

Public Benefit Research and Innovation

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September 22, 2014

Honorable Herb J. Wesson, Jr.
President, Los Angeles City council
Councilmember, 10th District
200 North Spring Street, Room 430
Los Angeles, CA 90012

Dear Council President Wesson:

As per your letter of July 7, 2014, we submitted our responses to a series of questions on the proposed hotel minimum wage on September 3, 2014, in advance of the September 8 deadline. Because of this timeline, we did not get the opportunity to discuss the relationship of the hotel minimum wage to the Mayor's proposed city-wide minimum wage, and the related study conducted by the Institute for Research on Labor and Employment at the University of California, Berkeley, released just two days prior. We would like to take this opportunity to supplement our analysis.

Our purpose is not to evaluate the proposed city-wide minimum wage, or the study itself, only the relationship to the hotel minimum wage. The Berkeley study considers the impacts of a phased increase to \$13.25 for all workers, after which wages would rise annually at the cost of inflation. In brief, the study suggests that such an increase would be largely beneficial to the local economy, and that a minimum of negative impacts would occur. It does identify two industries in which some greater effects may be felt—apparel manufacturing and restaurants.

As hotels include restaurants, and some have argued that hotel restaurants should not be treated differently than other restaurants, we felt it appropriate to consider the similarities and differences between the two industries.

First, it is important to note that the Berkeley study does suggest that in San Francisco, which has a city-wide minimum wage, the effects on restaurants were minimal, though not insignificant. Moreover, the study cites other analyses that indicate limited effects in other cities.

Nonetheless, it is important to consider, are hotels different from other industries, and should the city see them differently, in setting a minimum wage?

In some senses, cities, including Los Angeles, already do. Hotels are both uniquely subsidized and uniquely taxed. Cities have long recognized the need to stimulate tourism and have supported hotels in order to achieve that goal, for example, by building convention centers, which are often loss leaders, supporting marketing through convention and visitors bureaus and by directly subsidizing the construction of new hotels or the renovation of existing hotels. Many of Los Angeles's hotels have been built with such supports over the years.

Similarly, virtually all cities have a transient occupancy tax (TOT) or bed tax, paid by those who stay in hotels. This is one of the few, and one of the largest, specific taxes the city of Los Angeles has in one industry. The rationale, as we noted in our 2006 report "*From the Pockets of Strangers*," is both that cities can gain revenue from non-residents and that hotels are generally generating this revenue from relatively well-heeled travelers for whom an additional tax is not a great disincentive.

Such effects can be seen in hotel prices, which are widely variable. The cost of most goods or services is determined in part by the cost of producing them, and in part by the local economy—that is, the ability of local consumers to pay. Restaurant prices, for example, do not increase and decrease dramatically day to day because the local market has a meaningful role in determining those prices. Alternatively, hotel prices may be significantly different from week to week, month to month or year to year. They are set not by the local economy but by demand, which is generated externally, or by special offerings such as a convention.

As of this writing, Los Angeles County is experiencing record room rates and occupancy. According to Smith Travel Research, August was the best month ever on both counts in our history, and room rates leapt up \$10 from the previous record set in July to a County-wide average of \$164.

As a point of comparison, a decade ago, we found the County-wide average was \$96 a night. Such increases are dramatically larger than increases in the costs of meals, and reflect the attractiveness of travel.

A second factor to consider is the impact on payroll and workers. In our 2013 study, *“Effects of a Fifteen Dollar an Hour Minimum Wage in the City of Los Angeles,”* we looked at which workers were paid the lowest, and which industries would have the greatest impact on payroll and revenue.

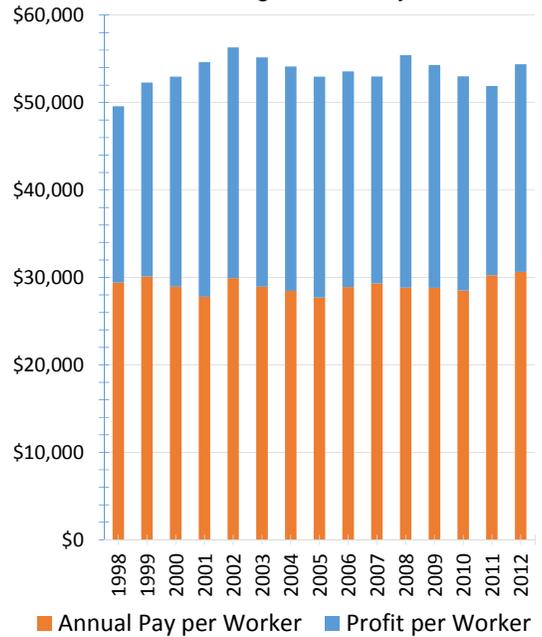
In that study, we considered restaurants and accommodations together, and found that the wage increase in those two industries would be 14% of industry revenue, second to agriculture in costs, while we found that 68% of workers in the two industries made below \$15, far and away the greatest percentage.

However, in our *Repaying Hospitality* report later in the year, we looked only at the hotel industry, and found that the increased costs would represent approximately 4-5% of hotel industry revenue, while roughly 81% of hotel workers make below the proposed wage of \$15.37.

Overall, this would mean that while the hotel industry has one of the highest percentages of workers below the proposed wage, it is in the lower tier of industries in terms of costs to increase wages. The average wages paid to hotel workers in Los Angeles County and the average industry profit per worker is shown in *Figure 1*. The average annual wage in 2012 was \$30,632 and the average annual profit per worker is \$23,763 (adjusted to 2014 dollars).

If the total cost of increasing the minimum wage for hotel workers to \$15.37 was taken out of industry profits, rather than offset by small increases in room rates, industry profits would drop from \$0.78 to \$0.72 per \$1.00 in wages paid to workers, as shown in *Figure 2*.

Figure 1
 Annual Hotel Profit and Wages per Worker in Los Angeles County



Source: Economic Roundtable analysis of payroll data from County Business Patterns and profit from IMPLAN. Both in 2014 dollars.

Figure 2
 Impact of Raise LA on Hotel Profit per Worker



For every dollar spent on wages, the hotel earns 78-cents profit.



For every dollar spent on wages, the hotel earns 72-cents profit.

Source: Economic Roundtable analysis of payroll data from County Business Patterns and profit from IMPLAN. Both in 2014 dollars.

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Finally, we'd like to make one additional note about the hotel industry relative to other industries—ownership structure and capitalization. In 2013, there were 180 hotels sold in California for a total of \$2.2 billion, an average price of \$122 million per hotel. This price includes hotels both above and below the number-of-rooms threshold for this ordinance. To afford this, hotel owners are generally large, well-capitalized companies, and have varied and diversified holdings. Few if any hotels covered by the proposed ordinance do not fit this description.

Such statistics are not easily available for restaurants, in part because the industry is so varied. The costs of building or purchasing a taco stand versus a McDonalds versus a high end eatery vary widely. It is unlikely, however, that many restaurants are as well capitalized as even the least successful hotel covered by the proposed ordinance.

In short, it is our opinion that the hotel industry differs in key ways from many other industries in the city. It is a low-wage industry that is highly capitalized and highly subsidized, and its revenues are far less dependent on local consumer purchases than other industries. For that reason, we believe it is appropriate for the council, if it so choose, to treat the hotel industry in a manner separate from other industries.

We are available to answer any questions the City Council may have about the information provided in this supplemental letter.

Sincerely,



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