

Baltimore's Center of Controversy:

Should a new "Convention Center Hotel" be built adjacent to the Convention Center? If so, who should own it? The city favors itself—is that decision the right one?

Facts, figures and questions for a deliberating community and City Council



*Prepared for
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Daily, crowds are drawn to the attractions that ring Baltimore's Inner Harbor: the Science Center, the Constellation, the U.S.S. Torsk, the National Aquarium, and the shopping pavilions. Among the crowds --school children from around the region, Baltimoreans themselves off for a day's pleasure, tourists from all around the world, and conventioners meeting in the Convention Center. With so much festivity in the Inner Harbor, so much energy at work, why do the city fathers believe that there's something wrong with this seemingly sunny picture?

What's missing, they argue, is a "Convention Headquarters Hotel," built next to and physically adjoining the Baltimore Convention Center. Such a user-friendly arrangement, the argument goes, will improve the competitiveness of the "under-performing" convention center, and increase the number of conventions and conventioners spending their time and their money in Baltimore. It is this particular hotel -- at this location with the physical connection, -- that's needed, they say, to complete the picture of a buoyant and burgeoning tourism industry.

The answer to the first question (Do we need a new hotel?) raises a second: if we do, who should build it?

This challenge on the civic agenda finds Baltimore city, as represented by the Baltimore Development Corporation (BDC), disposed to answer both questions by concluding, first, that that it does indeed need the hotel and, second, that it will also build and own it — perhaps the largest and most unique public works project in city history.

The city proposes to build and own a 750-room full-service hotel with 62,000 square feet of meeting space, restaurants, lounges, retail space, parking and other amenities on a 4.5-acre site (Lots 6A/7A) just west of the convention center. Total

development cost is estimated at \$298.5 million, which includes \$195 million for construction of the hotel, and \$103.5 million for associated costs. The city will raise the money by selling \$290.8 million in revenue bonds and using \$7.7 million in interest earnings on the bond proceeds.

“The city’s choice is not between a privately financed vs. a publicly financed headquarters hotel project,” M.J. “Jay” Brodie, president of BDC, and Irene E. Van Sant, the organization’s project analysis director, wrote in May. “The choice is between a publicly financed hotel project and no hotel.”

Others counter that a privately owned hotel built with a combination of private financing and public subsidy is possible. Since 1997, BDC has received at least three proposals from private developers to build a hotel on the site.

At the end of the discourse, city residents and the City Council are confronted with two issues: Does the city need this proposed new hotel, and if so, who should build it?

To provide background to the public debate, The Abell Foundation has commissioned John B. O’Donnell to research the history of the issue and the City Council, which in the end, is charged with decision-making responsibility.

THE CONVENTION CENTER

The Baltimore Convention Center, which opened in 1979, was built as an economic development tool to attract to Baltimore conventions, trade shows and meetings that would leave in the city millions of dollars spent on lodging, food, entertainment and other services. Like many convention centers, it is a money-loser, a so-called loss leader whose role is to bring to the city conventioners who spend money at hotels, restaurants and shops.

Built at a cost of \$51.4 million, the 425,000 square-foot building included 115,000 square-feet of exhibition space and 40,000 square feet of meeting rooms.

Within a decade, it had become clear that the center lacked the size and amenities to make Baltimore a major convention city. Consequently, city and state officials decided on a major expansion and renovation. Completed with \$100 million in state general obligation and revenue bond funds and \$50 million in city revenue bonds, the expanded center opened in September 1996 and the renovation of the original space was completed in April 1997. Tripled in size, the center now offers 300,000 square feet of exhibition space, 85,000 square feet of meeting room space and a ballroom of 36,000 square feet.

The state pays two-thirds of the debt service while the city picks up the other third. In addition, the state pays two-thirds of the operating deficit while the city picks up the other third.

The deficit doubled between 2001 and 2004, peaking at \$5.5 million, according to state budget documents. This year, it is expected to be \$5 million and to rise to \$5.4 million next year. Also, the city and state each pay \$200,000 annually toward capital improvements.

The state's obligation to fund the deficit and capital improvements expires in FY 2008. Unless the General Assembly extends that obligation, the city will become responsible for the entire deficit and the capital improvement fund.

Even after the expenditure of \$200 million for its construction and renovation, the convention center has failed to turn Baltimore into a major convention destination. City and convention center officials attribute the center's less-than-sterling showing to the

absence of a major hotel adjacent to the center that can serve as a convention headquarters hotel.

Since completion of the renovations and expansion, the convention center has been “under-performing,” according to officials of the Baltimore Development Corp., the city’s economic development arm. Its problems were exacerbated by the tragic events of September 11, 2001, which caused an immediate downturn in conventions and trade shows nationally and also prompted some long-range changes in the convention business. Combined with a nationwide boom in construction of new centers and expansion of existing facilities, these developments intensified the competition among cities to attract these events.

The Maryland Stadium Authority, which is responsible for most of the debt service and deficit payments for convention center, told the General Assembly this year that “the lack of a nearby convention hotel always has been an impediment to the true success of the Convention Center.”

Bookings for conventions that occur after this year are substantially less than those for competing cities, *The Baltimore Sun* reported in late December. At that time, *The Sun* reported, only four conventions had been booked for 2009. *The Sun* said Washington, Philadelphia and other cities are far ahead of Baltimore in bookings

In the year ended June 30, 2004, the Baltimore Area Convention and Visitors Association (BACVA) reported that it had signed up 193 conventions and meetings and had booked 250,618 hotel room nights involving 128,115 visitors. Nearly three-quarters of the conventions and meetings were booked for 2004 and 2005.

BACVA president Leslie Doggett asserted in February that the convention center is doing well. In testimony prepared for a state Senate Budget and Taxation subcommittee, she said the convention center “is actually outperforming the national average for events hosted.

“According to a PricewaterhouseCoopers report, the average number of events for centers with 100,000 to 500,000 square feet of exhibit space is 42 events per year,” Ms. Doggett said. “The Baltimore Convention Center has 300,000 square feet of exhibit space. In FY 2004, the Baltimore Convention Center hosted 66 events, and 50 events in 2003... well above the average.”

She did not describe the events or how many attendees they drew to the convention center. Nor did she say whether they were events that drew Baltimore-area residents to the convention center or events that brought out-of-towners, a more desirable clientele because it brings to the local economy money that otherwise would not be spent here – for hotel rooms and restaurant meals, for example. BACVA would not release further information on these events

A General Assembly budget analysis in early 2005 said the convention center is “attracting a comparable number of events and attendees as its competitors; however, it is not attracting enough out-of-town business, and as a result, the economic benefit to the state and city is diminishing.”

Convention center attendance is far below its peak in 2001, according to a study published by The Brookings Institution, a Washington think tank, in January.

BACVA and BDC say many convention planners bypass Baltimore because it lacks a headquarters hotel contiguous to the convention center.

They argue that a large, full-service hotel must be built adjacent to the convention center in order to increase business at what BDC calls the “under-performing” convention center.

Yet, in making that argument, they have offered no information or analysis on the impact that construction of headquarters hotels in other cities has had on their convention center’s business.

BACVA’s lost business reports for a recent 19-month period suggests that lack of a convention headquarters hotel is a minor factor in the city’s failure to land conventions and that high hotel room rates are much for significant.

THE STATE OF THE BALTIMORE HOTEL MARKET

Baltimore’s hotel industry suffered a setback after September 11, 2001 as Americans became more cautious about travel, particularly by air. But the decline in Baltimore was milder and briefer than that suffered by other cities.

High room rates are a sign of a healthy hotel market and Baltimore’s hotel market is strong, providing good occupancy levels and room rates at a time when hotel profits nationally are on the rise.

The hotel industry, in general, is doing well. In January, PricewaterhouseCoopers said the lodging industry experienced a 29.9 percent increase in profits in 2004 to \$16.6 billion and projected a 25 percent increase in profits in 2005 to \$20.8 billion and record profits of \$25.2 billion in 2006.

According to the Maryland Stadium Authority, there are nearly 26,000 hotel rooms in the Baltimore “market area” including 7,266 rooms in the “primary city/county area.”

In 2003, Baltimore had the ninth highest occupancy rate nationally and was 21st among the top 100 metropolitan areas in hotel room rates, with an average daily room rate of \$97.65, the Maryland Stadium Authority said in a December 15, 2004 report on convention center and BACVA funding. This compared to an industry average of \$83.23.

Smith Travel Research, of Tennessee, a widely used monitor of the hotel industry, has identified hotels it considers primary and secondary competitors of the proposed convention headquarters hotel. They have a total of 4,689 rooms.

The primary competitors -- the Marriott Inner Harbor, the Renaissance, the Hyatt Regency, the Sheraton and the Marriott Waterfront -- have 2,720 rooms. In 2004, the average room rate of the five was \$167.42 and the occupancy rate was estimated at 74.3 percent, slightly higher than the 73 percent BDC projects for the new hotel in its fourth year of operation. These are quite healthy numbers.

The secondary competitors had a 66.6 percent occupancy rate in 2004 and an average room rate of \$121.50.

At the primary competitors, 52 percent of the business in 2003 came from meetings and conventions, ranging from 40 percent at the Renaissance to 65 percent at the Marriott Waterfront. Interestingly, the primary competitor with the highest meetings-related occupancy, the Marriott Waterfront, is farthest from the convention center. About 90 percent of its convention and meeting business is in-house and unrelated to the convention center.

HOTEL PRICES AND CONVENTION BUSINESS

BACVA says that Baltimore hotel rates are pricing the city out of a large segment of the convention market.

“We are finding that higher rates are eliminating Baltimore from much of the competition for citywide conventions,” the association said in its business report for the year ended June 30, 2004. “...The perception of our customers is that Baltimore is an expensive city with which to do business.”

In 2004, for example, BACVA reported that three big conventions that had considered Baltimore decided to locate in other cities where they got “more competitive rates.”

The Society of Nuclear Medicine opted for Miami for a meeting that will use 18,000 room nights; the Clinical Laboratory Management Association chose Chicago for a meeting that involves 10,000 room nights; and the American Legion chose Louisville for a 2009 convention that will use 19,000 hotel room nights.

“Louisville promised the group a confirmed rate of \$99 five years from now,” BACVA said in a report in 2004. “That rate is hard for Baltimore to beat, especially when the city’s occupancy rate is healthy.”

In March, 2005, Louisville opened a new 616-room privately owned convention headquarters hotel built with private financing and public subsidy.

Operated by Marriott, the hotel is connected by skywalk to the Kentucky International Convention Center, and is offering room rates far below Baltimore rates. For a convention in October 2005, the rate is \$115 a night. A nearby Hyatt Regency hotel in Louisville is offering rooms at \$107 a night.

Leslie Doggett, president of BACVA, told the Greater Baltimore Committee recently that it is very difficult for Baltimore to compete without comparable room rates. BDC has given the City Council projections that show an average room rate at the

proposed Hilton hotel of \$195.06 in 2009, nearly \$100 more than Louisville guaranteed the American Legion for that year..

HVS International, the city's hotel consultant, did a "lost business survey" covering the January 2003 through May 2004 period. HVS queried convention planners who choose another city after having "tentatively held show dates" at the Baltimore Convention Center. Of 108 planners contacted, 45 responded.

Based on the survey, HVS estimated that the proposed Baltimore hotel would attract 103,000 room nights from increased convention center bookings. That figure is 22.5 percent of the 458,000 room nights that HVS said are lost annually when conventions choose another city after considering Baltimore.

However, BACVA reports a substantially greater loss of hotel conventioneer patronage in the year ended June 30, 2004 -- 822,877 room nights.

BDC and BACVA have said that a key to the success of the hotel as a magnet for conventions is Hilton's agreement to set aside 600 of the 750 rooms for conventions under a complicated "room block agreement."

But, the hotel can't rely solely on convention center business if it is to be successful, BDC says.

The 103,000 convention room nights that HVS projects for the new hotel represent about half the patronage the hotel will need to achieve an occupancy level of 73 percent, which the consulting firm projects for the fourth year of operation and succeeding years.

BACVA's view is that the proposed Hilton hotel will also have to compete for the meetings that are held in hotels rather than convention centers. Noting that the Marriott

Waterfront now has a substantial meetings business, Debra Dignan, BACVA's associate vice president of sales, said in an interview, "It's a great opportunity for them to be in competition, to offer different packages."

In BDC's view, the new hotel will boost the use of the convention center if BACVA succeeds in marketing the city to convention planners at a time when other cities are offering increasingly tempting financial incentives to those planners.

"It's BACVA's job to attract conventions," BDC said.

For its part, BACVA says it can generate interest in the city but it is up to others to close the deal.

"An important point that is often lost," BACVA president Doggett told the General Assembly in February, "is the fact that it is BACVA's job to drive business demand to the region but it is up to the hotels and the Baltimore Convention Center to actually secure the deal.

"In other words, we can generate the interest in Baltimore as a convention and leisure destination but it is up to our hospitality partners to put together a competitive, attractive package that actually gets people here."

In a paper issued in early May, M.J. "Jay" Brodie, president of BDC, and Irene Van Sant, the BDC's project analysis director, wrote, "Room rates are a function of supply and demand; without additional hotel rooms, the pricing problems we face today will only get worse."

The new headquarters hotel will increase the number of rooms in the primary competitor group by 27.6 percent. The increase would be 16 percent for the combined primary-secondary market.

BDC financial projections show that this hotel will have to maintain fairly high room rates and high occupancy levels in order to produce sufficient revenue to pay debt service and provide excess revenue to the city treasury.

Indeed, BDC has expressed concern about the possibility that another convention-oriented hotel would be built near the Inner Harbor and compete with the proposed Hilton. When the ARC Wheeler Group's purchase of a two-acre site across Light St. from the Inner Harbor was announced in June 2005, M.J. "Jay" Brodie, president of BDC, was quoted in *The Baltimore Sun* as saying downtown could not support a hotel on that site aimed at convention business.

Responding to questions about the BDC attitude toward a hotel on the McCormick site, Mr. Brodie and Ms. Van Sant said, "We have standards and controls for this site that any developer has to comply with, regardless of the use. Other than that, we can't block development if it is privately financed. Now, if a developer comes to the city and wants city money, then we can do our analysis and we can decline to participate in a project."

The opening of the city-owned headquarters hotel may reduce room rates, at least temporarily. It is likely that lower rates will help attract conventions that seek lower rates. In 2001, occupancy rates fell from 75.6 percent to 68.4 percent among primary competitors after the Marriott Waterfront opened, according to Smith Travel Research figures. Average room rates fell less than a dollar, from \$145.25 to \$144.60.

"Baltimore is so strong as a tourism destination that its strength has affected the price of hotel rooms to the point where blocks of rooms are unavailable to prospective

meeting planners at competitive prices,” a Maryland Stadium Authority task force said in a Feb. 3, 2005 report.”

HVS International, the BDC consultant on the hotel project, noted problems with high rates. In its survey of event planners whose conventions rejected Baltimore between January 2003 and May 2004, HVS found that the price of available rooms was “critical” to the decision of nearly half of them to opt for another city.

HVS found that the average daily room rate that it projects for convention attendees at the Baltimore headquarters hotel after operations stabilize -- \$160 in 2003 dollars – “exceeds the acceptable maximum rate of approximately 50 percent of event planners.”

Further, HVS said, “The projected rate in the headquarters hotel may become a critical issue for more meeting planners. However, the quality and convenience of the new product may raise the threshold of price sensitivity.”

BDC and its consultants predict a strong market for the new Hilton. They project the city will have nearly \$6 million in excess hotel revenue available in 2011, the stabilization year, for the general fund or for hotel reserve funds..

In 2011, the fourth year of operation, BDC’s presentation to the City Council projects an average room rate of \$209.01 and a 73 percent occupancy level.

In addition to the Hilton headquarters hotel, two limited service hotels have opened near the convention center recently. Two other limited services hotels are being proposed for the Inner Harbor East and H&S Properties and Struever Bros. Eccles & Rouse Inc. plan to start construction in fall 2005 at Inner Harbor East on a 200-room Four Seasons hotel and a 106-unit luxury condominium complex.

In another project, H&S Properties and Struever Bros. have talked of building a hotel, offices and shops on the former harbor-side site of the Allied Signal chromium plant.

Unlike full service hotels, like the proposed convention center hotel, limited service hotels are being built today without public subsidy or with limited subsidy. The reason: They are much cheaper per room and private financing is more available.

Bruce Walker, founder and president of Source Strategies Inc., a San Antonio firm that studies the hotel industry in Texas, said a full service hotel, with food and beverage service, meeting rooms and other amenities, costs \$250,000 per room to build while a limited service hotel with the same quality rooms can be built for \$60,000 to \$70,000 per room.

At a construction cost of \$195 million, proposed convention headquarters hotel in Baltimore would cost \$260,000 per key.

THE STATE OF THE CONVENTION BUSINESS

There is no guarantee that the headquarters hotel will attract substantial new business to the convention center. Indeed, the Greater Baltimore Committee asked BDC, “Is the hotel expected to attract new and bigger conventions?”

In a written response, M. Jay Brodie, president of BDC, did not answer the question directly but said that a BACVA survey in 2004 found that “suitability of hotels was ranked as the key factor by meeting planners” in site selection. The response did not say that the hotel-related reason most often cited by meeting planners for choosing another city after considering Baltimore, according to BACVA’s FY 2004 lost business report, was “hotel rates too high.” Of 327 meetings and conventions lost, 51 – representing 93,727 room nights – cited that reason for going elsewhere. The only

reason cited more frequently was “board decision,” which was offered by 81 lost meetings involving 138,053 room nights. “Lack of headquarters hotel” was cited seven times, representing 40,652 room nights.

“We believe,” Mr. Brodie wrote, “that Baltimore must achieve what its competitors have – more hotel rooms in close proximity to the convention center. The Hilton hotel is the best way for the city to accomplish that goal.” Yet, as noted earlier, BDC has offered no data or analysis of the impact of new convention headquarters hotels on their adjacent convention centers.

“I have yet to find a case where the addition of a headquarters hotel has spurred a consistently significant increase in convention center business,” said Heywood Sanders, a professor of public administration at the University of Texas San Antonio, who follows the convention business and is a critic of the construction of headquarters hotels and convention centers.

The convention and trade show industry is in a state of transition that is making it increasingly difficult for cities to attract meetings and prompting them to offer better and better deals to conventions – both on the cost of renting space in the convention center and, beyond that, lodging and other costs. Nationally, the size of the convention pie is shrinking as the amount of space for conventions is growing.

Some of the change was instigated by 9/11, which caused a sharp but temporary decline in business and leisure travel. That prompted many companies to find other ways to conduct the business previously transacted at conventions – for example, through teleconferencing, web casting and other uses of the Internet. Once they found these new approaches worked, they decided to stick with them, said Ms. Dignan of BACVA.

“According to Tradeshow Week, the amount of available meeting space is expected to grow 9 percent over the next six years while the number of available meetings is expected to decrease by 6 percent,” Ms. Doggett, BACVA’s president and CEO, told the General Assembly in January.

She also said in a letter to committee chairmen, “Changing market conditions are wreaking havoc on the industry and how convention and visitor bureaus do business, and Baltimore is no different. . .

“Meeting planners in search of bargains now have choices from cities that are giving away convention center space for free.”

While the impact of 9/11 on the travel and hotel businesses has been largely overcome – chiefly through gains in the leisure travel segment of the industry -- and there has been some recovery in the convention business, convention numbers are still far below their highs in the 1990s. Many companies have not gone back to the old ways, preferring to continue their clampdown on travel and demanding that employees show them a rate of return on their business travel.

Michael Hough, a consultant on trade shows, wrote on his website, “Many qualified buyers are not attending the events we produce because they no longer perceive a value in them, or their bosses do not perceive they have a value to the business. This is particularly true among the next generation who believe they can learn everything needed right at their desktop.”

Cities that traditionally thrived on conventions and trade shows too large for Baltimore to handle -- like Chicago, Orlando, Atlanta and Las Vegas -- are now competing for the smaller events that Baltimore seeks.

A new Baltimore competitor will be a 470,000 square foot building that Chicago is adding to the McCormick Place convention complex at a cost of \$850 million, bringing total space there to more than 2.6 million square feet.

Another new competitor – “our next major competition,” according to the Ms. Dignan, associate vice president for sales at BACVA – is under construction in Baltimore’s backyard. The Gaylord National Resort and Convention Center on the Potomac River near I-95 in Prince George’s County is scheduled to open in March 2008, around the time the convention headquarters hotel in Baltimore is projected to open. The Gaylord complex will include 400,000 square feet of exhibition and meeting space and a 1,500-room hotel.

The most recent report by *Tradeshaw Week* shows a sharp decline in the last five years in the amount of utilized exhibition space and attendance at trade shows, consumer shows (like auto, home improvement and boat shows) and combined shows. The consumer shows are considered less valuable to convention cities because they draw patronage mainly from local residents who do not spend on hotels and restaurants as out-of-town convention attendees do.

Tradeshaw Week reports that, overall, the total number of events is up 2.3 percent this year to 4,889. At the same time, exhibit space used by those shows is off 33.7 percent from 531 million square feet in 2004 to 352 million square feet in 2005 and attendance is off slightly from 51 million to 50.6 million.

Since 2000, *Tradeshaw Week* said utilized exhibition space is down 38.7 percent and attendance is down from 126 million to 50.6 million, a drop of 59.8 percent.

The increase in the number of total events is due largely to growth in the less desirable consumer shows.

In 2000, consumer shows amounted to 13 percent of exhibitions; in 2005, they account for 22 percent. Average attendance at consumer shows is 40,000 this year compared to average trade show attendance of 5,862.

In a 2004 report Source Strategies Inc., the San Antonio consulting firm, looked at convention attendance over the previous decade and said, "Demand for conventions has declined by 50 percent for the last four years compared to the previous six years (110.8 million prior average compared to 55.5 million current average.)"

Meanwhile, construction and expansion continue as use and attendance shrink, the result of advances in the use of technology along with corporate and trade association mergers and consolidations in various industries like manufacturing, retail and technology.

An example is the Super Show, held annually by the Sporting Goods Manufacturers Association, which is seeing consolidation in its industry. The amount of convention space that it uses annually has declined from 1,390,000 square feet in 1999 to 797,390 feet in 2003, a drop of 43 percent, according to a *USA Today* article published in January 2005. An association spokesman attributed much of the decline to industry consolidation, saying, "When you have two big companies merge, you don't need every single person who was working for both companies."

In Atlanta, attendance at the George World Congress Center fell from 837,752 in 1997 to an estimated 396,500 last year, the article said, even as the center was enlarged from 950,000 square feet to 1.4 million square feet.

The Brookings Institution, the Washington think tank, published a report in mid-January that detailed the boom in construction and expansion of convention centers, offering a bleak outlook for cities scrambling for convention business and seeking to build new hotels to boost their convention business.

Authored by Professor Sanders, of the University of Texas at San Antonio, the report said:

- The amount of convention space increased by 51 percent between 1990 and 2003.
- Twenty-two cities are planning or building new centers and another 22 are building or planning expansions.
- A “structural change” is underway in the convention industry that is “the product of industry consolidation, particularly in the hardware and home improvement industry, reductions in business travel in the face of increasing cost and difficulty, and alternative means of conveying and gathering information.”
- The biggest centers – in Orlando, Chicago, Atlanta – are expanding to handle simultaneous small and medium sized events, the shows Baltimore seeks to attract to the convention center.
- In 2003, the use of convention space by the largest events was down 4.2 percent while attendance was down 3.2 percent.
- The Baltimore’s Convention Center has seen attendance decline 28.2 percent since fiscal year 2001 to pre-expansion levels of 1997.
- Studies that justify publicly owned convention headquarters hotels “paint a picture of tens of thousands of new out-of-town visitors and millions of dollars in economic impact. Despite that rhetoric, these projects carry real risks and larger potential costs, particularly in an uncertain and highly competitive environment.”

“Faced with convention centers that are routinely failing to deliver on the promises of their proponents and the forecasts of their feasibility study consultants,” Sanders wrote, “many cities wind up, as they say, ‘throwing good money after bad.’ Indeed, weak performance—an underutilized center, falling attendance, an absence of promised private investment nearby—is often the justification for further public investment.”

HVS International, the BDC consultant on the proposed Baltimore hotel, criticized the Sanders work in a response published in May. Thomas Hazinski and Hans Detlefsen of HVS, accused Sanders of selective use of unrepresentative statistics and of “selective focus on negative change.”

HVS argues that the industry is not in the dire straits depicted by Professor Sanders. Yet, the HVS report offers a somber if not bleak picture.

Messrs. Hazinski and Detlefsen assert, “An industry that was once immune to the effects of economic cycles now finds itself exposed to periods of negative growth and overall lower long-term growth rates. These are sobering trends but should not be characterized as an industry collapse. The data also indicates some recovery in demand in 2003 and 2004.” ”

They also wrote, “Over the past three decades, the meeting and convention industry has evolved dramatically from a budding industry to a mature one, entering a new stage of the industry’s lifecycle. Historically rapid growth in the supply of exhibit space has allowed rapid growth in the industry, as groups that formerly had no appropriate exhibition venue available, now have many facilities competing for their business.”

The authors developed a “utilization index” that, they said, charts the use since 1986 of gross exhibition space by events tracked by *Tradeshaw Week*. Their index shows that utilization peaked at 21.63 percent in 1999 and has fallen steadily since then, reaching a 19-year-low in 2004 of 16.52 percent.

Saying, “competition for business is likely to remain fierce,” HVS argues that cities “with a strong package of convention facilities, location, access, marketing efforts,

technology and overall destination appeal will succeed, while other cities will struggle to find an appropriate market niche.”

Professor Sanders isn't the only one to report alarmingly on an increase in convention space at a time when the convention business is declining.

“If convention center space exceeds demand, why hasn't anyone put the brakes on expansions and new construction?” Michelle Russell, editor of the Professional Convention Management Association magazine, asked in the October 2004 issue.

Projects elsewhere similar to the proposed hotel project.

BDC says 61 hotels of more than 700 rooms have been built in the United States since 1993. These included 51 that did not receive public subsidies -- 48 built in major gaming and resort destinations and three built in New York City. Of the remaining 10, five were built as public-private partnerships and five were built as publicly owned and financed projects.

BDC cites five of them as the model for construction and ownership of the new Baltimore hotel. Four were publicly financed and are publicly owned. The fifth, the St. Louis hotel, is privately owned but was financed in large measure with public funds, including \$98 million in Empowerment Zone revenue bonds.

Despite the turnaround nationally in the hotel industry some of these hotels have done poorly, in part because those cities have a glut of downtown hotel rooms. St. Louis and Houston are two examples.

Here is a list of the five along with a summary of their performance:

- **The 1,100-room Denver Hyatt**
The hotel, across the street from the recently expanded Colorado Convention Center, is scheduled to open in December 2005. Its development is financed with \$367.5 million in AAA/Aaa-rated and insured bonds sold in June 2003 at an interest rate of 4.6 percent. The

city, which opted to build and own the hotel after failing to reach agreement with a private developer, has agreed to backstop 40 to 50 percent of the annual debt service.

Nearly doubled in size at a cost of \$310 million, the expanded convention center opened in December 2004.

- **The 800-room Austin Hilton**

The hotel, financed with \$265.1 million in revenue bonds rated A/Baa3 opened in downtown Austin at the beginning of 2004. The hotel represented a 21 percent increase in downtown room supply. “There appears to be demand for these new rooms,” Strategic Strategies, Inc said in a report on third quarter results.

”The Hilton appears to have been absorbed without significant damage to other, private enterprise hotels (except the Hyatt, which is down 10 percent),” the firm said in a report on the third quarter of 2004.

- **The 1,200-room Houston Hilton Americas.**

Financed with \$326.2 million in revenue bonds rated AAA/Aaa, the hotel opened in December 2003 at a time when downtown Houston saw a doubling of the number of hotel rooms, adding 2,458 rooms in time for the Super Bowl that was played there in 2004. In addition to building and owning this hotel, the city of Houston also provided tax incentives for the other new hotels. The openings of several hotels followed the collapse of Enron and the 2001 recession. The result was a disaster for the Houston hotel market.

“The entire market gain in room nights sold has gone to the new public Hilton rather than to the existing, privately-owned hotels,” Source Strategies said. “Tax incentives contributed to the explosion in new hotel supply downtown, as well as the consultant-driven hype that major new convention volume was ‘on the way.’ To date, we know of no significant increase in the rates of booked convention business for the future.”

A byproduct of the doubling of downtown Houston hotel rooms was the foreclosure in February 2005 on the 977-room Downtown Hyatt. Until recently, the 32-year-old Hyatt was the only large downtown hotel.

- **St. Louis convention center hotel.**

This is actually two hotels, the 165-room Renaissance Suites, which opened in April 2002, and the 916-room Renaissance Grand, which opened in February 2003. The project involved the renovation of two historic hotels and construction of a new 21-story tower that became part of the Renaissance Grand.

Unlike the others in this list, this hotel is privately owned (by Kimberly Clark) but was eligible for revenue bond financing because it is in the St. Louis Empowerment Zone. Financing included \$80.7 million in city and government cash contributions and \$98 million in revenue bonds initially rated Baa3 by Moody's Investor Services.

The hotel has fallen far short of expectations, prompting Moody's to downgrade the bonds in December 2003, to Ba3 and again in August 2004, to B3.

Moody's attributes the hotel's problems to the increasing competition in the convention industry, a soft hotel market caused in part by overbuilding and overly optimistic predictions of the hotel's success.

The hotels have been operating at a deficit and using reserves to pay debt service. Moody's says debt service reserves could be exhausted by mid-2005. Despite a negative outlook, Moody's is optimistic that Kimberly-Clark and Marriott will subsidize hotel operations at least through 2006 to protect their investments and lock down a \$21 million historic tax credit.

In September 2000, a division of HVS International, the consultant for the proposed Baltimore hotel, said the St. Louis convention center accounted for 460,000 room nights in the city annually. "It is expected that with the addition of the subject properties, the city will be able to accommodate over 800,000 room nights in future years," HVS reported.

Moody's says that when bonds to finance hotel construction were sold in November 2000, the St. Louis Convention and Visitors Commission made a similar "aggressive forecast." The commission predicted that expansion of the convention center and the addition of these hotels would generate 800,000 room nights from conventions and group meetings by 2004, Moody's said. Instead, from a peak of 500,000 convention room nights in 2000, the total fell to 400,000 in 2003. It is now projected to be 470,000 in 2007.

- **The 800-room Chicago Hyatt**

There is no public record on the success of the Chicago Hyatt, which opened in 1998. The Metropolitan Pier & Exposition Authority, owner of McCormick Place convention center, built the hotel with \$126 million in revenue bonds. A year after construction, the hotel debt was rolled into the authority's general debt. Thus, the performance of the hotel is not reported publicly.

BDC has also cited some other hotels built with public funds. They are:

- **The Radisson Plaza, Myrtle Beach SC.**
The 402-room hotel, financed with \$64.3 million in revenue bonds and another \$12.1 million in subsidies, opened in January 2003. It fell far short of projections and in 2004 its owner, the Myrtle Beach Hotel Board Corporation, approved a technical default and paid a premium on \$40.8 million in senior bonds. Myrtle Beach refinanced with \$47.7 million in bonds in an attempt to deal with the hotel's money problems and backed the bonds with city hospitality fee revenues, depriving other projects of backing from that revenue source.

The hotel board and Radisson agreed in March 2005 to part ways and the board chose Sheraton.

- **Sheraton Hotel, Overland Park, Kansas.**
The 412-room convention center hotel and the adjacent convention center were built at the same time. The hotel, which opened in December 2002, was financed with \$92.2 million in revenue bonds. The city contributed \$6.5 million in land and infrastructure and backed debt service with as much as \$7 million a year in city funds and other backup pledges. HVS International did the market study for the hotel, which has fallen short of revenue projections. In 2003 net income was projected to be \$6.65 million; it was \$3.08 million. Last year, net income was expected to be \$8.41 million; it was \$4.42, according to Professor Sanders of the University of Texas at San Antonio.
- **Omaha Hilton, Omaha Nebraska**
The 450-room Hilton Hotel, across the street from the convention center, opened in Spring 2004. Construction of the hotel, a parking garage and a connecting skywalk to the convention center were financed with \$109 million in AAA-rated and insured revenue bonds. The city provided a contingent guarantee of 40 to 66 percent of debt service (with an aggregate cap of 40 percent), subject to annual appropriation. City of Omaha budget documents show that the hotel, which opened in Spring 2004, has fallen well short of revenue projections. For 2004, the city budgeted revenue of \$6 million and later revised that figure to \$2.4 million. For 2005, the city projected revenue of \$3.2 million, far short of scheduled debt service of \$5.4 million. The city is drawing on reserves to pay debt service.
- **Sheraton Grand, Sacramento**
The 500-room hotel, built with \$92.8 million in senior bonds, \$4.1 million in subordinate bonds and \$8 million in government subsidies has not met projections made in 1999 when the bonds were sold. In March, 2005, the Sacramento city treasurer announced that the hotel would be unable to make the first payment on the subordinate bonds, which is due Jan. 1, 2006. His report said the hotel had a 76.1 percent occupancy rate and an average room rate of \$122.86 in 2004, both higher than Northern

California benchmarks. However, consultants had projected a 73 percent occupancy rate at an average room rate of \$145.00 for 2004.

For the first quarter of 2005, according to PKF Consulting, which tracks the hotel's performance, the Sheraton Grand had an average room rate of \$135.35 and occupancy of 79.8 percent, both substantial increases over 2004.

The hotel, which opened in 2001, has fallen far short of projections for the convention business it would attract. PKF notes that in the first quarter of the year, convention and meeting demand for 2005 is off by 5,796 room nights compared to 2004. Convention and meetings business has fallen from 51 percent of hotel patronage in the third quarter of 2004 to 41.2 percent in the first quarter of 2005. Group bookings for 2006 have improved over the 2005 rate by 4,145 room nights, PKF said.

THE STRUGGLE TO ATTRACT CONVENTIONS

In 2003, Source Strategies examined the construction of 16 major convention hotels that had been built since 1980 in four Texas cities – Austin, Dallas, Houston and San Antonio.

“The opening of large, full-service hotels near convention centers clearly do not increase demand in the local area market around convention centers,” the report concluded. “Consequently, such openings only dilute the business of other existing hotels, driving down their revenues and profitability.”

In the face of declining demand and increasing supply, it may be exceedingly difficult for the new Baltimore hotel to attract a substantial increase in convention business in Baltimore.

In 2004, BACVA booked 36 conventions and trade shows that are expected to bring 167,725 people to Baltimore, according to a Maryland Stadium Authority report in December. BACVA reported that in the year ended June 30, 2004, it had signed up 193 conventions and meetings and had booked nearly 250,000 hotel room nights. Only 27

percent of those meetings represented long-term commitments. The rest were booked for 2004 and 2005.

The association also reported that it had “more than 600,000 tentative room nights on the books for future years” from “groups that have a definite interest in holding a meeting in Baltimore.”

In the 19 months ended Jan. 31, 2005, BACVA’s lost business report said, 551 groups that had considered Baltimore for their meetings decided against the city. Those groups would have used 1,247,713 hotel room nights.

Those groups gave a wide variety of reasons for rejecting Baltimore. Seventy-seven groups decided to hold their meetings elsewhere because they considered Baltimore’s hotel rates too high. They represented 15 percent of the lost room nights.

Twelve groups that would have taken 61,120 room nights cited the lack of a headquarters hotel as their reason for going elsewhere.

BACVA provided the following report on business it lost between July 1, 2003 and Jan. 31, 2005:

Baltimore Area Convention and Visitors Association			
Lost Business for the period 7/1/2003 – 1/31/2005			
Lost Business equals tentative business where bid information was requested by the customer and provided by BACVA, but Baltimore was not selected for reasons listed.			
Number of meetings: 551 Total attendance: 1,335,701 Rooms requested: 1,247,713			
Business Reason	Rooms Requested	(% of total)	Meetings
Board decision	192,517	15.40%	103
Center negotiations	12,635	1.01%	2
Chose another date	24,098	1.93%	8
Climate	42,885	3.43%	14
Competitor's pricing (Fair market value)	97,049	7.78%	37
Convention Center rates too high	58,265	4.67%	11
Dates not available – BCC	19,710	1.58%	8
Dates not available – hotel	20,045	1.61%	44
Does not meet booking Policy-BCC	9,675	0.77%	2
Geographic rotation	94,208	7.55%	20
Hotel rates too high	183,389	14.70%	77
Inadequate exhibit space – BCC	64,556	5.17%	9
Inadequate meeting space – BCC	44,345	3.55%	9
Inadequate meeting space – hotel	11,999	0.96%	12
Inadequate number of rooms – hotel	22,510	1.80%	5
Lack of Client response	42,900	3.44%	26
Lack of headquarters hotel	61,120	4.90%	12
Lack of hotel response	2,681	0.21%	8
Lack of Local Support	9,355	0.75%	4
Lack of union facilities	815	0.07%	1
Meeting Cancelled	50,529	4.05%	52
Overall pricing too high	40,203	3.22%	11
Politics of group	40,269	3.22%	40
Preferred dates not available	19,800	1.59%	6
Quality of service	13,095	1.05%	4
Requires larger hotel	29,124	2.33%	12
Sept. 11, 2001 terrorist attacks	177	0.01%	1
Turned away for better business	39,759	3.19%	13
TOTALS	1,247,713		551

A report by a Maryland Stadium Authority task force, dated Feb. 3, 2005, cites two examples of conventions and trade shows that Baltimore lost to other cities because the competitors gave away their convention centers. The report doesn't say when those meetings were lost.

- Baltimore was competing with Washington D.C. for a biennial convention that would have brought 6,000 attendees, representing 10,495 hotel room nights, to Baltimore in December, 2009. Both cities offered similar pricing packages. "At the final hour Toronto came in and made an offer that included complimentary rental in their convention center," the report said. The group would have had to pay \$67,450 rent at the Baltimore Convention Center. Baltimore lost \$5.7 million in direct spending when the convention went to Toronto.
- Another group was considering a return to Baltimore for an April 2008 conference that would have brought to the city 4,000 people, who would have used 10,195 room nights and represented direct spending of \$3.8 million. Baltimore was competing with Philadelphia, which offered competitive but lower pricing. Baltimore matched the offer by Philadelphia, which then countered by giving the group free convention space.

The task force said, "According to BACVA, over the past three years, Baltimore lost business to other cities because of cost, or conversely, for lack of the funds to subsidize conventions. These losses translated into 137,478 room nights (60,600 attendees) for a loss of \$1.42 million in room tax revenues alone. Total economic impact would have been \$57 million."

The task force recommended that the city earmark \$500,000 annually from hotel occupancy tax revenues to subsidize conventions and to seek new business.

"Without the creation of this 'opportunity fund' Baltimore stands to lose significant convention and meeting business; much more than the amount being recommended for the fund itself."

Ms. Doggett, president and CEO of BACVA, acknowledged the difficulty of selling Baltimore to conventions in a February 2005 report to the state Senate Budget and Taxation Committee.

She said BACVA targets “high revenue generating” organizations -- “medical groups, technology groups and conventions with a strong tradeshow component because they utilize food and beverage, electricity and Internet connections, which generate revenue for the center.

“Attracting these types of groups can be challenging because we are competing with cities that have larger convention center space, warmer climates (Fort Lauderdale and Orlando) and lower rates where doctors and scientists want to go and take their families in wintertime.”

Who should build and Own the new hotel?

BDC has seemingly contradictory positions on this question, saying on the one hand that public ownership and public financing is the only way the hotel can be built while asserting on the other hand that the city should not offer private hotel investors a subsidy.

“In a May 2005 paper, M.J. “Jay” Brodie, president of BDC, and Irene Van Sant, the organization’s project analysis director, wrote, “Today, the capital markets are requiring as much as 50 percent equity in downtown hotel projects” and that “hotel investors are requiring returns on equity of 20 to 25 percent.

“This has resulted in private developers requesting ever increasing amounts of public subsidy.”

BDC officials said, “It wouldn’t make sense for the city to subsidize to get that private return for a developer.”

They said, “The City’s choice is not between a privately financed vs. a publicly financed headquarters hotel project; our choice is between a publicly financed hotel project and ‘No’ hotel.”

Interestingly, managing director of HVS convention, Sport & Entertainment Facilities Consulting, who the city’s consultant on the hotel project, wrote in October 2004, “Private equity investors may require from 10% to 15% cash return on equity” in public-private hotel development deals.

And when RLJ/Quadrangle submitted its proposal for a public-private hotel development, it described its proposed investment return of 12-14 percent as “appropriate.”

In recent years, the city has received proposals to build the convention hotel with private financing supplemented by public funding.

It is not unusual for public funds to be used to subsidize the construction of privately owned hotels, particularly today.

In Baltimore, there is precedent going back at least to the construction of the Hyatt Regency Hotel in the 1970s.

The Inner Harbor Master Plan, developed in the 1960s, envisioned the construction of a new hotel.

Convincing developers to build one was a difficult task. “The hotel would not have happened except for the city’s participation,” according to BDC. “They shopped the site around to everyone and got no one” to express interest.

After two possible deals fell through, Mayor William Donald Schaefer, in a series of intense negotiations, made what some considered as an extraordinary offer to the Pritzker family, which then owned the Hyatt Corporation. The mayor proposed:

- To lend Hyatt \$12 million at 7% interest, using \$10 million from a federal Urban Development Action Grant.
- To have the city build a \$4 million parking garage to serve the hotel.
- City construction of elevated walkways to connect the hotel to Harborplace (and therefore to the harbor promenade).
- A city guarantee of a minimum occupancy rate in the initial years of hotel operation.

In return, the city would get a share of the hotel's profits.

The Pritzkers' equity investment in the \$40 million hotel was \$500,000.

Once opened, the Hyatt became the most successful hotel in the Hyatt chain and has been a source of cash for the city ever since. The city receives two-thirds of the hotel's profits in 7 of every 8 years. In the eighth year, the profit is plowed back into the hotel for upgrades. In 2003, BDC said, the city's share of the profit was \$3.8 million.

In large part because of the Inner Harbor and the construction of the Hyatt hotel, Baltimore developed as a major tourist destination.

In the late 1990s, city subsidies were a key ingredient in the construction of the Marriott Waterfront Hotel, which became a catalyst for development of Inner Harbor East. In that case, the city gave the hotel an exemption from property taxes for 25 years under a Payment In Lieu of Taxes (PILOT) agreement. The hotel pays \$1 a year in property taxes under the PILOT.

Without the PILOT, the hotel would pay \$2,152,289 this year in property taxes at the city's current property tax rate. BDC estimates the value of the PILOT, after discounting for current value of money, at \$40 million.

In addition to the property tax relief, the hotel project also received \$10 million in cash from the city – a \$5 million grant and a \$5 million loan at an interest rate of 2 percent.

THREE PROPOSALS FOR PRIVATE DEVELOPMENT WITH PUBLIC SUBSIDIES

There have been at least three proposals from private parties in the last eight years to use private financing and public subsidies to build a headquarters hotel on Lots 6A/7A. Two of those were submitted in 2003 by developers seeking to build the hotel that the city now proposes to build. Earlier, in 1997, Peter Angelos submitted a proposal.

In May, Mr. Brodie and Ms. Van Sant wrote, “At no time in the past eight years has a viable privately financed deal, even with public subsidy, been put forth for this key site.”

They wrote, “Today, the capital markets are requiring as much as 50% equity in downtown hotel projects; hotels investors are requiring returns on equity of 20 to 25%. This has resulted in private developers requesting ever increasing amounts of public subsidy.”

Turning to the proposals submitted in 2003, BDC said developers wanted significant tax rebates estimated at \$4 million to \$5 million a year along with “a city pledge or guaranty of debt service payments on either private debt or public bonds.

“It was clear that despite private ownership of the hotel these proposals required the city to take the key risk if the hotel did not do as well as projected, while the private owner retained most, if not all, of the direct financial benefits.”

“The city and its financial advisors concluded that such proposals were unacceptable.”

The Angelos 1997 proposal

Mr. Angelos proposed a \$150 million project to build an 850-room Grand Hyatt hotel on Lots 6A/7A, site of the proposed Hilton. The Grand Hyatt would have included 64,000 square feet of meeting space, including two ballrooms, and 50,000 square feet of exhibition space.

Mr. Angelos asked the city:

- To donate the land, which he valued at \$10 million.
- To provide a \$2 million annual abatement on property taxes for 20 years, saying the money would be used to pay debt service on \$17 million in secondary financing.
- To issue \$16 million in revenue bonds to finance construction of the privately owned parking garage. Debt service would have been covered by revenue from the garage.
- Subsequently, he asked the city for \$10 million to renovate the lobby and other public areas of the Hyatt Regency on Pratt St.

Through an aide, Mr. Angelos said he proposed to acquire Hyatt Corporation's one-third interest in the Hyatt Regency Hotel's cash flow (the city has the other two-thirds) for \$43 million and to extend the interest beyond its expiration in 2013.

In his proposal, Mr. Angelos said that together the new Grand Hyatt on Lots 6A/7A and the existing Hyatt Regency on Light Street would offer 1,335 rooms and be connected to the convention center by pedestrian bridges. The two hotels "could act as a headquarters for some of the country's largest meeting groups," the proposal said.

BDC says it never got close to an agreement with Mr. Angelos. It also claims that he asked the city to sell him its two-thirds interest in Hyatt Regency profits, a statement he emphatically disputes.

After Mr. Angelos' exclusive negotiating rights expired in 2000, BDC began a search for a developer, a search that was put on hold temporarily after the events of Sept. 11, 2001 dealt a severe but temporary blow to the travel industry.

Then, in March 2002, M. Jay Brodie, president of BDC, met with Robert L. Johnson, founder of the Black Entertainment Television and founder of RLJ Development in an effort to interest him in developing a major hotel on the site west of the convention center. Eight months later, in November 2002, RLJ Development and Quadrangle Development Corp. of Washington, D.C. jointly submitted what Mayor O'Malley called "a very significant proposal."

After RLJ and Quadrangle submitted their proposal, the BDC went public and published a Request for Proposals (RFP) to see if other developers were interested in building a hotel on the site.

In February 2003, RLJ/Quadrangle and two other teams – the Believe Team headed by Otis Warren & Co of Baltimore and Garfield Traub Development of Dallas; and TreyPort Ventures LLC, headed by Portman Holdings L.P. of Atlanta and Treyball Development Inc., of Beverly Hills – submitted proposals.

RLJ/Quadrangle and TreyPort proposed to develop and own the hotel and to build it with a combination of private equity and public subsidy. The Believe Team proposed a hotel owned by the city and financed by revenue bonds.

Moreover, The Believe Team submitted a second proposal, offering to build a hotel on a smaller Conway St. lot next to the Sheraton Hotel garage. That lot, now used for parking, is closer to both the convention center and the Inner Harbor than Lots 6A/7A and considerably smaller.

The city then decided to use the public ownership model espoused by The Believe Team and asked the other developers to propose a city-owned and city-financed hotel.

After the revised proposals were submitted in 2003, BDC staff recommended the selection of RLJ/Quadrangle to oversee development of the city-owned hotel. A BDC advisory panel, the BDC board and the mayor approved the recommendation.

BDC says RLJ/Quadrangle will be “an owner’s representative for the project to assist BDC and the owner in reviewing the design documents, specifications, contracts and to provide construction monitoring services.”

BDC has distributed a list of nine hotels built with tax-exempt financing since 1999. One of those is the 400-room Hyatt Regency Chesapeake Bay Golf Resort, Spa and Marina in Cambridge, Md., which opened in August 2002. The Maryland Economic Development Corporation (MEDCO) financed the \$156 million project with revenue bonds.

Quadrangle had a role in Cambridge similar to but greater than its role in the convention headquarters hotel. The firm held an equity stake in the Cambridge project and was responsible for negotiating the construction contract with Clark Construction Co. of Washington and for overseeing construction, according to court papers.

An important difference between the Baltimore and Cambridge projects is that Quadrangle, Clark and Hyatt or their affiliates will own the Cambridge hotel once the bonds are paid off.

A guaranteed maximum price and a guaranteed delivery date, both subject to penalties, were part of the Cambridge project just as they are part of the headquarters hotel project..

In a complicated round of litigation initiated in 2002 by a Clark suit that sought more than \$20 million in overruns, MEDCO said Quadrangle and QDS, a Quadrangle

affiliate, were supposed to act as MEDCO's agent and protect its interests in negotiating with the contractor and overseeing construction.

MEDCO alleged that it had learned during the discovery process involving the Clark suit that "Quadrangle and QDS appear to have engaged in misrepresentation, concealment, breaches of fiduciary duty, breaches of contract, breaches of agency authority and other wrongful acts and omissions in connection with the project and in connection with their relationship to MEDCO on the project" and "that during development, design and construction of the project, Quadrangle and QDS appear to have engaged in self-dealing between themselves and with the Clark entities, to their collective benefit as Developers and to the detriment of MEDCO."

The allegations were never tested at trial. The parties settled in November 2004 after the General Assembly passed and Governor Robert L. Ehrlich signed legislation that authorized a surcharge on the room rentals at the Cambridge hotel to finance a \$12 million state revenue bond issue to pay Clark for overruns.

Robert Gladstone, chairman of Quadrangle, says the case did not go to trial because Clark "pursued a political strategy," and that the case was stayed before Quadrangle's motion to dismiss MEDCO's complaint was considered. Court records show that the case was stayed in May 2004, following General Assembly adoption of the legislation, so that settlement negotiations could proceed.

Robert C. Brennan, who became executive director of MEDCO in 2004, would not comment on the litigation but said in an interview that he saw "nothing inappropriate" in the role Quadrangle is expected to have in construction of the Baltimore hotel and that he has "high respect for Mr. Gladstone."

BDC will not comment on the litigation except to say of Quadrangle, “Their role there was completely different” in Cambridge.

BDC will pay RLJ/Quadrangle a consulting fee for its work on the convention headquarters hotel. Officials said the fee has not yet been negotiated but that the team will not be paid the amount that it sought in August 2003.

In a submission dated Aug. 21, 2003, RLJ/Quadrangle proposed a fee schedule for work on developing the publicly financed and publicly owned hotel of 4 percent of total development cost including financing. At a total development cost of \$298.5 million, the fee would be \$11.9 million. During operation of the hotel, RLJ/QDC proposed an asset management fee of 1 percent of revenues and a parking management fee of 5 percent of revenues.

The hotel owner hires an asset manager to oversee its investment and the hotel’s operation. The manager reviews and interprets financial data prepared by the operator and submits them to the owner. The manager must also disclose any irregularities on the part of the hotel operator and franchisor to the owner.

BDC says RLJ/Quadrangle will not be the asset manager. The asset manager will be selected through publication of a Request for Proposals (RFP).

BDC has not offered a written explanation for rejecting The Believe Team’s alternate site on Conway St. Officials said their rationale was threaded throughout the material they submitted to an advisory panel and the BDC board.

BDC refused to make public that material, saying, “It should suffice for your report to state that the Conway Street site was rejected by both the Hotel Advisory Panel and the BDC board.”

However, in an interview, officials noted that the Conway St. site is less than an acre and that, in designing a hotel for the site, the Believe Team had to “stack” ballrooms and meeting rooms. “That is not desirable from a hotel operators point of view,” BDC said. Furthermore, officials added, while the Conway St. site is much closer to the convention center than the proposed hotel, it is in back of the center and “not near” areas of the center that conventioners use.

Explaining its decision to opt for a publicly funded and publicly owned hotel, BDC said, “A significant gap exists between the cost of building a headquarters hotel, with its large meeting spaces, food and beverage operation, and the amount of debt and equity that could be raised from private sector financing sources.”

Declaring that full service hotels are no longer being built with private financing, except in gaming and resort locations, BDC said, “In our experience, private financing does not exist to build a headquarters hotel in Baltimore; the city’s choice is not between a privately financed vs. a publicly financed headquarters hotel project; the choice is between a publicly financed hotel project and no hotel.”

THE 2003 PROPOSALS

Two of the three development teams that responded to the BDC Request for Proposals to develop the hotel site proposed privately owned, privately financed hotels with the aid of public subsidies.

The RLJ/Quadrangle proposal

Phase One -- \$211 million

A 750-room Hilton hotel with 75,000 square feet of meeting and ballroom space and a 750-space parking garage.

Financing

- \$124.9 million private financing for the hotel guest tower

- \$71.1 million in city and Maryland Stadium Authority bonds to finance the hotel meeting and ballroom facilities and “selected food and beverage facilities.”
- \$15 million in public financing for the parking garage

Future Phases -- \$137.8 million

Hotel expansion by up to 400 rooms, and office space, financed privately financed at \$117 million; a \$20 million federally financed Maglev station.

The team also asked for real estate tax abatement projected to amount to \$11.5 million over the first ten years of operation and a “favorable land purchase price and terms with minimum current carrying cost, say \$12,000/year for the first 10 years.”

RLJ Quadrangle said that without public financing of the meeting, ballroom and food and beverage facilities, “Returns on total capital invested in the hotel fall in the 2-3 percent per annum range – clearly too low to support investment in the project.”

The proposal said, “We tested the concept of publicly financing the hotel conference center including select food and beverage facilities – all spaces which are significantly enlarged due to the headquarters function specified for this hotel. As the test result shows, investment returns on the privately financed hotel tower increased to an appropriate market standard in the 12-14 percent ranges.”

BDC says this proposal called for public financing of the unprofitable portions of the hotel, the public spaces, while RLJ/Quadrangle would have financed – and profited from – the most profitable part of the hotel, the guest rooms.

The TreyPort proposals

The team included Portman Holdings, L.P. of Atlanta, Treyball Development, Inc., of Beverly Hills, CA, (headed by actor Will Smith and his brother Harry), John

Portman & Associates, Inc., of Atlanta and MetroVision Community Development of Pittsburgh. Later, Whiting-Turner Contracting Co., of Baltimore was added.

TreyPort proposed a privately owned hotel financed with private debt and equity investments and public subsidies. Subsequently, BDC asked the three teams bidding for the right to develop the project to submit a new plan based on city ownership and revenue bond financing of the project.

The first proposal

An 869-room hotel with 55,000 sq. ft. of meeting and banquet space, 592 parking spaces and amenities including a wellness clinic and spa and a sound stage and recording space to costs \$276.2 million.

Financing

TreyPort proposed to finance the \$276.2 million project with \$27.5 million in private equity, \$248.7 million in private mortgage debt and a generous city economic support package that included, where possible:

- Waiver of all municipal fees related to the development of the project.
- Waiver of real property taxes on the site and the improvements.
- Exemption from taxes on the purchase of materials and services for construction of the hotel.
- Conveyance of Lots 6A/7A, assessed in 2005 for \$20.9 million, to TreyPort “for the entire economic life of the improvements at little or no cost.”
- Rebate back to the hotel ownership of city tax receipts generated by the project for the economic life of the project.
- TreyPort also sought city pledges of financial assistance if hotel revenues were insufficient to cover debt service:
 1. A City or State contingent credit pledge to cover annual shortfalls in debt service up to \$5 million a year – capped at \$30 million. There were two provisos:
 - a. In the first two operating years, before the credit pledge could be called, the hotel owner would first be required to fund up \$3.7 million (in the first year) or \$2.5 million (in the second year) of mortgage shortfalls.

- b. The city's obligations would end in the event annual Net Operating Income was twice the mortgage obligation or the city funded \$30 million under the pledge.

BDC says the city did not have the power to grant all tax rebates sought by TreyPort and that the taxes the city could rebate, if it chose to do so, would have cost the treasury \$5 million annually. Moreover, BDC says, the city would have had to escrow the \$30 million TreyPort sought as a debt service backup because there was no proviso in its proposal for City Council appropriation of the funds if they were needed.

The second proposal

An 800-room hotel including 40 suites, 86,400 square feet of dedicated function space, a health and fitness mezzanine, 800 parking spaces and infrastructure for a 200,000 square foot office building.

Financing

TreyPort estimated the cost at \$200.7 million before financing costs. TreyPort proposed to issue AAA-rated bonds to cover most of the cost; \$10 million in "participation" by the TreyPort team including \$2.5 million in cash and \$7.5 million letters of credit that would "burn off" over five years beginning in the third year of operation.

TreyPort also wanted a "contingent obligation:" from the city to cover approximately 50 percent of debt service in the event hotel revenues were insufficient. The contingent obligation would be called if hotel cash flow were to fall below 45 percent of projections.

The Believe Team proposals:

The team's members were Otis Warren and Company of Baltimore, managing partner, Garfield Traub Development LLC, of Dallas, a national real estate and hotel development firm. Peter Fillat, a Baltimore architect, and designer of the Marriott

Waterfront Hotel, Whiting-Turner Contracting Co. and Brennan Beer Gorman Monk (BBGM), hotel designers whose Peninsula Bangkok was rated No. 1 hotel in the world by Travel & Leisure Magazine in August 2003.

The team submitted two proposals for public financing/public ownership, one for the city-owned Lot 6A/7A north of Camden yards and one for a smaller lot on Conway St. next to the Sheraton Inner Harbor and closer to the convention center and Inner Harbor.

Lot 6A/7A

A 755-room Westin hotel with 54,457 sq. ft. of meeting and ballroom space, retail space and 496 parking spaces to be built at a cost of \$165.6 million including \$106.7 hotel construction cost and \$11.8 million parking garage construction.

Financing

The team proposed two methods of bond financing, one requiring issuance of \$219 million in bonds, the other requiring issuance of \$224.1 million. In both cases, members of the team would have bought an additional \$10 million in bonds. The differences in the financing scenarios revolved around the amount of debt service the city would have to guarantee and the amount of excess hotel revenue the city was projected to receive.

In one case, The Believe Team said, the city would have had to backstop \$239 million in debt service over 30 years. Over the same period, it would have received cash flow of approximately \$387.6 million. In the other case, the city would have had to backstop \$204.7 million in debt service over 30 years while receiving \$297.6 million in

cash flow. After 30 years, in each case, the city would own a hotel valued at \$398.1 million.

Conway St. site

A 759-room hotel Westin hotel with similar amenities and 352 parking spaces added to the Sheraton garage for a total of 873 spaces, connected by an elevated bridge to the convention center.

Financing

Proposed cost was \$172 million, including \$8 million to purchase the lot controlled by Willard Hackerman of Whiting-Turner Contracting Co.

As with the proposal for Lots 6A/7A, The Believe Team offered two different scenarios for bond financing, both of which required a backstop credit pledge by the city. In one case, the city would issue \$231.4 million in bonds; in the other case, it would have issued \$232.9 million.

The differences in the financing scenarios centered on the amount of debt service the city would have had to guarantee and the amount of excess hotel revenue it was projected to receive. In one case, the city would have backstopped \$252.5 million in debt service while receiving \$371 million in net case flow over 30 years and. In the other case, the city would have backstopped \$212.2 million in debt service while receiving \$305 million in cash over 30 years. After 30 years, in each case, the city would own a \$410.7 million hotel.

THE CITY'S CURRENT PLAN

Baltimore plans to build, furnish and equip a four-star quality, full-service convention headquarters hotel for \$195 million on the two city-owned lots known as 6A/7A, which are now used as a parking lot. The 4.5-acre site lies directly north of Oriole

Park at Camden Yards and is bordered by Pratt, Paca, Camden and Howard streets and split by Eutaw Street, which would be closed to traffic. However, the bed of Eutaw Street would be undisturbed and become a pedestrian way because many city utilities lie beneath the roadbed. The hotel would be built on the western parcel, a block from the convention center and connected to it by pedestrian bridges.

The key features of the hotel are:

- A minimum of 750 guest rooms
- Approximately 62,000 square feet of ballroom and meeting space.
- Restaurants, lounges and retail space (13,200 square feet).
- Structured parking of approximately 600 spaces
- Street-level retail and outdoor public spaces.
- A pedestrian bridge across Eutaw Street connecting the hotel with the grand ballroom and a pedestrian bridge across Howard Street connecting the project to the Baltimore Convention Center.
- Space for an underground Maglev station should Baltimore be selected for the futuristic high-speed magnetic levitation train demonstration project.

To shield itself from liability, the City will charter a non-profit corporation to own the hotel.

Hilton Hotels Corporation, the operator, will sign an agreement with BACVA to set aside 600 rooms for conventions under a complicated formula.

RTKL is the hotel architect. The city Urban Design and Architecture Review Panel granted preliminary approval to the design in January.

Also involved in the project are the city finance and law departments, Piper Jaffray, the bond underwriter, HVS International, the hotel consultant and two financial advisors, First Southwest Company and Jackson Securities.

Whiting-Turner Contracting Co. had been designated as the design-builder but could not reach agreement with BDC on a \$195 million contract to, in BDC's words,

undertake “the project from the schematic stage of design to completion under a guaranteed maximum price (GMP) and a guaranteed completion date.”

Buyers of the bonds that finance hotel projects of this kind usually require the design-builder to guarantee price and completion. If the builder fails to reach “substantial completion” by the designated delivery date, it must pay liquidated damages equal to daily debt service.

After BDC and Whiting-Turner failed to reach agreement, BDC issued a Request for Proposals (RFP) in March, 2005 for a “design-build firm,” saying a GMP and guaranteed completion date had to be included in all submissions. Three firms submitted proposals in May, Whiting-Turner, Hensel Phelps Construction Co. of Chantilly, Va., and FaulknerUSA of Austin Texas. BDC anticipates making an award by June 30.

BDC said proposals were based on the same RTKL plans that Whiting-Turner was using when it was unable to reach agreement with BDC.

The GMP will cover:

- Design errors.
- Known or unknown subsurface conditions.
- Price increases in materials or labor.
- Trade buyout differentials.
- Costs in correcting defective work, overtime, or costs in accelerating work to meet the scheduled substantial completion date.
- Weather delays and work stoppages.
- Shortages in materials or labor arising for any reason.
- Subcontractor defaults.
- Force majeure, unforeseen event beyond the contractor’s control that prevent it from fulfilling its obligations under the contract such as natural disasters or other "Acts of God", war, or the failure of third parties to perform their obligations to the contractor.
- Other costs of completing work, which exceed the GMP, that are not identified as owner’s costs and are not the result of the owner’s actions.

Smaller than the city consultant recommended

At 750 rooms, the hotel will be smaller than the 800 rooms recommended in 2002 by HVS. And there is no provision for the expansion that HVS recommended and RLJ/Quadrangle included in its original proposal.

BDC officials say, “Hilton and we believe we’re building the right size. Fifty more rooms got to be extremely expensive” and, they concluded, would have “put the city at more risk.”

Financing the project

BDC says it plans to issue \$290.8 million in revenue bonds and to raise another \$7.7 million by collecting interest on the bond proceeds for a total of \$298.5 million. However, guarding against unexpected developments, like rising interest rates, the O’Malley administration has asked the City Council to authorize a bond issue not to exceed \$305 million.

City officials are seeking a AAA rating from bond rating agencies. To get the rating, the city must purchase insurance on the bonds at a cost of nearly \$17 million, a step that will assure investors of repayment and, according to BDC, save the city about 2 percentage points on the interest rate – substantially reducing the cost of financing the project. BDC financial projections are based on getting an interest rate of 4.88 percent on the bonds.

Sources of Funds

Bonds	\$290,770,000
Interest on construction fund	\$7,729,000
TOTAL	\$298,499,000

Uses of funds

Construction fund	\$195,000,000
Interest fund	\$35,666,000
Debt service reserve fund	\$19,624,000
Bond insurance premium	\$16,938,000
Owner contingency/Pre-Opening expenses	\$11,000,000
Operating capital	\$10,000,000
Costs of issuance	\$7,269,000
Non-profit hotel corporation budget	\$3,000,000
Rounding amount	\$2,000
TOTAL	\$298,499,000

The economic benefits

BDC projects substantial benefits for city residents and municipal government, most of which would be realized if the city had stuck to its initial plan to have a developer build and own the hotel while adhering to city minority and women’s enterprise requirements.

The benefits cited by BDC:

- 663 construction and related jobs during development.
- \$1.229 million in City taxes during construction,
- More than \$40 million in business for minority and women controlled enterprises based on a \$125 million hard construction budget.
- More than 550 permanent hotel jobs with an annual payroll of \$19 million.
- Piggyback income, parking and utility tax revenues of \$800,000 a year.
- Millions of dollars that would not be available to the city if the hotel were privately developed.
 - In 2036, at bond maturity, the “the city’s financial benefit is projected to equal \$162.8 million (in today’s dollars).”
 - In 2020, the hotel’s 13th year of operation, “the city’s financial benefit is projected to equal \$64.5 million (in today’s dollars.)”

The economic commitment

Once construction begins, the city will lose nearly \$1.5 million annually from the 298-space parking lot that a Philadelphia firm now operates on Lots 6A/7A.

The city is also placing at risk the 4.5-acre site, which was appraised for \$18 million in 2003 and is valued by state property tax assessors at \$21 million. If the hotel operation were to turn into a financial disaster and the city lost it to foreclosure, the land, too, would be lost.

The major economic commitment involves repayment of the \$290 borrowed through the bond issue to finance the project. Financial projections provided by BDC show that net operating revenue is expected to be more than sufficient to cover debt service. BDC projects net operating income of \$852.7 million over 29 years, an average of \$29.4 million.

If those funds are insufficient, then the city will tap the incremental property tax revenue generated by the hotel (estimated at \$136.5 million over 29 years, an average of \$4.7 million) and the hotel occupancy tax revenue generated by the new hotel (projected to be \$122.4 million over 28 years, an average of \$4.4 million).

If those funds still don't cover debt service, the city is seeking to further assure bond buyers by, among other things, pledging city general funds to cover as much as 25 percent of debt service annually to make up a shortfall. The general fund pledge is \$139.3 million over 29 years, an average of \$4.8 million. If the funds were needed, City Council would have to appropriate the money annually because the commitment does not represent a pledge of the city's full faith and credit. The city could not make such a pledge without the electorate approving a general obligation bond issue at referendum. That is not being contemplated.

In addition, city is setting aside \$29.5 million in bond sale proceeds and \$10 million in excess hotel revenue, if any, for debt service reserves, and will pay another \$17

million from bond sale proceeds for insurance on the bonds. In the event that all else fails, the insurance guarantees repayment to the bond buyers and, according to BDC, saves about two percentage points on the interest rate the city pays the bond buyers.

Hilton Hotels Corp. has agreed to guarantee \$25 million in debt service for the first eight years of hotel operations and \$5 million for the next seven years. Hilton and BDC are still negotiating details of the agreement.

According to BDC, Hilton has proposed that the \$25 million obligation “would be reduced by 50 percent if the cash flow hits a 1.5 times coverage of debt service for a consecutive twelve-month period” and that it would “be reduced by the remaining 50 percent if the cash flow hits 1.5 coverage of debt service for a consecutive eighteen-month period.”

If those coverage levels were not met the obligation would nevertheless be reduced to \$5 million after eight years and would remain in place for the seven years left in Hilton’s management agreement.

Hilton’s obligation is capped at \$25 million even if those funds are used before the 8-year guarantee or subsequent 7-year guarantee expire.

Terms and conditions for releasing the Hilton guaranty have to be agreed upon by the bond rating agencies, BDC said.

BDC listed the order in which various backup funds would be tapped if net operating income and revenues from the hotel’s property tax and occupancy taxes were not sufficient:

1. A cash trap fund of up to \$10 million funded with excess hotel revenue. The fund is designed to protect bondholders from poor hotel performance.
2. An operating reserve of \$10 million funded at bond closing.

3. 15% of debt service from general funds – money raised by the citywide Hotel Occupancy Tax
4. An 8-year \$25 million guarantee provided by Hilton.
5. 10% of debt service from general funds raised by the citywide Hotel Occupancy Tax.
6. The debt service reserve fund of \$19.5 million funded at bond closing.
7. Foreclosure and payout by the bond insurers.

City officials are confident these sources will not be tapped. With those backup pledges, however, BDC officials say rating agencies will provide a bond rating “that will result in the lowest possible interest rate on the bonds.”

In an April presentation to the City Council BDC included some worst-case scenarios. In a “no growth shock” scenario, BDC said that if there is no increase in demand for hotel rooms or in hotel room rates above the 2003 level, then city general funds would have to be tapped for debt service. City Council would have to appropriate money beginning in the third year of operation to cover shortfalls in debt service ranging from \$1 million to \$2.1 million annually. Moreover, the city would have already given up nearly \$1.5 million in revenue from the parking lot now on the site. Still, BDC said, the hotel would still provide a positive financial benefit to the city./

BDC also offered a “break-even” scenario where occupancy levels fall to 60 percent in the fourth year of operation, the stabilization year, and never rise over the life of the bonds. Under this scenario, hotel revenue would cover debt service but the operating reserve fund and cash trip fund would be tapped between from 2011 through 2026 to finance a portion of the reserve fund for replacement of furniture, fixtures and equipment (FF&E), ranging from a high of \$2 million in 2014 to a low of \$425,000 in 2025. In this case, too, the city would benefit economically from the hotel operation, according to a Piper Jaffray analysis that BDC gave to the City Council.

“We have conservatively structured this transaction to be self financing and not a drain on the city,” BDC said in a January paper. BDC also said the city is seeking to “make the project as ‘self financing’ as possible” and to “minimize the impact on the city’s existing revenues.” The city’s Director of Finance and its financial advisors have “vetted the entire financing,” BDC said.

THE ROOM BLOCK AGREEMENT

Room block agreements – under which hotels commit many rooms to meeting organizers -- are an important tool for attracting conventions. In its 2002 market study for BDC, HVS International said an 800-room headquarters hotel should be built next to the convention center and that it “must offer at least a 700-unit room block (87.5% of the hotel’s rooms) to the meeting planner in order to serve as a competitive, headquarters property in this eastern United States market.”

Currently, BACVA has no formal room block agreement with any downtown hotel.

Under the current plan, Hilton Hotels will sign a formal agreement that commits 80 percent of the hotel’s rooms to BACVA.

The agreement gives BACVA control of the 600 rooms for a specified number of days over a specified period of months, depending on how far in the future a specific convention center event is to take place.

The following chart sets out the number of rooms BACVA can control in each period:

The Booking Period as defined by the number of months the event is to occur after the date of the room block request	Required room block days	Required hold period for the room block request
12-17 months	73 of 365 days – 20%	90 days
18-23 months	128 of 365 days – 35%	150 days
24-36 months	183 of 365 days – 50%	210 days
37-48 months	201 of 365 days – 55%	365 days
49-60 months	219 of 365 days – 60%	540 days
60+ months	274 of 365 days – 75%	730 days

Each booking period is dated from the date BACVA asks Hilton for rooms. For example, a request on Sept. 1, 2009, to provide rooms for a convention beginning on May 7, 2013 falls into the 37-48 month booking period.

Thus, the farther in advance a convention is booked, the more rooms it is likely to find available under the room block agreement.

The room block agreement is a minimum requirement for rooms to be available to BACVA and does not bar Hilton from providing more rooms at its discretion.

Currently, BDC says, convention planners must put together a 10-hotel package, including rooms beyond the city limits, to handle a convention that needs 1,200 to 1,500 rooms. Convention planners want all the hotels to be near the convention center including a headquarters hotel that is contiguous to the convention center. With construction of the new hotel, BDC is confident that the city will be able to handle conventions with three or four nearby hotels.

Room block agreements: The problems

In addition to the room block agreements that hotels sign with convention and visitors associations like BACVA, meeting planners conclude agreements with individual

hotels as they make arrangements for a convention, agreeing to use a block of rooms in exchange for a favorable rate.

While room block agreements are important to convention planners and to the city, they appear less important to convention goers.

In increasing numbers, attendees are opting for hotels that do not have room block agreements with planners of their conventions.

The Convention Industry Council in 2004 said this is a costly and “alarming trend,” because convention organizers must pay penalties for failing to book the rooms that hotels set aside under a room block agreement.

In a council survey, almost 50 percent of respondents (and 60 percent of those who paid their own way) said that saving money – an average of \$40 to \$70 a night – was the reason they booked accommodations outside the room block. The next two most frequently cited reasons, at about 25 percent each, were “control over the registration process” and “preference for a hotel.”

“Clearly,” the council concluded, “attendees no longer believe that organizers have negotiated the ‘lowest rate in the house.’ ”

The council and convention planners are taking steps to reverse the trend, including pleas for the attendees to honor the room block agreements and efforts to have attendees book their hotel rooms through the convention website

The Special Libraries Association met in Toronto in early June. Its web site had this pre-convention plea to members:

“Please help us fight our current housing challenges by booking through the SLA Conference Housing Bureau. Attrition penalties are crippling, and if they are not brought under control, they will affect conference attendee costs. For example, a \$200,000 penalty would

translate into \$17 per member or \$75 per full-paying conference attendee.”

Here are a couple of examples involving conventions scheduled for the Baltimore Convention Center in 2005:

- In advance of its April convention, The Council for Exceptional Children designated eight hotels for use by attendees, including The Hyatt Regency and Renaissance Harbor Place, which were described as “co-headquarters hotels.”

The website said, “Your patronage of these official hotels is important to the overall success of the convention.” And it offered an inducement, saying that by booking at one of these hotels, conventioners “have a chance to win a complimentary convention registration or a 50 percent discount on the negotiated “discount” room rate.

- *PhAST*, an organization dedicated to presenting the latest breakthroughs in Photonic Applications, Systems and Technologies, met at the convention center in late May. Its convention website urged members to register through *PhAST* at one of seven listed hotels that had set aside rooms and warned against staying at a hotel not designated as an official hotel.

This is what *PhAST* put on its website:

“To protect the value of the rooms that have been set aside for the event, hotels typically include a performance clause in the hotel contract that provides monetary damages if the event organizer's attendees occupy fewer rooms than agreed upon. . . . The increased use of Internet-based travel portals such as Expedia, Orbitz, and Travelocity by many travelers has further eroded the integrity of many housing blocks. Booking outside the block raises daunting and very serious financial and relationship issues for hoteliers and their customers. Event planners can face substantial financial damages, in some cases, even if attendees have secured their housing at the designated hotel but have done so through alternative methods such as an Internet based portal When attendees book outside the block both the planner and supplier can suffer significant financial losses.”

While convention planners hope to reverse the trend, this raises questions about the significance of room block agreements in the future. And it raises questions, too, about whether an agreement that would commit 600 of the 750 rooms at the new hotel to

conventions on a sliding scale will ultimately hurt business at the hotel. Further, if the owner of the hotel, the city, concludes that business is being hurt by setting aside large blocks of rooms, will seek to reduce its commitment in order to free more rooms for leisure and business travelers?

In Sacramento, CA., the management of the publicly owned Sheraton Grand convention hotel, which projects a drop of 2,000 group room nights in 2005, is reducing the amount of convention and meeting business and increasing its tourist/transient business. It has expressed concern that its room block commitment for convention business may hinder this effort, according to a November 2004 report by PKF Consulting.

KEY ISSUES FOR THE CITY COUNCIL TO CONSIDER

- Does Baltimore need a new hotel?
- If so, who should build and own it?
- What is purpose for city ownership of a hotel?
 - To help the convention center?
 - To provide millions of dollars for city coffers on yearly basis?
 - To provide revenue to finance the Baltimore Convention Center deficit, which has doubled in recent years and, after 2008, will be the sole responsibility of the city unless the General Assembly renews the state's obligation to cover two-thirds of the deficit?
 - To provide the city a multi-million asset at no cost to the city?
- Although BDC has said the purpose of this hotel is to increase business at the Baltimore Convention Center, it has offered no data on what, if any, impact new convention headquarters hotels have had on convention center business in other cities.

- In recent years, the city has received at least three developers have proposed to build a convention headquarters hotel on the site for this proposed hotel.
 - Would they be interested today in reviving their proposals?
 - If so, what subsidies would they seek from the city?
 - If not, why not?
 - In their view, is there only one way for this hotel to be built, as BDC asserts?
- BACVA says that over a three-year period Baltimore lost 120,000 room night bookings for lack of a convention headquarters hotel. Had the proposed hotel existed and had it booked all 120,000 of those room nights, those conventioners would have filled only 14.6 percent of available rooms at the hotel.
- Over a recent 19-month period, BACVA says, the city lost 1.2 million room nights when conventions that considered Baltimore before selecting another site. Only five percent of that lost patronage was attributed to lack of a convention headquarters hotel, suggesting that absence of such a hotel is not is not the major reason for the lackluster convention center performance.
- Should the Mayor and City Council approve placing the city in direct competition with the privately owned and operated hotels?
- Would the city and BDC seek to prevent construction of a major, privately-owned hotel on the Light Street of the former McCormick spice plant in order to prevent competition with the proposed city-owned hotel as BDC president Brodie suggested in a June 2005 *Baltimore Sun* article?

- If the economy were to turn sour and produce historic lows in travel and tourism, would the city subsidize room rates in order to boost hotel occupancy?
- If the hotel failed to generate enough revenue to cover operating expenses – seemingly an impossibility under BDC projections -- would the city subsidize the deficit?
- How ironclad will be the agreement of the Hilton Hotels Corp. to set aside 600 of the 750-rooms for conventions?
- In a good economy, would the room block agreement impede or help hotel business?
- If the city must provide generous subsidies in order to get the hotel built, should it provide the subsidies to itself and obtain the benefits of the deal while also shouldering the risk in a business acutely subject to ups and downs of the economy?
- If the private sector were to build and own the hotel, aided by generous city subsidies, would the city be undertaking substantial risk by giving up a valuable piece of property and foregoing property tax and hotel tax revenues generated by the site?
- As the competition among cities for convention business grows more intense, how likely is it that the hotel will fail to attract significant new business to the convention center, given the turmoil in the industry and the increasing amount of convention center space around the country? Can

Baltimore compete with the first-tier convention cities as they increasingly seek the mid-size conventions that are Baltimore's prime target?

- How prudent is it for the city to earmark tens of millions of dollars in city funds for payment of debt service on hotel bonds in the event that hotel revenues are insufficient?
- Do the risks to the city match the projected – and not guaranteed – rewards or is there another way for the city to obtain the reward, that is a 750-room full-service hotel, without shouldering the risk

The City Council Search for Answers

City Council confronts difficult issues here. It is being asked to approve perhaps the biggest public works project in city history and to take – for Baltimore – an unprecedented step in putting the city into the travel and tourism business by making itself a competitor of privately owned hotels.

It should not be enough for the council to say, “Others are doing it, so we should do it, also,” which seems to be the BDC rationale.

The hotel may well be successful, given the strong tourism and business patronage of hotels in Baltimore, without providing substantial help to the convention center.

City Council should not approve this proposal unless the O'Malley Administration offers convincing evidence that other publicly financed hotels have given a major boost to the convention centers they were supposedly built to help.

Before making a decision, the Council should seek more information. Specifically, it should:

- Ask the Baltimore Development Corporation (BDC) to open its records on the hotel to the public – particularly the documentation it used to persuade its advisory panel and its board to approve the selection of RLJ/Quadrangle. This unprecedented \$300 million publicly financed municipal project, should be subject to the fullest public scrutiny.
- Request data on the impact, if any, that new convention headquarters hotels in other cities have had on their convention centers.
- Ask BDC how the hotel can maintain the room rates set forth in April 2005 presentation to City Council and compete other cities, like Louisville, that offer much lower room rates.
- Question developers who have proposed in recent years to build a privately owned hotel with city subsidies and financial guarantees – Peter Angelos, RLJ/Quadrangle and TreyPort LLC. Do they agree with BDC assessment that their proposals were not “viable?” Ascertain if they would be interested today – and if so, under what circumstances and with what subsidies and financial guarantees they would want from the city. Would they be able to obtain private financing?
- Invite Heywood Sanders, author of the report published by the Brookings Institution that questions the value of expanding convention centers and building headquarters hotels to testify. Question him about his report and the state of the convention business.

- Invite Thomas Hazinski of HVS, the city consultant who has criticized Professor Sanders' work, to appear at the same meeting so that they can discuss their differences face-to-face.
- Examine the convention business – the nationwide increase in convention center space and the decline in use of convention center space. Ask experts to testify – and not just proponents of the hotel and promoters of the convention business.
- Invite the operators of existing hotels in the city to testify and discuss the impact this hotel will have on their operations.
- Invite the planners of conventions that have chosen other cities after considering Baltimore to discuss their reasons for rejecting the city.

Only by fully airing the issues, the differences and all the information about this proposal can the City Council get a complete picture of the rewards and risks involved in having the city build and own a hotel.