

# Carmel's financing, ownership, of \$40 million luxury hotel creates the opportunity for risk or reward

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Chris Sikich

City bonds will pay for nearly half of a planned \$40 million boutique hotel for downtown Carmel. Now taxpayers could be asked to pay even more of the cost. Dwight Adams / IndyStar

(Photo: Provided by City of Carmel)

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Carmel, Ind. — Mayor Jim Brainard is negotiating a deal for Carmel to become deeply involved in financing, owning and operating a \$40 million luxury hotel, which is raising questions about the rewards and risks of the city's increasingly aggressive approach to redevelopment.



The mayor thinks the Hotel Carmichael is the missing piece in the suburb's emerging downtown, a lure for business executives, tourists catching a show at the Palladium and residents who want a night on the town.

The highlight of the five-story classically designed building will be crooner Michael Feinstein's nightclub, a cabaret dinner-and-music venue similar to his Club 54 Below in Manhattan. The mayor also envisions the hotel's luxurious, colonnaded grand lobby as a gathering place where people will grab a beverage and hang out.

Brainard persuaded the City Council, despite misgivings from some members, to approve \$18 million in bonds for construction late last year. Now, he's negotiating with banks for a city-backed loan to cover the remaining \$22 million.

Taxpayers already are on the hook for the bonds, to be paid back over 20 years through income taxes and business property taxes. The city estimates hotel revenues will pay back the loan, cover all of the hotel's operating expenses and deliver a healthy surplus the city can reinvest in other projects.

In reality, though, no one knows precisely how many people will book rooms at the hotel, frequent the restaurant or visit the nightclub, and in the worst-case scenario taxpayers could be asked to pay back the loan or cover operating deficits.

Brainard insists the city's financial projections are sound and any risk is slight.

"We wouldn't do it if we didn't believe that the risk had been reduced to the point where taxpayers are protected and the reward is substantial," he said. "These are all pieces of a puzzle that fit together to make us very effective when attracting economic development."

But it's also clear that the private sector viewed the hotel as too risky to build without significant government help. Some financial experts say that should have been a warning sign to stop. Others question why the city is competing with the private hotels thriving nearby.

"If the private sector won't build it," asked [Michael Hicks](#), director of the Center for Business and Economic Research and professor of economics at Ball State University, "how is government going to be more effective?"

In the past, Carmel taxpayers have been bitten by ambitious financial projections, and the city was forced to pump millions of dollars into projects originally touted as being more self sufficient, including The Center for the Performing Arts and the Monon Community Center.

For the hotel project, the full extent of the risk versus the reward will be in the details. Brainard plans to submit the hotel's public-private partnership and financial plan to the City Council as soon as next month.

**Carmel 'played our hearts out': [Greyhounds see title slip away in Class 4A loss to Warren Central](#)**

## Striking a deal

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Carmel and [Pedcor](#), the Carmel-based firm behind the City Center development, are creating an involved public-private partnership to build, own and manage the hotel.

Hotel Carmichael — a play on Carmel and Michael Feinstein, artistic director at The Center for the Performing Arts — will be built directly east of the Center for the Performing Arts in the L-shaped open space at City Center. The front entrance and grand lobby will lead out to the elevated parking platform along City Center Drive and Veterans Way, and the hotel will have a walk-out floor along the Monon Greenway below.



THE Carmichael

Conceptual Image

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Hotel Carmichael (Photo: Provided by City of Carmel)

In addition to the nightclub and ritzy lobby, the hotel will feature 122 rooms, a full-service restaurant, private dining, outdoor seating and conference space.

"It's important to have a hotel of this quality at the center of our city to be able to continue to attract corporate headquarters to the area," Brainard said. "It's a piece that's been missing and will make our job much easier when we make our pitch to corporate customers."

The city and Pedcor will create a public-private entity to own the hotel. That entity will contract with a management group to run the hotel, most likely Coury Hospitality, an Oklahoma-based consultant advising the city on the development.

Owner Paul Coury told the City Council last year there is too much risk for the private market to solely fund a full-service, luxury hotel in a city the size of Carmel, especially away from a regional commercial corridor such as U.S. 31.

That came as no surprise to Carmel officials, who had been trying to lure a hotel to City Center since construction started on the massive redevelopment in 2004.

The \$40 million estimated price tag includes \$27 million for construction, \$3 million to pay Pedcor for the use of its land and other infrastructure costs, \$2.8 million for various consultants, \$300,000 to license the Marriott brand and the remainder for legal, contingency and other fees.

The city hired Coury because his niche is working with Marriott to develop hotels in its upscale Autograph Collection series. Each hotel in the series has its own name, branding and design.

There are 82 in the United States, many in large cities such as New York, Phoenix and San Diego.

Coury anticipates 70 percent occupancy at an average of \$198 per room in the hotel's first full year in 2020, rising to 77 percent occupancy at an average \$250 per night in 2028. He said that's less than half what such a hotel could charge in a large market.

Based on those figures, he estimates the hotel will generate \$9.6 million in 2020, including income from renting rooms and other spaces, plus the sale of food and beverages. He thinks that will rise to \$14 million in 2028.

He estimates the net revenue after all expenses, including management fees and debt, to be \$1 million in 2020 rising to \$1.3 million in 2028. Once the debt is paid off in roughly seven years, 66.7 percent of revenue will go toward the city and 33.3 percent to Pedcor. After 10 years, the company and the city will split the revenue evenly.

Indianapolis has brokered deals with hotels, though none with the same ownership stake as Carmel. Those deals have had mixed success at earning taxpayers a profit so far.

Indianapolis has an 8 percent stake in the Conrad and provided \$25 million toward the \$100 million development. The Conrad has paid Indianapolis \$1.2 million since 2010, according to city spokeswoman Taylor Schaffer.

The city has yet to see a dime on another investment. Indy provided \$59.5 million toward the \$450 million JW Marriott in 2008 in return for 25 percent of annual profits after the hotel reaches a certain profit margin.

There's more room for caution. The occupancy rate at Hamilton County hotels was 68 percent in 2017, below what Carmel expects to see in its first year. Carmel's consultants, though, are confident the downtown hotel will be much more of a draw than the average county inn.

Brenda Myers, executive director of Visit Hamilton County, said demand for hotels is increasing, with overall room bookings up 10 percent year over year.

She said some of the hotels within the county have occupancy rates as high or higher than what Carmel predicts, particularly those that target business clients.

"I can't speculate (on the success of Carmel's hotel) without understanding their market mix," she said, "But I don't think their estimates are unrealistic."

## Past missteps

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Carmel's financial projections have been wrong in the past. While Brainard said the city has learned from experience, some financial experts say there's cause for concern.

The city pays more than \$2 million annually to subsidize The Center for the Performing Arts, despite an initial \$307,000 worst-case scenario made before the scope of the project was doubled. At the Monon Community Center, taxpayers contributed \$1 million annually in 2008

and 2009, before staff implemented a more efficient rate structure to raise revenue and better managed stafexpenses to operate within the budget.

City equity ultimately will back the loans for the hotel, according to a Request for Bid released to financial institutions. The specific terms of the city's deal with Pedcor have yet to be revealed, so it's unclear whether the developer will provide financial guarantees to protect taxpayers.

Both the mayor and Pedcor officials downplayed the possibility of a revenue shortfall. But both also declined to say who would be responsible for covering a shortfall should one occur.

"Both Carmel and Pedcor will benefit if the project is successful and will lose if the project is not successful," said Melissa Averitt, Pedcor's senior vice president. "However, given the low leverage and anticipated high debt service coverage ratio of the project, the failure of the project is very unlikely."

The Hotel Carmichael. (Photo: Provided by City of Carmel.)

Hicks, the Ball State economist, said he's generally supportive of Carmel's redevelopment but thinks making long-term commitments to operate a hotel is too risky.

"When you build things, you have a very good idea of your long-term cost," he said. "The minute you start doing operations, you open yourself to uncertainty."

The other concern, he said, is the private sector is better suited to make the harsh decisions needed to turn a profit. As long as the city is involved, he said, the first thought could be to provide excellent service, even if it's expensive, rather than to make money.



"I stayed at a state park in Ohio recently," he said, "and when the staff came to clean my room in the morning there were four of them. The public sector's first thought is how to do it well, not how to make money."

For proof, one need look no further than Carmel. The city has decided funding certain amenities is worth the price, including a Christmas market, ice-skating rink and golf course.

This year, the city anticipates supplementing Brookshire Golf Club with \$200,000, granting Carmel Christkindlmarkt \$125,000 and paying a management contract of \$61,918 for the ice skating rink.

Brainard sees funding certain amenities as a civic service, akin to the city's responsibility to pay for police and fire protection. No one, he said, expects police and fire departments to turn a profit.

He thinks the payoff in developing Carmel's downtown and supporting cultural amenities,

though, is clear.

"Carmel has gone beyond what most suburbs have been able to do by building a walkable, pedestrian friendly downtown," he said. "Twenty years ago, Carmel was like a hundred other suburbs in the United States."

Industry experts say it's rare for a city the size of Carmel to become so deeply involved in building and owning a hotel, though cities do sometimes provide subsidies.

Noblesville, for instance, contributed \$6 million toward the \$30 million Embassy Suites, the largest hotel conference center in the county.

Daniel Lesser, president and CEO of New York-based LW Hospitality Advisers said the use of tax dollars to subsidize hotels with convention space has become fairly common.

Lesser said large-scale hotel development projects are expensive and considered high risk, because of the potential for low return on investment.

He thinks hotels subsidized by cities, particularly those with convention space, do drive economic development and widen the tax base. He said there's no shortage of both success stories and ill-conceived projects.

"The results of each investment is highly dependent on the submarket demand for a specific project and the economic structure of the deal," he said.

Carmel already has incurred costs for the hotel beyond construction.

The Carmel Redevelopment Commission hired Coury in May 2017 for \$20,000 a month to oversee development. That will fall to \$15,000 a month this April, May and June and to \$10,000 a month in July.

In addition to paying Coury, the commission has agreed to pay California-based Hirsch Bedner Associates \$460,000 for interior design, Kansas City-based MMGY Global \$89,500 to develop branding and Los Angeles-based architect David Schwarz up to \$600 an hour for consulting.

## What's next?

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The City Council will have the final say in whether the hotel moves forward, and approval seems likely.

The council voted 5-2 in September for \$96 million in bonds for a variety of projects, including \$18 million for the hotel. Council members Tony Green and Laura Campbell voted against the bonds, saying they were opposed to the city inserting itself into the private marketplace.

They were echoing the concerns of some of the city's hoteliers, who worry Carmel's ability to fund a hotel with taxdollars will create an uneven playing field.

Who pays for potential shortfalls might be a sticking point in the next vote.

Sue Finkam, the City Council's finance committee chair, said the council has no appetite to fund potential shortfalls, short of some sort of natural disaster.

"We hired a consultant who has expertise in the field so our projections are as close to realistic as possible," she said. "I know the council will not be interested in funding a shortage."

John Stafford, former municipal finance adviser to Fort Wayne and Allen County, said Carmel is in a much more advantageous position to make such decisions than most Indiana cities.

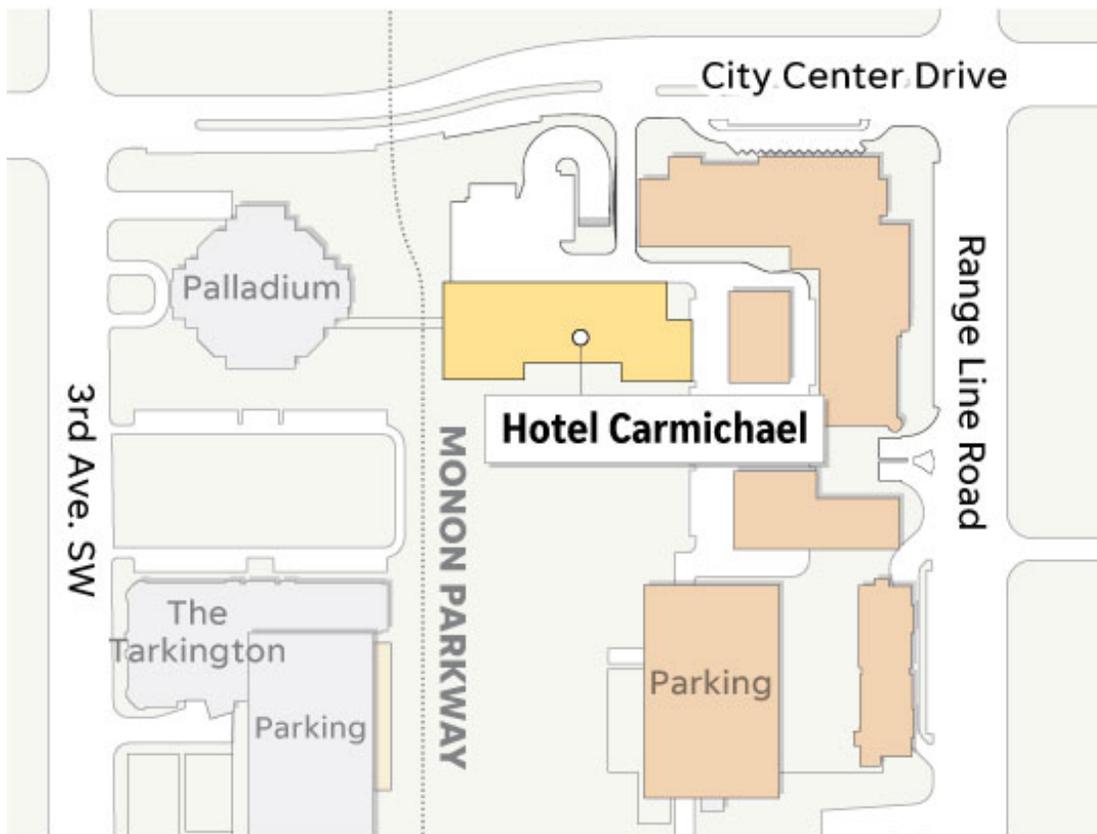
He said it's become crucial for local government to attract and retain a well educated and talented workforce and each community is going to have to decide what's an appropriate risk or reward.

He advises communities to ask one question, in particular.

"What is the worst-case scenario and what is the game plan for covering it? You are dealing with taxpayer money and you have to be cognizant of that."

## CITY CENTER COMPLEX

Carmel plans to begin construction on the Hotel Carmichael in 2019. The hotel will have 122 rooms, a full-service restaurant, night club, private dining, outdoor seating and conference space.



SOURCE: City of Carmel

STEPHEN J. BEARD / INDYSTAR