE 1
DEVELOPMENT ASSUMPTIONS

	Cumulative Square Feet	Hotel Rooms	Estimated Jobs	Avg Daily Room Rate	Hotel Occupancy	Hotel Other Rentals	Hotel Utilities	Other Retail & Restaurant Sales
2015	6,300	0	52	$0	0%	$84,000	$0	$2,750,000
2016	218,450	147	219	$135	63%	$96,875	$194,905	$4,821,250
2017	218,450	147	219	$139	69%	$109,750	$203,579	$4,821,250
2018	218,450	147	219	$143	71%	$122,625	$212,253	$4,821,250
2019	218,450	147	219	$147	72%	$135,500	$220,926	$4,821,250
2020	218,450	147	219	$151	72%	$135,500	$229,600	$4,821,250

Note: Pro-forma excludes parking garage which will be owned by Rio Nuevo.

2.0 IMPACT SUMMARY

The construction of this hotel/retail project in Downtown Tucson would provide significant economic benefits within this blighted area. The proposed hotel will complement the other commercial development in the 5th and Congress project and will allow this site to develop to its full potential.

- About 220 direct construction jobs and 140 additional indirect jobs would be supported in the City of Tucson during the construction period. The total construction impact is estimated at $40.6 million.

- Once completed, the project could generate an average annual economic impact of $22.9 million, or a total of $187.6 million over the next eight years.

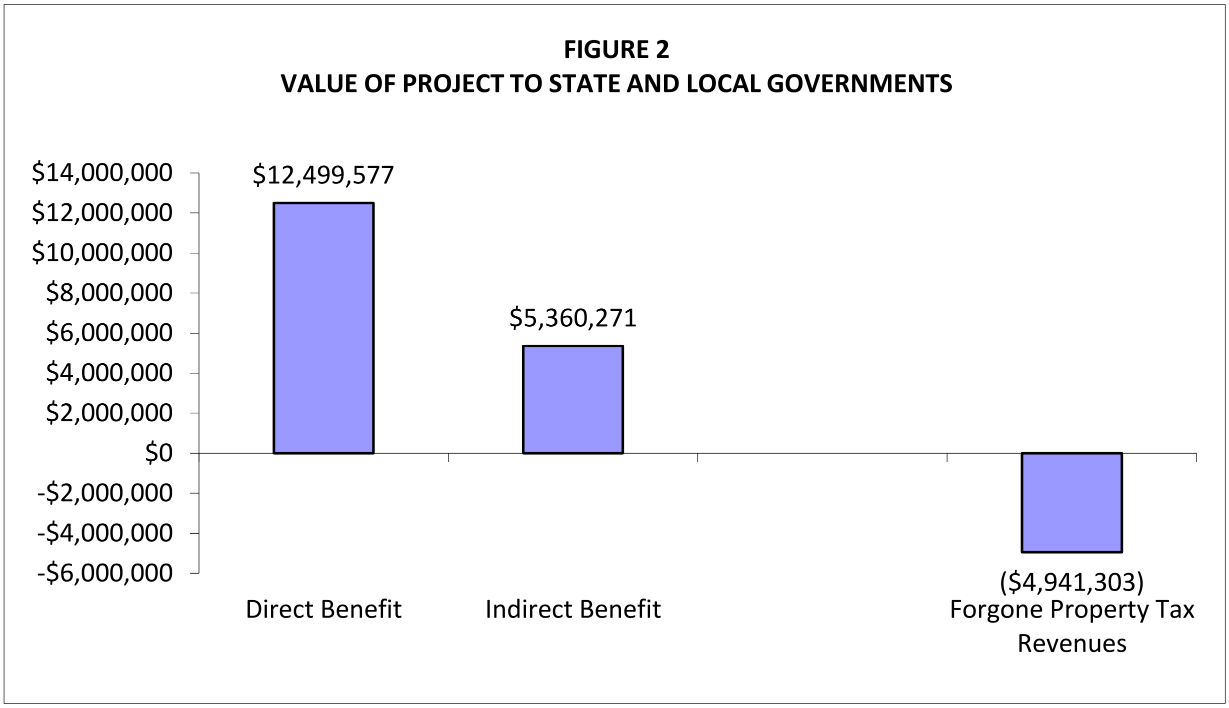
- The hotel would directly support about 55 jobs, and the restaurants and retail would add another 164 jobs. The project could also support an additional 100 indirect jobs at *other local businesses* in Tucson. These indirect jobs are the result of business to business purchases made by the hotel, as well as local spending by employees.

- An estimated $4.5 million in direct personal income, or payroll, and an average of $7.2 million in total direct and indirect personal income would be generated by the development annually, creating the potential for significant local expenditures by employees and their families.

- In terms of local tax revenues, the hotel, retail and restaurants that are part of 5th and Congress would directly and indirectly generate approximately $4.6 million in local revenues to the City of Tucson from 2015 to 2023 (net of local sales tax incentives), $3.6 million to the county, school district and other local taxing jurisdictions and $9.6 million to the state. Indirect revenues include taxes paid by employees, whereas direct revenues are generated by businesses in the development.

- The project could qualify for a GPLET with a term of 8 years, which would exempt all real property taxes to the city and other local governments. These exemptions are included in the revenue impacts above. The value of this exemption for all jurisdictions combined is estimated at $4.9 million over eight years. However, during the term of the GPLET the project would generate direct sales tax from on-going retail and bed taxes, direct personal property taxes and indirect property and sales taxes from supported employees, for a total benefit to the state and local governments of $17.9 million over eight years. Thus, the benefit to the city, county, state and school districts would significantly exceed the value of the GPLET property tax exemption.

- Once the GPLET term ends in 2024, the project would continue to generate revenues to state and local governments including an estimated $835,000 per year in direct property, sales and bed tax revenues to the city and $650,000 to the county, school districts and other special districts. This is in addition to the $451,000 in estimated annual indirect revenues to local governments.



The proposed mixed use project would generate new revenues for the city, as well as creating approximately 220 new jobs in the downtown area. The hotel will help Tucson compete for annual events and conventions and provide much needed additional rooms in the downtown area. The nature of the restaurants and retail in this development, combined with numerous public events and performances at the nearby Rialto Theatre will attract additional Tucson residents and visitors into the downtown area for dining and entertainment. Other local businesses could benefit as well from this synergistic effect. The 5th and Congress development would support the local economy while providing an anchor for redevelopment activity in eastern end of downtown.

3.0 ECONOMIC IMPACT ANALYSIS

The economic impacts resulting from 5th and Congress include both the one-time construction impacts and on-going operations impacts. These impacts are quantified in terms of direct and indirect jobs, personal income and sales, or output that would be generated by the project. Indirect impacts are the result of the multiplier effect and capture supported supplier and consumer businesses in the City of Tucson that would benefit from the new development. There are additional positive impacts that would occur in other parts of the region that are not captured here.

3.1 Construction Impacts

The proposed construction costs for this mixed-use project are shown in Figure 3. Construction is expected to occur during 2015 and part of 2016. In terms of local economic impacts, the hard costs associated with the project, as well as soft costs that will occur locally, are included in the impact calculations.

FIGURE 3
CONSTRUCTION COSTS FOR 5th AND CONGRESS

Hard Costs	**$22,294,000**
Hotel	$16,550,000
Commercial	$1,200,000
200 Congress	$469,000
Landscaping, Offsites, Contingency	$4,075,000
Soft Costs	**$2,955,000**
Hotel	$2,705,000
Commercial	$150,000
200 Congress	$100,000
FF&E	**$2,100,000**
Total	**$27,349,000**

Note: Costs exclude Menu and parking garage construction.

The total increase in economic activity from new construction expenditures is estimated at $40.6 million, as shown in Figure 4. The project would result in direct construction expenditures, excluding land and equipment, of about $25.2 million. The multiplier effects of this construction spending on the City would result in a total increase in economic activity of about $40.6 million. These impacts are projected to occur during the construction period. The approximately 220 direct jobs and 140 indirect and induced jobs created by this construction activity would result in more than $14.7 million in personal income in the City of Tucson during the next year and a half.

FIGURE 4
CONSTRUCTION IMPACTS OF 5th AND CONGRESS
ON THE CITY OF TUCSON

	Direct Impacts			Total Impacts		
	Expenditures	Jobs	Personal Income	Output	Jobs	Personal Income
Hard Costs	$22,294,000	187	$7,646,839	$35,191,989	302	$12,195,163
Soft Costs	$2,955,000	28	$1,684,027	$5,364,679	52	$2,527,602
Total	$25,249,000	215	$9,330,866	$40,556,667	354	$14,722,765

3.2 Operations Impacts

Once construction is completed, the proposed project will create about 220 jobs. The hotel, retail and restaurants will generate economic impacts through business-to-business spending locally, as well as through employee spending.

The total economic activity from on-going operations of the project is shown in Figure 5. The approximately 220 new jobs and $4.5 million in direct personal income, or payroll, will generate an average of $15.5 million in increased direct output each year. The income from these jobs is estimated at about $21,000 per employee. Annual impacts are phased in as hotel gains market share and as occupancy and room rates.

FIGURE 5
ECONOMIC IMPACTS OF 5th AND CONGRESS
ON CITY OF TUCSON

	Direct Impacts			Total Impacts		
	Output	Jobs	Personal Income	Output	Jobs	Personal Income
2015	$2,750,000	52	$956,800	$4,232,199	64	$1,394,360
2016	$8,555,678	219	$4,509,135	$13,324,710	179	$6,044,280
2017	$14,871,327	219	$4,509,135	$23,224,559	303	$7,210,387
2018	$15,184,917	219	$4,509,135	$23,721,004	308	$7,271,668
2019	$15,428,412	219	$4,509,135	$24,106,480	312	$7,319,251
2020	$15,595,390	219	$4,509,135	$24,370,823	314	$7,351,882
2021	$15,749,493	219	$4,509,135	$24,614,784	317	$7,381,996
2022	$15,903,596	219	$4,509,135	$24,858,745	319	$7,412,111
2023	$16,057,699	219	$4,509,135	$25,102,706	322	$7,442,226
8 Year Total	$120,096,511	219	$37,029,880	$187,556,010	322	$58,828,161

The multiplier effect of this increase in business activity in the City will result in a total annual output impact of $25.1 million by 2023, or a total of $187.6 million over the next eight years. The approximately 100 direct, indirect and induced jobs supported by the development will result in about $7.4 million in annual personal income in Tucson by 2023, or a total of $58.8 million over the next eight years.

The jobs generated by this project would support a total local population of about 560 people in the City of Tucson, based on local commuting patterns. Supported population includes families of direct employees, as well as families of employees at related supplier and consumer businesses. This estimate assumes that about 79 percent of the employees will live and work in Tucson, based on local commuting data from the American Community Survey.

The differences between direct and total economic impacts are called multiplier effects. Multiplier effects are a way of representing the larger economic effects on the local economy. The multiplier effects translate an increase in output or business sales/production into a corresponding increase in jobs and personal income. The total increase in output includes the impacts on other local supplier and consumer businesses. In essence, the multiplier effect represents the recycling of local spending. This process creates new business opportunities.

The multipliers used in this analysis are from IMPLAN, a national vendor of economic impact software, and are specific to the City of Tucson. Industry specific multipliers were used for the hotels, retail, restaurants and commercial construction. The average output multiplier for this mixed use development is 1.56. This means that for every $1 million of annual output created by the development, an additional $560,000 in economic activity and 6 local jobs are supported at other local businesses outside the development. On average, the income from these indirect jobs is estimated at about $29,000 per employee. Additional indirect jobs and payroll would be supported in other parts of the metro area.

4.0 REVENUE IMPACTS

In addition to supporting jobs, income and output at related businesses in the city through multiplier effects; the hotel, retail and restaurants in 5th and Congress would also generate significant local tax revenues, primarily from sales and bed taxes. In total, the project could generate approximately $4.6 million in direct and indirect local tax revenues to the City of Tucson from 2015 to 2023 (net of local sales tax incentives), and $13.2 million in additional revenues to the county, RTA, school district and state (Figure 6).

FIGURE 6
STATE AND LOCAL REVENUE IMPACTS
5th AND CONGRESS

	City of Tucson				County, RTA and Schools			State of Arizona			
	Property[1]	Sales	Bed Tax	Total Benefit	Property[2]	Sales	Total Benefit	Sales	Pers Income	Total Benefit	Total Public Benefit
Direct Impacts	**$12,079**	**$1,863,325**	**$2,184,636**	**$4,060,040**	**$122,939**	**$681,688**	**$804,627**	**$7,634,910**	**$0**	**$7,634,910**	**$12,499,577**
2015 (const)	$0	$0	$0	$0	$0	$86,206	$86,206	$965,502	$0	$965,502	$1,051,707
2016	$1,190	$119,245	$93,630	$214,065	$12,107	$43,753	$55,860	$490,033	$0	$490,033	$759,957
2017	$1,914	$214,716	$271,750	$488,380	$19,481	$75,375	$94,855	$844,195	$0	$844,195	$1,427,430
2018	$2,147	$221,161	$295,562	$518,869	$21,847	$76,986	$98,833	$862,242	$0	$862,242	$1,479,944
2019	$2,233	$255,132	$291,794	$549,159	$22,728	$78,247	$100,974	$876,363	$0	$876,363	$1,526,496
2020	$2,082	$258,645	$298,266	$558,993	$21,187	$79,125	$100,312	$886,199	$0	$886,199	$1,545,504
2021	$1,568	$261,727	$304,739	$568,034	$15,959	$79,895	$95,854	$894,829	$0	$894,829	$1,558,717
2022	$811	$264,809	$311,211	$576,831	$8,255	$80,666	$88,921	$903,459	$0	$903,459	$1,569,211
2023	$135	$267,891	$317,683	$585,710	$1,376	$81,436	$82,812	$912,089	$0	$912,089	$1,580,611
2024 (post-GPLET)	*$55,864*	*$325,746*	*$453,833*	*$835,444*	*$568,576*	*$81,436*	*$650,013*	*$912,089*	*$0*	*$912,089*	*$2,397,545*

	City of Tucson				County and Schools			State of Arizona			
	Property	Sales	Bed Tax	Total Benefit	Property	Sales	Total Benefit	Sales	Pers Income	Total Benefit	Total Public Benefit
Indirect (Employee-Driven)	**$285,761**	**$281,311**	**$0**	**$567,072**	**$2,693,316**	**$89,022**	**$2,782,339**	**$997,051**	**$1,013,809**	**$2,010,860**	**$5,360,271**
2016	$21,591	$29,605	$0	$51,196	$203,497	$9,369	$212,865	$104,929	$133,881	$238,810	$502,871
2017	$36,487	$35,316	$0	$71,803	$343,887	$11,176	$355,063	$125,172	$125,317	$250,489	$677,356
2018	$37,072	$35,617	$0	$72,689	$349,409	$11,271	$360,680	$126,236	$125,498	$251,734	$685,103
2019	$37,527	$35,850	$0	$73,377	$353,696	$11,345	$365,041	$127,062	$125,639	$252,701	$691,119
2020	$37,839	$36,010	$0	$73,849	$356,637	$11,395	$368,032	$127,629	$125,735	$253,364	$695,245
2021	$38,127	$36,157	$0	$74,284	$359,350	$11,442	$370,792	$128,151	$125,824	$253,976	$699,052
2022	$38,415	$36,305	$0	$74,720	$362,063	$11,489	$373,552	$128,674	$125,913	$254,588	$702,859
2023	$38,703	$36,452	$0	$75,155	$364,777	$11,535	$376,312	$129,197	$126,002	$255,199	$706,666
Total Direct and Indirect (2015 to 2023)	**$297,840**	**$2,144,636**	**$2,184,636**	**$4,627,112**	**$2,816,255**	**$770,711**	**$3,586,966**	**$8,631,961**	**$1,013,809**	**$9,645,770**	**$17,859,848**

[1] Based on city property tax rate of 1.4304%. Incorporates depreciation on personal property which is excluded from GPLET.

[2] Based on county/school property tax rate of 14.5584%. Incorporates depreciation on personal property which is excluded from GPLET.

4.1 Direct Revenues

The project would be eligible for a GPLET agreement that would exempt it from real property taxes during the term of the lease. Normally, there would be a lease excise tax in lieu of property taxes, but since the project is located in a redevelopment area and it would result in more than a 100 percent increase in property value, the lease excise taxes would also be exempted over the first eight years of the project. It is anticipated that the GPLET would end after the 8th year and the project would then pay normal real property taxes to the city and other local governments. Once the GPLET expired, the project could generate approximately

$624,000 per year in direct local property taxes. Direct property tax revenues are based on the value of new construction (hard and soft costs) at an 18 percent assessment ratio.[1] It is important to note that the GPLET does not impact personal property taxes and that the property tax revenues shown during the GPLET term from 2016 to 2023 represent taxes on depreciated FF&E. Personal property taxes over the 8 year term are estimated at $12,000 to the city and $123,000 to the county and school district.

In addition to property taxes, the project would generate one-time sales taxes from new construction estimated at $1.2 million for the city, RTA and state combined, of which $290,000 would go to the City of Tucson. The city's portion of construction sales tax is requested to be rebated to cover the cost of infrastructure improvements and is therefore not included in the revenue impact.

There would be on-going sales and bed tax revenues associated with the hotel, retail and restaurants. Sales taxes would be charged on room rentals as well as food and beverage sales, retail sales, other rentals and utilities. It is estimated that the project would generate sales and bed taxes in the amount of $586,000 per year to the city, $81,000 in sales taxes to the RTA and $912,000 in sales taxes to the state by 2023. All total, the project could generate about $12.5 million in direct state and local sales and bed tax revenues from 2015 to 2023. Note that this total excludes any construction sales tax to the city as well as all additional retail sales taxes that are being requested as incentives.

4.2 Indirect Revenues

Along with the direct taxes generated by the project, there are also indirect taxes generated by employees of the hotel. Using the results from the economic impact analysis, it is possible to estimate indirect tax impacts.

Indirect property tax revenues, which represent property taxes on new housing for employees, were based on average residential assessed per capita in Tucson, times the annual supported population, times the average countywide property tax rate of 14.912 percent. On average, indirect property taxes are estimated at about $38,000 per year to the city, and an additional $356,000 per year to the school district, community college and county. All total the project would generate about $3.0 million in indirect property tax revenues to all jurisdictions combined from 2016 to 2023, based on the assumptions used in this analysis.

Indirect sales tax revenues include sales taxes from direct employees and employees at supported local businesses. Indirect sales taxes are estimated based on multiplying total personal income times 31 percent (share of taxable expenditures), times the Tucson live-work ratio of 79 percent, times the sales tax rate.[2] No residency ratio is used for RTA or state indirect sales tax. Indirect city sales taxes average about $36,000 per year, or a total of $281,000 over eight years. Additional sales taxes generated to the RTA and the state are estimated at an average of $11,000 per year, or $89,000 over eight years.

In terms of state personal income tax, direct and indirect employees could generate approximately $1.0 million in revenues from 2016 to 2023. State income tax revenues are

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[1] *Post-GPLET property taxes are calculated as follows (hard costs + soft costs + FF&E) *85% * 18% * mill rate.*

[2] *According to the Census Bureau Consumer Expenditure Survey persons in the median income range spend about 31 percent of their income on taxable goods.*

calculated using average income per employee and current tax schedules from the Arizona Department of Revenue.

4.3 GPLET Impacts

In addition to calculating revenue impacts to local and state government, this analysis also considers the property tax impacts of the GPLET relative to the amount of benefit to the property owner. A.R.S. 42-6209 requires that the economic and fiscal benefit to the state, county and city in which the government property improvement is located will exceed the benefits received by the prime lessee. The City is proposing an eight year term for the GPLET during which time the developer would pay no lease excise tax or real property tax since the project is located in a redevelopment area and would increase the value of the property by more than 100 percent. After that time, the property owner would pay real property taxes to the city and other taxing jurisdictions at the normal rate.

In order to meet the statutory requirements, it is necessary to show that total revenues to the state, county and city would exceed the value of forgone property taxes during the term of the GPLET. Revenues include direct sales tax revenues from construction (excluding the city portion which is requested as reimbursement to the developer) and on-going sales and bed taxes, as well as indirect property and sales taxes from supported employees. Over the eight year term, the direct and indirect revenues to state and local jurisdictions total $17.9 million (Figure 7). In comparison, the property tax savings to the developer are estimated at $4.9 million over the eight year GPLET term, of which $442,000 would have gone to the City of Tucson.[3] The value of other tax revenues generated by the project exceeds the property tax savings from the GPLET by $12.9 million over eight years, thereby meeting the requirements of the statute. In fact, the value of direct tax revenues only would still exceed the property tax savings to the developer by $7.6 million over eight years. If the GPLET agreement extends beyond eight years, the annual lease excise revenues from the project are estimated at $493,800, using current rates. These lease excise tax revenues would be distributed to the city, county, community college and local school district.

[3] *Property value (hard cost + soft cost) is adjusted by 85 percent prior to applying the assessment ratio since construction cost is generally greater than assessed value.*

FIGURE 7
8-YEAR VALUE OF GPLET

	Total Benefit to the City, County, RTA, Schools and State	Benefit to Developer (Property Tax Savings)[1]
Total Direct	**$12,499,577**	**$4,941,303**
2015	$1,051,707	$0
2016	$759,957	$617,663
2017	$1,427,430	$617,663
2018	$1,479,944	$617,663
2019	$1,526,496	$617,663
2020	$1,545,504	$617,663
2021	$1,558,717	$617,663
2022	$1,569,211	$617,663
2023	$1,580,611	$617,663
Total Indirect	**$5,360,271**	**$0**
2016	$502,871	$0
2017	$677,356	$0
2018	$685,103	$0
2019	$691,119	$0
2020	$695,245	$0
2021	$699,052	$0
2022	$702,859	$0
2023	$706,666	$0
8 Year Direct+Indirect	**$17,859,848**	**$4,941,303**

[1] Based on a property tax rate of 15.9888% in tax rate area 0163.

4.4 Summary

The proposed 5th and Congress development described in this analysis could create both economic and revenue benefits for the City of Tucson. This hotel is an important part of the overall development and will provide much needed hotel rooms in the downtown area to support conventions and other major events. The retail and restaurants would provide new dining and shopping opportunities, generating increased visibility and support for other economic development in the Downtown/Gateway area. The project will likely create synergy for additional redevelopment on adjacent properties and will serve to eliminate blight in this part of downtown. The economic benefits include the impacts of construction as well as the on-going operations impacts. The development would support a significant amount of jobs and payroll in the downtown area, and it would create additional demand at other local businesses based on supplier purchases and employee spending.