



Anaheim Hotel Worker Ballot Initiative

Fiscal Impact Analysis





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Executive Summary

The following report analyses the impact of the Hotel Worker Ballot Initiative (HWBI) on the City of Anaheim's Transient Occupancy Tax (TOT) revenue. Beacon Economics finds that the HWBI will have an adverse effect on the long-term financial health of Anaheim's hotel industry. The HWBI will more than double hotel labor costs, some of which will be passed onto guests in the form of higher average daily room rates (ADR). Because of their higher prices, hotels will receive fewer guests and lower occupancy rates, while incurring more expensive operating costs.

However, the HWBI will have a slightly positive impact on the City's TOT revenue over the next two to three years. The TOT is a 15% charge on hotel room revenue. Because Hotels will need to charge higher rates, their rooms will generate more revenue. While these higher rates will lead to a decrease in occupancy rates, the decrease will not fully offset the increased revenue from higher ADR. Therefore, the City's TOT is expected to increase between 0.5% to 2.5% over the next couple of years. For illustration purposes, the City expects TOT revenue to total \$236M for the for the next fiscal year, 2023/2024. Therefore, a 0.5% to 2.5% increase is roughly \$1.2M to \$5.9M. These empirical finding are supported by stakeholder interviews conducted with Hoteliers in Anaheim, case studies on similar regulations implemented in comparable markets, and peer-reviewed academic research^{1,2,3}.

¹ Corgel, Jack; Lane, Jamie; and Woodworth, Mark (2012) "Hotel Industry Demand Curves," *Journal of Hospitality Financial Management*: Vol. 20 : Iss. 1 , Article 6. Available at: <https://scholarworks.umass.edu/jhfm/vol20/iss1/6>

² Hudson, S., Meng, F., So, K. K. F., Smith, S., Li, J., & Qi, R. (2021). The effect of lodging tax increases on US destinations. *Tourism Economics*, 27(1), 205–219. <https://doi.org/10.1177/1354816619890752>

³ Collins, Clay, and E. Frank Stephenson. 2018. "Taxing the Travelers: A Note on Hotel Tax Incidence." *Journal of Regional Analysis & Policy* 48.

While the HWBI will have a slightly positive effect on the City's TOT in the short run, in the long run, HWBI will lower the growth trajectory of TOT and turn the net effect negative. Since the pandemic, the average month-over-month growth rate of TOT has been just over 4%. This growth rate will vary as the industry recovers, but it will likely decrease by 30% to 70% as a result of the HWBI over the next five plus years. This means TOT will be roughly \$4M less with HWBI than it otherwise would be during the 2027/2028 fiscal year. The additional financial strains that the HWBI places on the industry could push some Hotels out of business, and it will lower the attractiveness of Anaheim as a place to invest and build hotels. Thus, the growth in the number of hotels and hotel rooms may dramatically decrease or even stop altogether in the long run.

While outside the scope of this analysis, a depressed tourism market will have adverse indirect impacts on other tax revenue sources as well. For example, increased hotel rates will mean that tourists stay in Anaheim for shorter durations, spend less money in the City, and therefore pay less sales tax. Also, less hotel development will mean less construction spending, and the related direct and indirect economic effects.

The social goals of the bill are laudable. However, policymakers should be very careful about balancing these trade-offs with nurturing the overall tourism market, and they should be cautious about long-term unintended consequences.

Introduction

In May 2023, the City of Anaheim ordered a Fiscal Impact Analysis of the Initiative Petition entitled Hotel and Event Center Minimum Wage, Worker Retention, and Hotel Worker Safety and Workload Initiative – hereafter referred to as the Hotel Worker Ballot Initiative (HWBI). Beacon Economics was commissioned to estimate the impact this bill will have on the City's Transient Occupancy Tax (TOT). The Anaheim TOT is 15% of room sales derived from hotel, motel, and timeshare stays of less than thirty days.

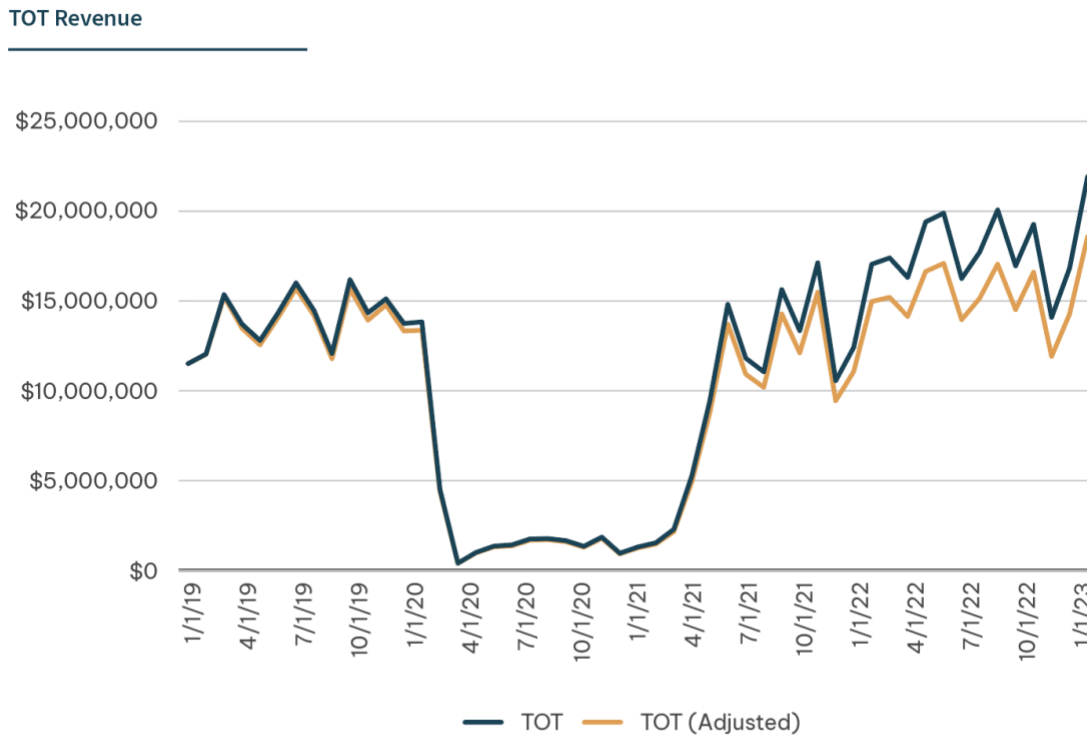
Beacon Economics had limited time to conduct this analysis, but relied on three methods to triangulate the estimates in this analysis. First, we quantified the effects using econometric modeling and conducted robustness checks to ensure the validity of its estimates. Second, we investigated case studies of similar measures implemented in other cities. Third, we conducted interviews with stakeholders in the Anaheim Hotel industry to gather qualitative information on the bill's effects on operating and implementation expenses.

The Anaheim Transient Occupancy Tax

The Transient Occupancy Tax is a crucial source of revenue for the City of Anaheim. During the fiscal year 2021-2022, which runs from July 1st to June 30th, the city collected a record \$177M in TOT. To put this into perspective, over the same period, the Anaheim Police Department cost the City \$148M. For the next fiscal year, 2023/2024, TOT is expected to bring in 42% of all the City's revenues.

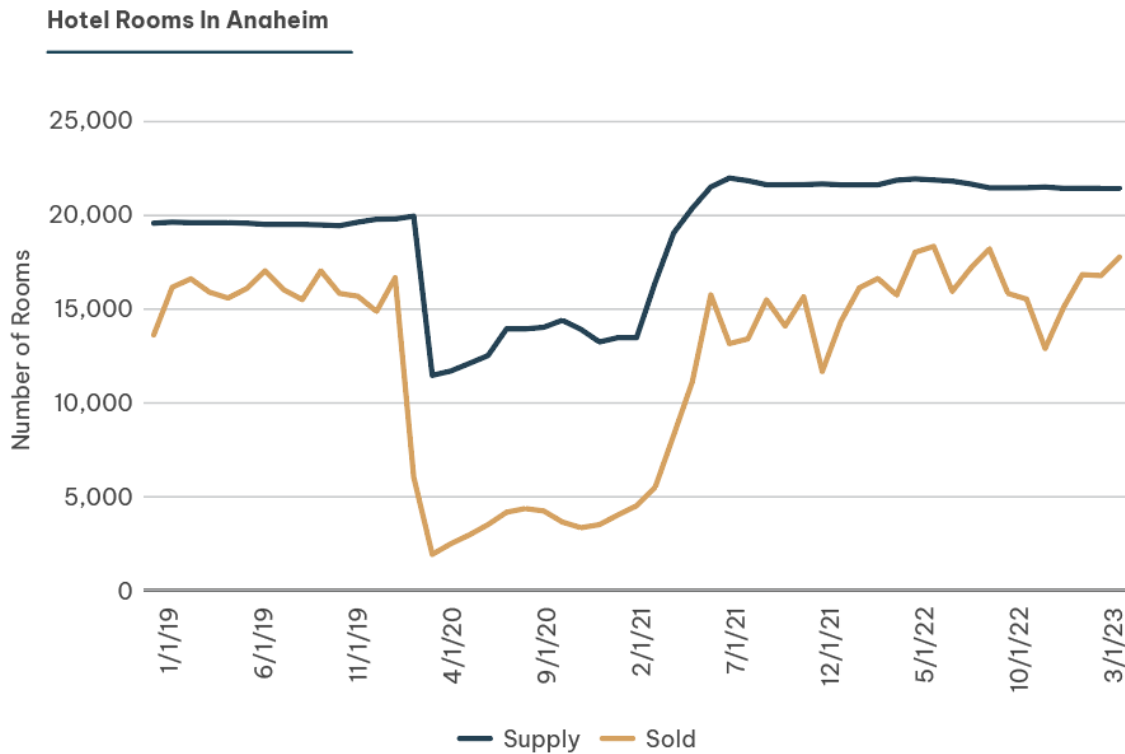
TOT is on track to reach a new high for fiscal year 2022/2023. By June 30th, it should reach roughly \$223M. Next fiscal year, it is expected to reach \$236M, another record high.

There are currently 162 hotels or other lodging establishments in Anaheim that pay TOT. As the figure below illustrates, TOT fell around 90% from March 2020 to May 2022 as a result of COVID-19 restrictions. It has since rebounded. In March 2023, these establishments paid \$21,181,269, the highest monthly total ever recorded. The high numbers can be partially explained by inflation, which has increased by 18% since 2019, the last pre-pandemic year.



Source: City of Anaheim and the Bureau of Labor Statistics; Analysis by Beacon Economics

The reason TOT reached a new high in March is not because of an increase in the number of hotels, available rooms, or the occupancy rate. In fact, as shown in the figure below, the pre-pandemic occupancy rate was in the low eighties, but, since the pandemic, has hovered around the low seventies. Accordingly, Anaheim hotels have not yet recovered to their pre-pandemic occupancy rates. It is worth noting that the Anaheim occupancy rate is a few percentage points higher than the cities of Los Angeles, Long Beach, and other northern neighbors. Also, several large new hotels were opened in the last three years, increasing the overall supply, such as the Westin, JW Marriot, Element, and others.

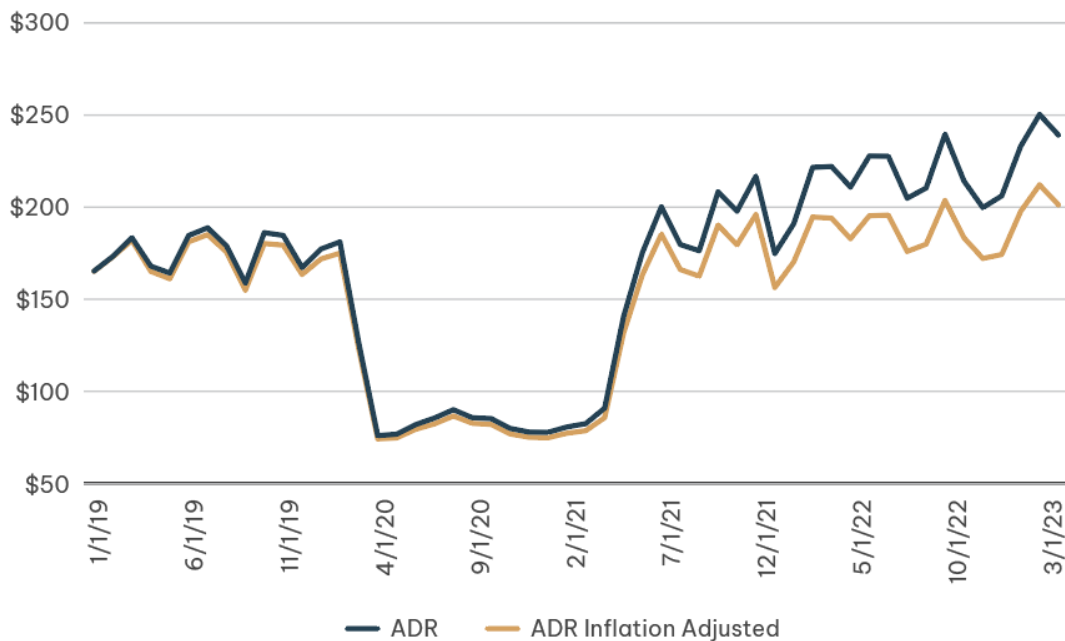


Source: STR and the City of Anaheim; Analysis by Beacon Economics

The reason for the TOT increase is an increase in the Average Daily Rate (ADR) of rooms. In the 12 months prior to the pandemic, ADR was \$176. From April 2022 to April 2023, it was \$222 in nominal terms. When inflation is taken into account, this figure drops to \$190 but is still 8% higher than pre-pandemic rates.



Average Daily Room Rates



Source: STR and the City of Anaheim; Analysis by Beacon Economics

The City's TOT revenue has benefited from its hotels' ability to charge slightly higher rates in the last couple of years than they could before the pandemic. Anaheim's world-class destinations, such as Disneyland, The Anaheim Convention Center, and Angel Stadium, play a large role in attracting tourists and providing hotels with this pricing power.

The Hotel Worker Bill

There are several provisions in the Hotel Worker Bill, but there are two that have the most impact, the Daily Cleaning Area Restrictions, and the Worker Minimum Wage, which are described in further detail below. If implemented, these two measures in particular will set in motion a chain of economic forces, that will ultimately impact the amount of TOT collected by the City of Anaheim:

- Hotel labor costs will increase, because of higher wages and especially because of reduced cleaning productivity, as a result of the square footage requirements
- These higher labor costs will force hotels to increase Average Daily Rates (ADR)
- Higher ADR will make Anaheim hotels less price competitive and discourage guests from staying in Anaheim hotels or cause them to reduce their length of their stay.

Daily Cleaning Area Restrictions:

The most impactful measure concerns restrictions on the square footage that room attendants can be required to clean. This measure will have the largest impact on the operation of hotels, and thus the most significant impact on the City's TOT revenue. These restrictions include:

- In hotels with fewer than 60 guest rooms, a room attendant can only be expected to clean up to 4,000 square feet (sq ft) of floor space in an eight-hour day and must be paid twice the regular hourly rate if they are required to work more.
- In hotels with more than 60 guest rooms, a room attendant can only be expected to clean up to 3,500 sq ft of floor space in an eight-hour day and must be paid twice the regular hour rate if they are required to work more. Additionally, 500 feet of allowable cleaning is reduced for each of the following:
 - if the cleaning attendant cleans more than six special-attention rooms (a checkout room for which the occupant declined daily room cleaning on the immediately preceding day) or additional-bed rooms (rooms with two or more beds).
 - If a room attendant is required to clean floor space in more than one hotel building
 - If a room attendant is required to clean floor space on more than one floor
 - Further reductions shall be reduced on a prorated basis if a room attendant works less than eight hours in a workday
- Written consent is required by room attendants if they are to work more than 10 hours a day.
- Hotels must clean an occupied room each and every night they are occupied.
- Hotels must maintain a record of each room attendant's name, rate of pay, pay received, identification of rooms cleaned, actual square footage of each room cleaned, number of special-attention rooms, number of additional hotel buildings, number of additional-bed rooms, and total square footage cleaned for each workday, overtime hours worked for each workday, and any written consents provided regarding overtime.

These stipulations have the largest impact on TOT of all the measures because it substantially reduces the worker productivity of room attendants. Most hotels in Anaheim have multiple floors, multiple-bed rooms, and/or special attention rooms, meaning that room attendants will be restricted to cleaning 2,500 sq ft per eight-hour shift.

Room attendants in Anaheim currently clean at a rate of roughly 800 to 1,000 sq ft per hour, which is two or three rooms per hour. This equates to roughly 6,000 to 8,000 sq ft per eight-hour shift. Consequently, room attendants will be roughly two-thirds less productive in hotels with more than 60 rooms, because they will only clean 2,500 sq ft. In hotels with less than 60 rooms, where they are limited to 4,000 sq ft room attendants will be about one-third to a half less productive.

However, it is worth noting that hotels with less than 60 rooms make up only 2% of the City’s TOT and 7% of the City’s hotel rooms. Out of the 162 hotels paying TOT in Anaheim, 55 have less than 60 rooms. The other 107 hotels make up 98% of all TOT revenue. Therefore, the two-thirds reduction in room attendant productivity applies to the majority of hotels and almost all of the tax-generating entities.

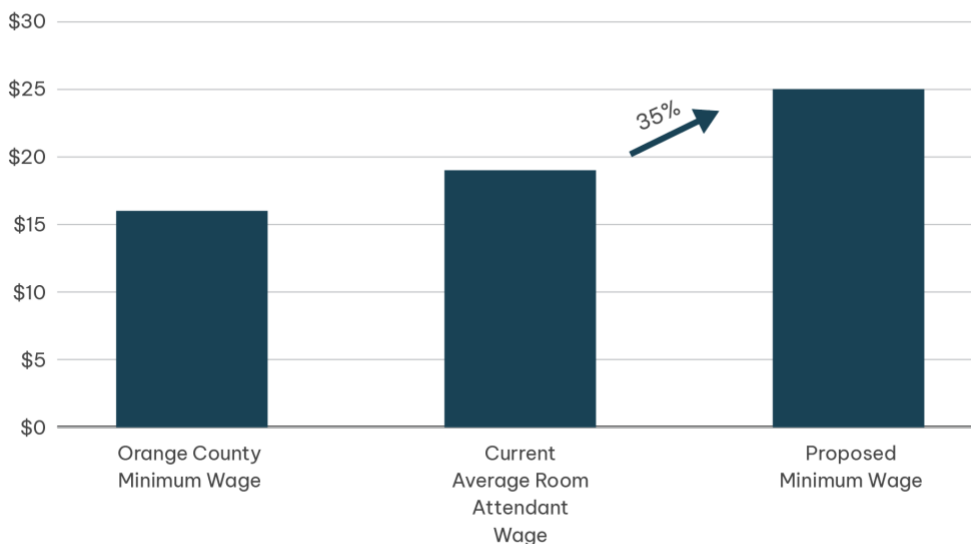
Hotels will also incur expenses and need to hire additional staff to implement and monitor these regulations. There are strict daily reporting requirements involved, and hotels are at risk of class action lawsuits if room attendants clean more square footage than they are supposed to.

Minimum Wage Increase:

This measure stipulates that all hotel workers or event center workers must be paid \$25/hour and that the minimum wage will increase annually on January 1 each year by 3% or based on inflation, whichever is greater.

Currently, non-supervisor hotel positions, such as room attendants, make on average \$18.50/hour. Therefore, \$25/hour constitutes a 35% increase from current compensation levels. Hotels will likely reduce employee benefits, to offset the higher wages. The minimum wage in Orange County is \$15.50.

Anaheim Wage Levels



Of note, the number of job openings for Hotel workers is currently high. Before the pandemic, the industry had a Job Openings rate of roughly 4.5%. Since the pandemic, the Job Openings Rate has hovered around 7.5%. Hotels have been struggling to find enough Hotel workers and

have been gradually raising pay as a result. There are roughly 900 hotel maids working in Anaheim currently.

There is extensive economic literature on minimum wage laws and their effects. While there continues to be disagreement on its outcomes, the most recent research suggests it likely has a net negative impact on the level of poverty in a community^{4,5}.

Less Impactful Measures:

There are several other measures included in the bill that are important for the industry but do not have a significant impact on City TOT. While they are important to consider from a policy implementation standpoint, they are not directly included in the empirical modeling of this fiscal analysis because they do not directly impact TOT in a meaningful way.

These include the measures to protect hotel workers from violent or threatening conduct, the measure stipulating that hotel workers receive all service charges and limited waivers for certain hotel and event center employers. Other measure will make the investment environment less appealing to developers, such as the Notice of Change in Control and Hotel and Event Center Worker Retention (although the cleaning area restrictions would have a large influence on a developer's investment decisions). There are several other components regarding enforcement and collective bargaining agreements that will affect the bill's economic impact. However, these considerations are outside the purview of this report, as they do not have a significant impact on the City's TOT revenue.

Event Centers

Anaheim is home to several world-class event centers – the Honda Center, Angel Stadium, the City National Grove, and of course the Anaheim Convention Center. The minimum wage component, the service charge component, and others impact these centers. They will make operating these Centers more expensive. It will be difficult for these centers to raise their rates to offset these expenses and still remain competitive. Therefore, it is highly likely they will have a negative fiscal impact on the City's budget. However, because they do not pay TOT, this is outside of the scope of the analysis of this report.

There is concern among Hoteliers that higher wages will force the Convention Center to increase its prices. This may be true in the long run, but not for a few years, because the Convention Center typically negotiates its contracts five years in advance of events. Thus, events and their prices for the next several years have already been set and scheduled.

⁴ Richard V. Burkhauser & Drew McNichols & Joseph J. Sabia, 2023. "Minimum Wages and Poverty: New Evidence from Dynamic Difference-in-Differences Estimates," NBER Working Papers 31182, National Bureau of Economic Research, Inc.

⁵ Loukas Karabarbounis, Jeremy Lise, Anusha Nath, 2023. "Economic Impact Evaluation of the City of Minneapolis's Minimum Wage Ordinance," Federal Reserve Bank of Minneapolis. <https://www.minneapolisfed.org/topic/minimum-wage>

If event centers start losing more bids because of high prices and hosting fewer events, this would have serious adverse effects on group demand, which is an essential component of Anaheim's hotel customer base. Hotel "group demand" refers to the total demand for hotel accommodations generated by a specific group or organization. It represents the collective need for rooms, services, and facilities by a group of individuals traveling together for a common purpose, such as a corporate event, conference, or tour. Because of the large number of event centers in Anaheim, group demand plays an outsized role compared to other destination markets.

Impact on Transient Occupancy Tax Revenue

This bill would have a very significant impact on the operations, profitability, and health of the Hotel Industry in Anaheim. However, it will not have a very substantial impact on the City's TOT in the short run. This is because TOT payments are based on a hotel's revenue, not their net income. Hotels will receive fewer customers because they will have to raise rates to cover their increased labor costs. However, these increased room rates will offset much of the loss in occupancy, resulting in similar TOT revenue to the City. The following section walks through these calculations in more detail.

To start with, the marginal labor costs that hotels will face will more than double. Not only do the square footage restrictions substantially diminish the productivity of room attendants, but Hotels will also need to pay all hotel workers much higher wages (roughly 35%). Labor costs make up roughly 35% to 50% of variable costs, depending on a hotel's size and service offerings. Therefore, these increases constitute very significant financial burdens.

Hotels cannot pass through all of these increased expenses, largely because they operate in a highly competitive market environment. For example, the City of Los Angeles mandated that on July 1, 2015, hotels with more than 300 rooms increase their wages to \$15.37 per hour, and hotels with 150 rooms increase their wages to \$15.37 on July 1, 2016. This wage increase constitutes roughly the same percent increase the current HWBI would enforce. For both the large hotels and smaller hotels, there was not statistically significant increase in ADR in the months following the implementation of the \$15.37 increase. Beacon also looked specifically at the West L.A. area, where there is intense competition and porous borders with Beverly Hills and Santa Monica. Likewise, there were no significant changes to ADR in the West L.A. market.

More recently, in August 2022, the City of Los Angeles implemented a bill that regulated the square feet that room attendants can clean, in the same manner as it is being proposed in Anaheim. In other words, the same 3,500 square feet restriction levels and related stipulations that are being proposed in Anaheim have existed in Los Angeles for the last 10 months. This is not a lot of time to see economic consequences, however, there appears to be no large change to ADR or occupancy rates.

These situations in Los Angeles tell us two important things. First, hotels often absorb a lot of the increase in expenses themselves. Second, these regulations damage the financial health of the

hotel industry. As will be discussed later, Los Angeles' hotel market has been depressed relative to Anaheim's.

Regarding TOT forecasting, the key question is - how much does an increase in ADR, decrease the occupancy rate? Beacon Economics analyzed this question using several methods. We ran timeseries regressions based on historical ADR and occupancy rates in Anaheim. We discussed the matter with half a dozen hoteliers. Also, we conducted an extensive literature review, taking into consideration academic articles and recent research. The relationship between ADR and occupancy will vary from one hotel to the next based on a number of factors such as geography, its level of offerings, customer loyalty, etc. All research and empirical analysis point to the same finding. In the short run, the vast majority of Anaheim hotels face an inelastic demand curve, meaning a 1% increase in price leads to a slightly less than 1% decrease in demand. This is why the HWBI will have a positive impact on TOT next year. If a 1% increase in prices leads to a slightly more than 1% decrease in demand, TOT would drop. However, all observations indicate this is not the case. Supporting this conclusion is the fact that Garden Grove hotels, which will not be subject to the HWBI, only have 4,300 rooms in total. This is only 20% of Anaheim's room supply, and not enough to absorb Anaheim's demand.

Based on these estimations, Beacon Economics estimates TOT to increase by 0.5% to 2.5%. The City of Anaheim expects TOT revenue to total \$236M for the next fiscal year, 2023/2024. If this is correct, TOT will likely increase by \$1.2M to \$5.9M.

It is important to note this only includes TOT revenue. Other tax revenue sources will decline as well from the result of fewer guests in hotels, such as sales and use taxes and event center fees. Hotels will inevitably face more financial hardship, lowering their attractiveness to investors. This could decrease their valuation, and therefore the property taxes they pay in the long run, which is discussed in more depth in the following section.

Long Run Impacts

How will the HWBI impact TOT in the long run, roughly five or ten years into the future? To gain insight into this question let us look at the current state of the Anaheim hotel industry, and then analyze how it may change in the future as a result of the bill.

In summary, the hotel industry is doing well and recovering from the pandemic, although faces uncertainty about the future. As noted earlier, while ADR is at record highs, occupancy rates have not returned to pre-pandemic levels. Consequently, revenue per available room (RevPAR), is only at 75% of the level achieved in 2019.

Perhaps more worrying, is that group demand was down 60-65% in 2022. It is expected to reach 75% this year, and fully recover in the next two or three years. There are several new attractions that should help this recovery, such as the Avengers Campus, Mickey & Minnie's Runaway Railway, Mickey's Toontown, and the Indiana Jones Adventure ride.

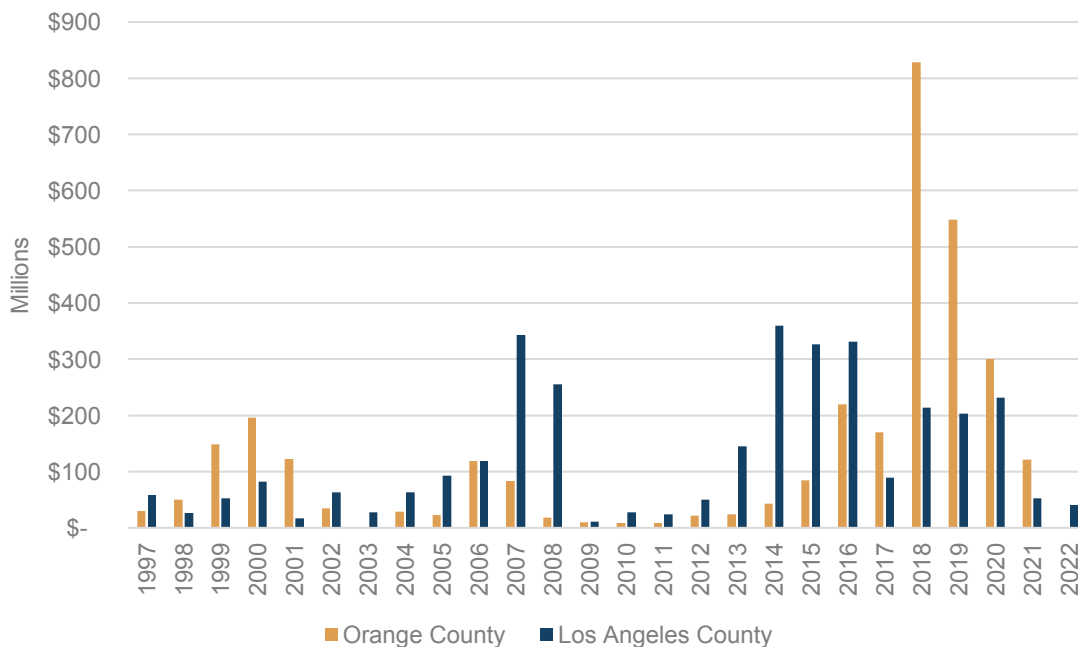
One risk is that the HWBI could stifle group demand through higher event costs leading to stalled occupancy recovery. Group demand is a critical customer market for Anaheim hotels, and could significantly lower occupancy rates if it continues to lag behind its historical average.

More worrying are the long-term effects that HWBI may have on the investment attractiveness of Anaheim. As detailed explained above, the HWBI will certainly lower the profitability of Anaheim hotels, and thus their return to investors. Estimates indicate that the profitability of some Anaheim hotels could be decreased by as much as 50%.

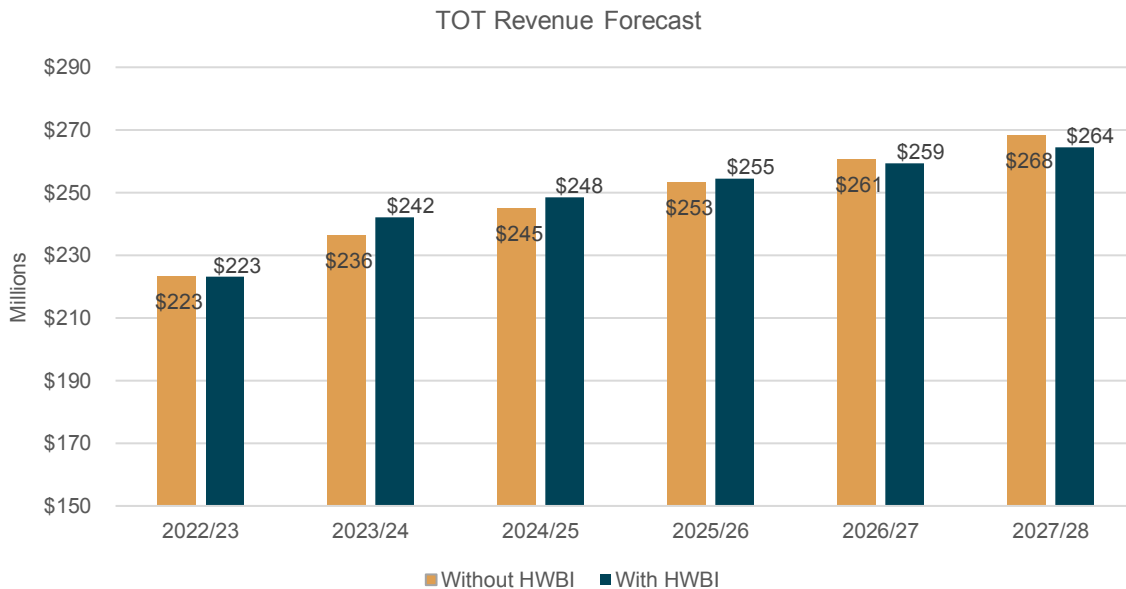
For commercial investors, the question is not whether they should they develop a property in Anaheim or not – the question is, where they should develop a property? If Anaheim does not promise higher returns than alternatives, then new development will not move forward. In fact, at least one hotel development project has been canceled because of the HWBI already.

To a certain degree, the Los Angeles market serves as a good example of this. Los Angeles hotels have faced higher minimum wage laws, and more square footage cleaning restrictions than Anaheim. While the Los Angeles market is not exactly an apples-to-apples comparison, it mirrors many of the same market dynamics that Anaheim faces. The square footage cleaning restrictions went into place in Los Angeles in 2015 and 2016. Since that time, the value of new hotel investment (as measured by the value of their permits) has never been as high again. Los Angeles has also faced considerable challenges getting new hotel development in its Downtown, and still has less hotel development than Anaheim today. Orange County’s population is only one-third the size of Los Angeles County’s, and yet had 17% more hotel development projects over the last 12 years, at \$2.37B compared to \$2.03B respectively. The occupancy rate of Los Angeles hotels is close to 70%, several percentage points lower than Anaheim’s.

Value of Hotel Permits



Therefore, it is very possible the Anaheim market will suffer the same lack of investment, and lower occupancy rates as Los Angeles if it is subject to the same labor regulations. The month-over-month average TOT growth has been 4% since August 2022, when the tourism industry fully opened back up. However, because of the suppression in hotel development caused by the HWBI, long-term growth of TOT will likely be lowered between 30% and 70%. This means the net TOT effect of the bill will turn negative in the next four years. By the 2027/2028 fiscal year, TOT will be roughly \$4M less with the HWBI than it would have been otherwise.



Additional Considerations

This analysis focuses TOT but there will be other spillover effects into the broader economy. For example, Travelers will reduce the length of their stay in Anaheim, and consequently their spending. Moreover, a reduction in new hotels will equate to a loss in millions of dollars of construction spending and indirect economic impacts.

In conclusion, the situation presents a trade-off between the objective of improving the livelihoods of hotel workers through a higher minimum wage and improved working conditions and the potential negative effects on the hotel industry and the city's tax revenue. While raising the minimum wage can positively impact workers' income and address concerns about income inequality, the increased costs and subsequent decline in demand can pose challenges for hotel owners and the local economy.





About Beacon Economics

Founded in 2007, Beacon Economics, an LLC and certified Small Business Enterprise with the state of California, is an independent research and consulting firm dedicated to delivering accurate, insightful, and objectively based economic analysis. Employing unique proprietary models, vast databases, and sophisticated data processing, the company's specialized practice areas include sustainable growth and development, real estate market analysis, economic forecasting, industry analysis, economic policy analysis, and economic impact studies. Beacon Economics equips its clients with the data and analysis required to understand the significance of on-the-ground realities and to make informed business and policy decisions.

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