Proposed TOT Rate Increase on Hotels in Carmel-by-the-Sea

Preface

The Carmel City Council is considering placing a 20% increase in the Transient Occupancy Tax (TOT) this fall, raising the hotel tax rate from 10% to 12%. With the existing 2% Hospitality Improvement District (HID) assessment, the total effective tax on visitors would increase to 14%.

This paper evaluates the potential impacts of that increase using local operating data, 12-month trailing performance trends, and comparable market case studies. The analysis focuses not just on tax rates, but on **how changes in total visitor cost affect demand, competitive positioning, and long-term tax generation**.

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1. Exhibit A

Strong Organic Growth Without Tax Increases

Exhibit A demonstrates that since the creation of the HID in 2013, Carmel's lodging market has significantly outperformed inflation. RevPAR has grown at an average annual rate of 9.4%, compared to 3.8% CPI, representing a substantial gain in real pricing power.

This growth has occurred despite major disruptions, including COVID and periods of reduced room supply due to renovations. It reflects two structural drivers: targeted marketing through the HID and sustained reinvestment in the lodging product.

Importantly, this RevPAR growth has translated directly into increased TOT revenue without raising tax rates. The data shows that **strong demand and pricing power, not higher tax rates, are the primary drivers of tax revenue growth**.

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2. Exhibit B

Tax Rate vs. Tax Productivity

Exhibit B compares TOT revenue per room across Monterey Peninsula jurisdictions. Carmel, with a 10% TOT rate, generates significantly more TOT per room than markets with higher tax rates.

For example, jurisdictions with 12% to 14% tax rates produce materially lower TOT per room due to weaker ADR and RevPAR performance. This demonstrates a critical point: **Higher tax rates do not compensate for reduced competitiveness.**

Instead, markets that maintain pricing power and demand generate the strongest fiscal outcomes, even at lower tax rates.

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3. Exhibit C

Case Study: Occupancy Impact of Tax Differentials

Exhibit C examines Half Moon Bay, where the city increased its TOT from 12% to 14%, and later to 15%, while nearby unincorporated hotels remained at a lower rate.

Prior to the increase, both markets performed similarly. Following the increase, a persistent occupancy gap emerged, with city hotels underperforming nearby competitors by approximately 8 to 10 percentage points.

This case study illustrates how **tax-driven price differences can shift demand across closely competing markets**, resulting in fewer overnight visitors and reduced local economic activity in the higher-tax jurisdiction.

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4. Exhibit D

Case Study: Competitive Share Loss and Acceleration Effects

Exhibit D evaluates Buellton's TOT increase from 12% to 14% using **share of occupancy and RevPAR within a competitive set of destinations, reported bi-monthly by Visit Carmel and measured on a 12-month trailing basis**.

The data shows that Buellton's occupancy share declines from approximately 17.6% to 17.0%, while Carmel's increases from roughly 17.1% to 17.8%.

The effect is more pronounced in RevPAR share, where Buellton declines from about 8.8% to 8.4%, while Carmel increases from approximately 14.8% to 15.9%.

While some divergence was already present prior to the tax increase, the key insight is that **the rate of divergence accelerates following the increase**, particularly in RevPAR.

Because these metrics measure **relative share within a competitive set**, the shift indicates that demand is not disappearing, it is being redistributed away from higher-cost markets.

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5. Exhibit E

Modeled Demand and Revenue Impact

Exhibit E applies established price elasticity research to Carmel's lodging market.

A 2% increase in TOT is projected to reduce demand by approximately 1.5% in upscale hotels and 2.7% in luxury hotels. This equates to roughly 5,000 fewer annual room nights.

The estimated financial impact includes:

- $1.8 to $2.1 million in lost hotel revenue
- Approximately $1.5 million in reduced local business revenue
- Secondary reductions in sales tax and broader economic activity

While the City would collect a higher tax rate on remaining demand, a portion of that gain is offset by reduced volume and downstream economic effects.

Conclusion

Across all exhibits, a consistent pattern emerges:

- **Exhibit A** shows that Carmel is already generating strong, above-inflation revenue growth without increasing tax rates.
- **Exhibit B** demonstrates that higher tax rates do not produce higher tax revenue per room.
- **Exhibit C** shows that tax increases can lead to sustained occupancy losses relative to nearby competitors.

- **Exhibit D** confirms that higher tax environments lose share within a competitive set, with effects that accelerate over time, particularly in revenue performance.
- **Exhibit E** quantifies the expected demand and revenue losses from a rate increase.

Taken together, the data indicates that increasing the TOT rate introduces **long-term competitive risk**. It places upward pressure on pricing, reduces demand, and shifts overnight visitors to alternative markets. Over time, this leads to declining share of both occupancy and RevPAR, weakening the very foundation that drives TOT revenue.

Carmel's current model, built on reinvestment, strong pricing power, and disciplined marketing through the HID, is already producing increasing tax revenues and a healthy lodging market.

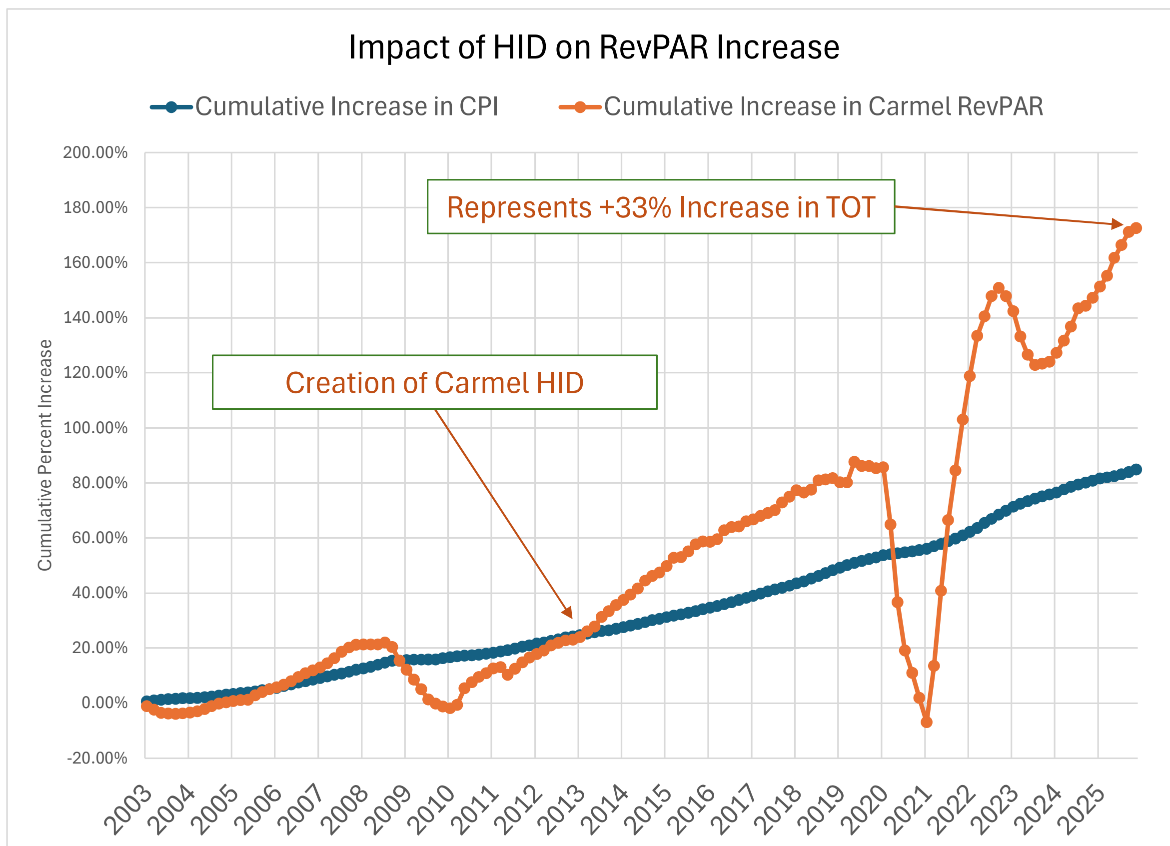
Maintaining that model, rather than increasing the tax burden, is the more reliable path to sustained economic growth and long-term fiscal stability.

Exhibit A

Carmel Hotel RevPAR vs CPI Since Creation of HID

Cumulative, 2003 to Sep-Oct-2025

	Carmel RevPAR	CPI	Delta
Avg 12-Month RevPAR Incr. since HID (2013)	9.4%	3.8%	149.1%
Avg 12-Month RevPAR Increase 2002 to 2012	2.3%	2.4%	-5.0%



Summary

Since the HID's creation in 2013, Carmel hotel RevPAR has grown at an average annual rate of 9.4%, significantly outpacing CPI at 3.8%, a +149% relative gain over inflation. This performance has occurred despite major disruptions, including the COVID-19 downturn and recovery, as well as a multi-year period (2021–2023) when a meaningful share of hotel inventory was offline due to renovations, constraining both demand and available room supply.

This sustained outperformance is not incidental. It reflects two primary structural drivers. First, the creation of the HID enabled hotel operators to self-assess and reinvest directly into targeted marketing, strengthening Carmel's competitive position and increasing market share against other coastal destinations. Second, significant reinvestment in the physical product has elevated the overall quality of the lodging inventory. To date, approximately 127 rooms (13% of inventory) have been renovated. An additional 57 rooms are currently under renovation and expected to return to service before this summer, with another 94 rooms committed to renovation over the next 12 months, further supporting rate growth and demand.

Applying CPI-level growth to the City's 2012 TOT base yields approximately $7.0 million in annual TOT by 2025, while RevPAR-driven growth implies roughly $13.5–$14.0 million, a difference of $6.5–$7.0 million annually. While real-world disruptions limited full realization in certain years, actual TOT still increased by approximately $2.3 million (+33%), demonstrating that stronger RevPAR growth has translated into meaningful tax revenue gains. Looking forward, continued marketing investment through the HID and ongoing property reinvestment position Carmel to sustain above-inflation RevPAR growth and continued expansion in TOT revenues.

Exhibit B

2025 TOT Production by Jurisdiction

City	Rooms	Occ%	ADR	RevPAR	TOT Rate	TOT	TOT/Rm	Source
Monterey County (unincorporated)	1,815	71.1%	$ 394	$ 279.83	10.5%	$ 19,459,678	$ 10,724	A
City of Carmel-by-the-Sea	**970**	**69.2%**	**$ 381**	**$ 263.58**	**10.0%**	**$ 9,527,386**	**$ 9,822**	**D**
City of Monterey	4,729	71.1%	$ 235	$ 167.14	12.0%	$ 34,620,131	$ 7,321	A
City of Pacific Grove	951	n/a	n/a	$ 164.62	12.0%	$ 6,857,000	$ 7,210	B
City of Marina	980	69.1%	$ 188	$ 129.64	14.0%	$ 6,492,037	$ 6,625	A
City of Seaside	665	n/a	n/a	$ 140.76	12.0%	$ 4,100,000	$ 6,165	C

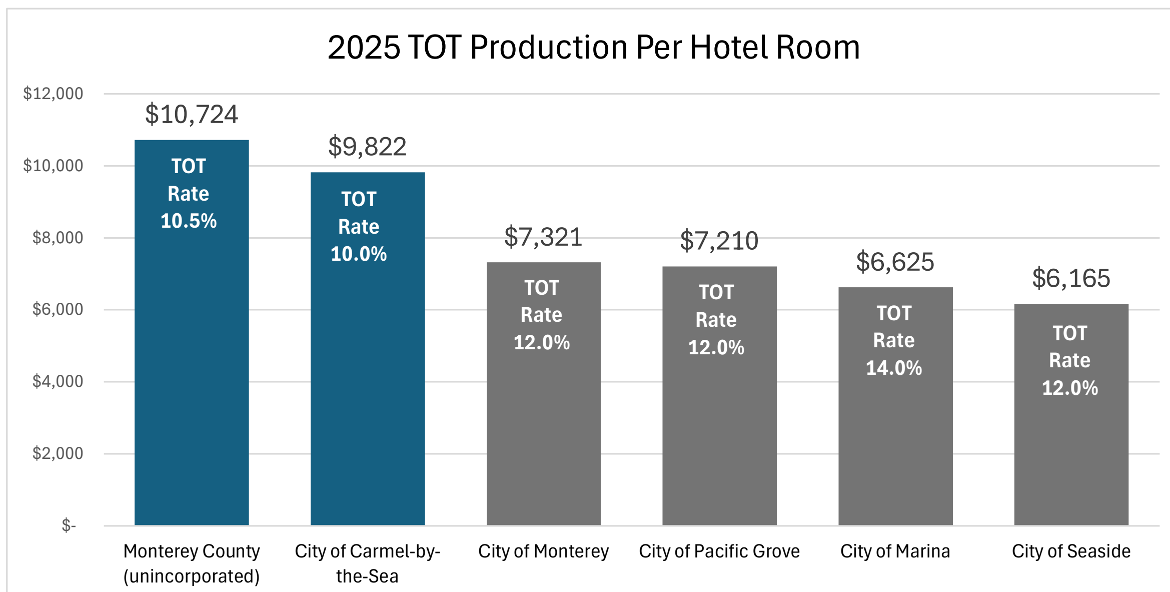
Source:

A See Monterey/STR

B City of Pacific Grove FY 2025-26 Budget, exlcuding Kimpton Hotel

C City of Seaside FY 2025-26 Budget

D City of Carmel TOT Reporting, 12 months ending October 2025



Sources: City of Carmel-by-the-Sea and See Monterey

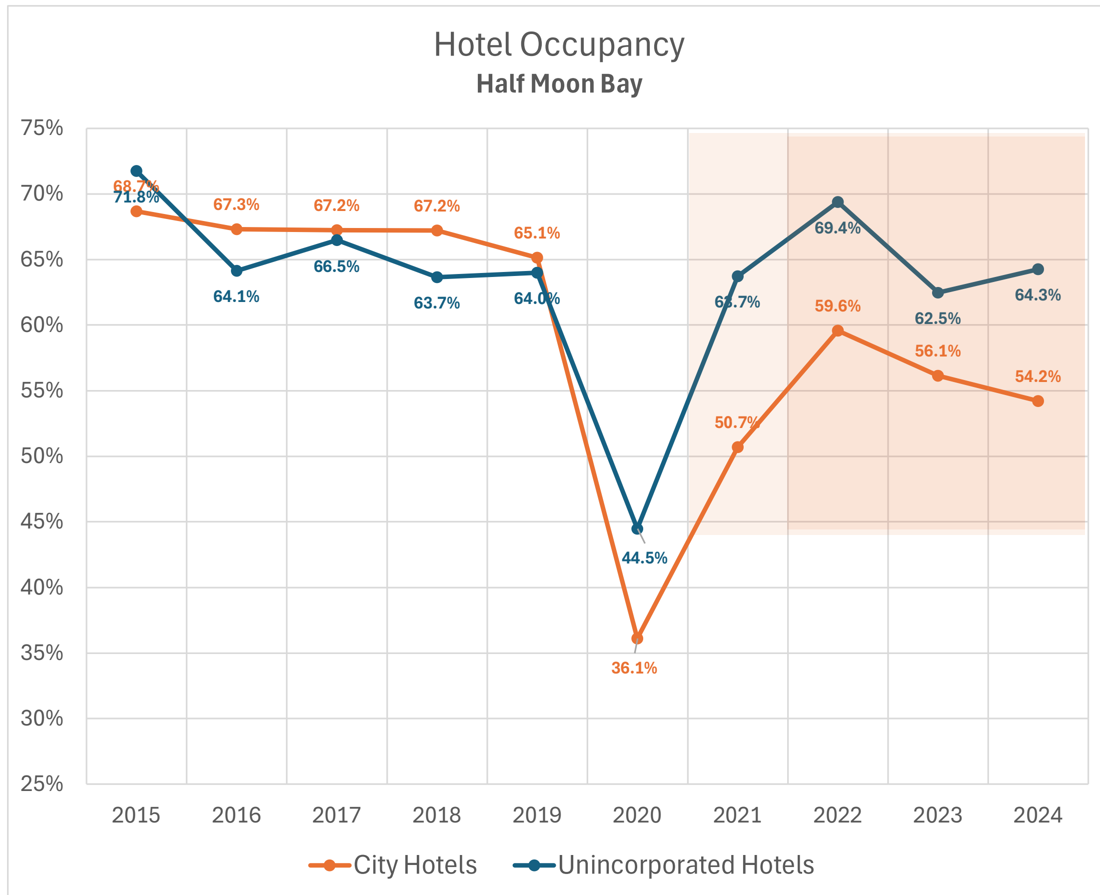
Summary

This analysis highlights a clear and consistent relationship between pricing power, RevPAR, and Transient Occupancy Tax production per room, rather than between higher tax rates and stronger fiscal outcomes. Jurisdictions with the lowest TOT rates and highest RevPAR, notably Carmel-by-the-Sea (10.0%) and unincorporated Monterey County (10.5%), generate the highest TOT per room, at $9,822 and $10,724 respectively. These outcomes are driven by materially higher ADRs and RevPAR, which more than offset their lower tax rates. Carmel serves as the baseline comparator, with several neighboring cities producing 34% to 59% less TOT per room despite higher nominal tax rates.

Conversely, cities that have adopted higher TOT rates (12% to 14%) but operate in lower-ADR, lower-RevPAR markets show substantially weaker per-room tax productivity. Marina, despite the highest TOT rate at 14.0%, generates only $6,625 per room, 48% below Carmel, while Seaside produces just $6,165 per room at a 12.0% rate, 59% below Carmel. The data suggests that raising TOT rates does not compensate for weaker demand fundamentals and may, in fact, reflect structural limitations in pricing power rather than a viable revenue-maximization strategy. The most fiscally efficient jurisdictions remain those that protect rate competitiveness while sustaining strong lodging economics.

Exhibit C

Case Study: Occupancy Impact of Half Moon Bay's TOT Increase



Summary

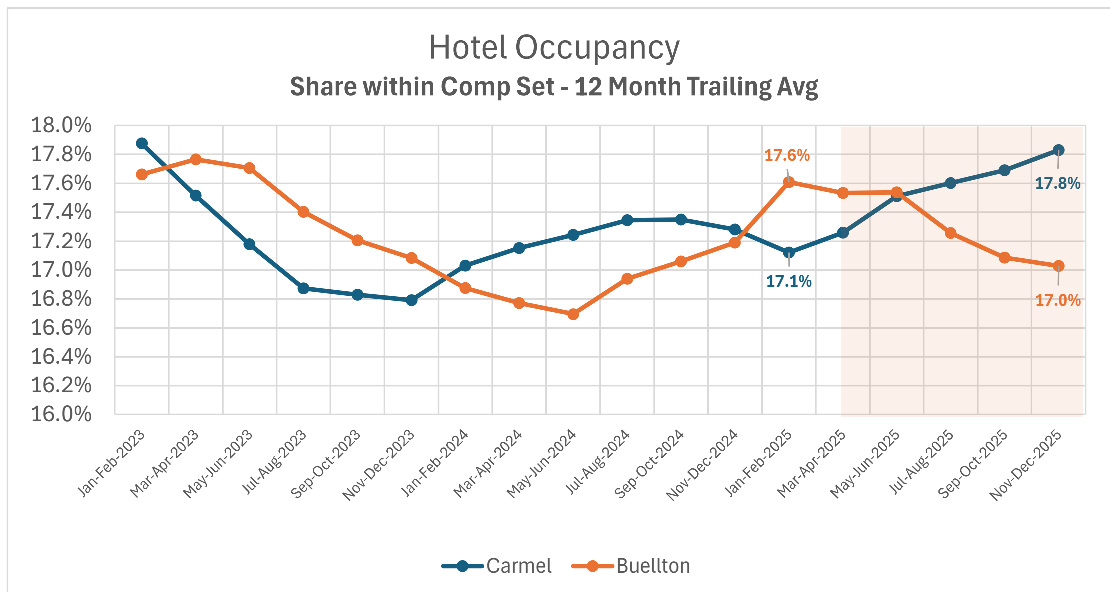
Before the pandemic, hotels inside the City of Half Moon Bay and those in nearby unincorporated areas performed similarly. From 2015 to 2019, city hotels paid a 12% hotel tax, while unincorporated hotels paid 10%, yet both areas recorded occupancy in the mid-60% range. This period establishes a clear baseline showing that the two markets were competitive prior to any tax changes. The sharp decline in 2020 reflects COVID-related shutdowns and is excluded from this comparison.

In July 2021, the City raised its hotel tax from 12% to 14%, while the unincorporated rate remained unchanged. In 2021, city hotels recorded 50.7% occupancy, compared with 63.7% in the unincorporated area. The City increased the tax again in July 2022, raising it to 15%. In 2022, city occupancy reached 59.6%, while unincorporated hotels reached 69.4%. City hotels continued to underperform in 2023 and 2024, trailing the unincorporated area by roughly 8 to 10 percentage points. From 2021 through 2024, city hotels sold approximately 86,000 fewer room nights than they would have if they had matched the occupancy levels of nearby unincorporated hotels. This represents about 10% of the City's potential room nights during that period. Fewer occupied rooms translate into fewer overnight visitors in the City, which has significant implications for businesses that rely on visitor activity. While the data does not prove the tax increases caused the decline, the timing and persistence of the gap raise questions about the impact of higher hotel tax rates on lodging demand.

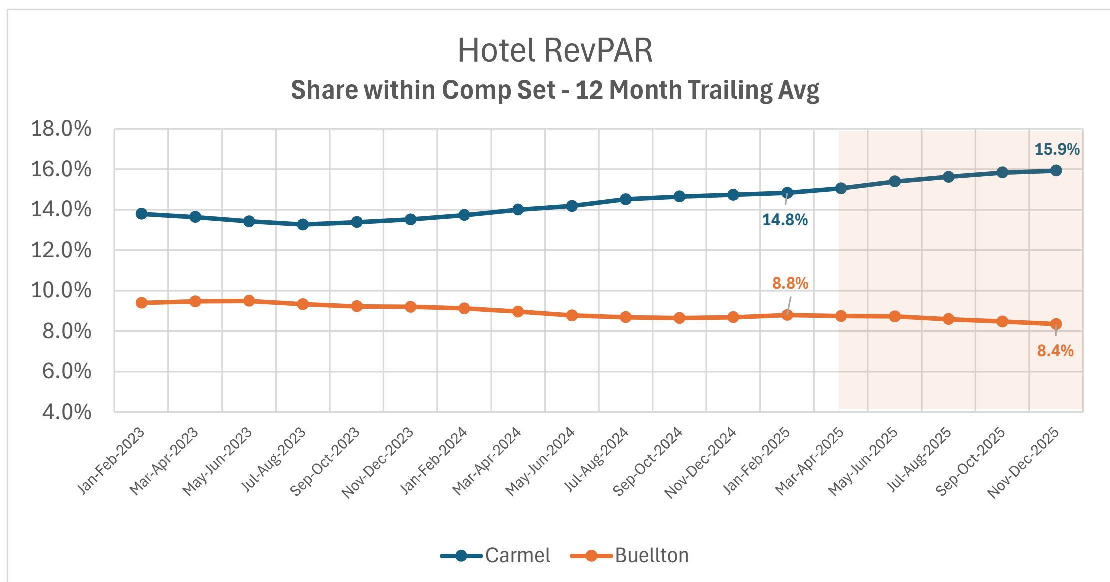
"*The data shows that hotels in the unincorporated County have bounced back better than those inside the City. When the City discussed raising the hotel tax, the Chamber and local hotels warned that higher costs could put City hotels at a disadvantage compared with nearby County properties that stayed at a 10% tax rate. Since then, City occupancy has slipped relative to those properties, which is clear from the data.* " - Krystlyn Giedt, CEO of HMB Coastside Chamber

Exhibit D

Case Study: Buellton TOT Increase and Trending Revenue Decline



Occupancy Comp Set includes: Carmel, Buellton, Calistoga, Monterey, SLO City and Yountville



RevPAR Comp Set includes: Carmel, Buellton, Calistoga, Monterey, Santa Barbara, SLO City and Yountville

Summary

Following Buellton's TOT increase from 12% to 14% in February 2025, its share of room demand within a competitive set of destinations, as reported bi-monthly by Visit Carmel, shows a continued and then accelerated divergence on a 12-month trailing basis. While some softening in occupancy share was already underway prior to the increase, the decline persists and deepens over time, indicating a sustained loss of demand relative to competing markets. Carmel, by comparison, maintains a stable to slightly improving share. The effect is more pronounced in RevPAR share of the comp set. Although modest divergence was visible prior to the tax change, the gap widens more rapidly following the increase, with Buellton's share eroding and Carmel's continuing to strengthen. Because these metrics reflect relative performance across destinations, the post-increase acceleration suggests demand is shifting away from higher-tax markets. Overall, the data indicates that higher TOT rates amplify existing competitive pressures, reducing price competitiveness and leading to a measurable loss of both occupancy and revenue share within the comp set over time.

Exhibit E

Price Elasticity of Demand of Hotel Rooms and TOT Increase

From UMASS Study: https://scholarworks.umass.edu/cgi/viewcontent.cgi?article=1291&context=jhfm

Price Elasticity of Demand = % Change in Quantity Demanded / % Change in Price		
Upscale Hotels	-0.75	
Luxury Hotels	-1.36	
Price Increase via TOT Increase	**2.0%**	(Proposed by Carmel City Council)

Expected % Change in Quantity Demanded	Demand	Inventory	ADR
Upscale Hotels	-1.5%	55%	$ 275.00
Luxury Hotels	-2.7%	45%	$ 530.28

Base for Calculations	12-Months Ended December 2025
City of Carmel TOT	$ 9,533,718
City of Carmel Room Nights	244,531
TOT per Room Night	$ 38.99
Occupancy	69.4%
ADR	$ 389.88

Year 1 Expected Reduction in Room Nights	Demand Lost	Lost Hotel Revenue	Lost Retail Revenue	**Total Lost Revenue**
Upscale Hotels	-2017	$ (554,675)		
Luxury Hotels	-2993	$ (1,587,139)		
Total	-5010	$ (2,141,814)	$ (1,521,081)	**$ (3,662,895)**
Year 1 Lost Tax Revenues from Demand Reduction		$ (214,181)	$ (140,700)	**$ (354,881)**

Resultant TOT @10%	$ 9,319,537
Increase in TOT from Rate Increase (2%)	$ 1,863,907
Reduction in Sales Tax Revenues	$ (140,700)
Effective Net Tax Revenue Increase	$ 1,723,207

Purpose

This one-page summary explains how a TOT increase affects visitor demand, hotel performance, and local tax revenues using elasticity research and Carmel operating data.

How Demand Responds to Higher Prices - Research shows that when total room price rises, demand declines. Luxury coastal markets like Carmel are more price-sensitive than average destinations. A modeled 2% increase in TOT is expected to reduce demand by roughly 1.5% in upscale hotels and 2.7% in luxury hotels.

Estimated Impact on Carmel Lodging - Based on historical occupancy levels, this demand shift equates to approximately 4,900–5,900 fewer annual room nights and about $1.7M–$2.1M in lost hotel revenue. While the City collects a higher tax rate on remaining bookings, reduced demand offsets a portion of that gain.

Secondary Economic Effects - Fewer visitors reduce spending at restaurants, retail shops, and attractions. Estimated merchant revenue reductions approach $1.5M annually. Lower hotel profitability can also limit reinvestment in maintenance, renovations, staffing, and wages.

Long-Term Considerations - If visitor spending grows about 4% annually, a 2% TOT increase effectively captures roughly half of that growth for the City while slowing hotel revenue growth. Over time this may impact competitiveness, reinvestment, and job stability within the tourism sector.

Key Takeaway - A TOT increase may raise municipal revenue in the short term, but elasticity modeling shows it also reduces demand in a price-sensitive luxury market. The net effect includes fewer room nights, lower visitor spending, and potential pressure on the broader local economy.

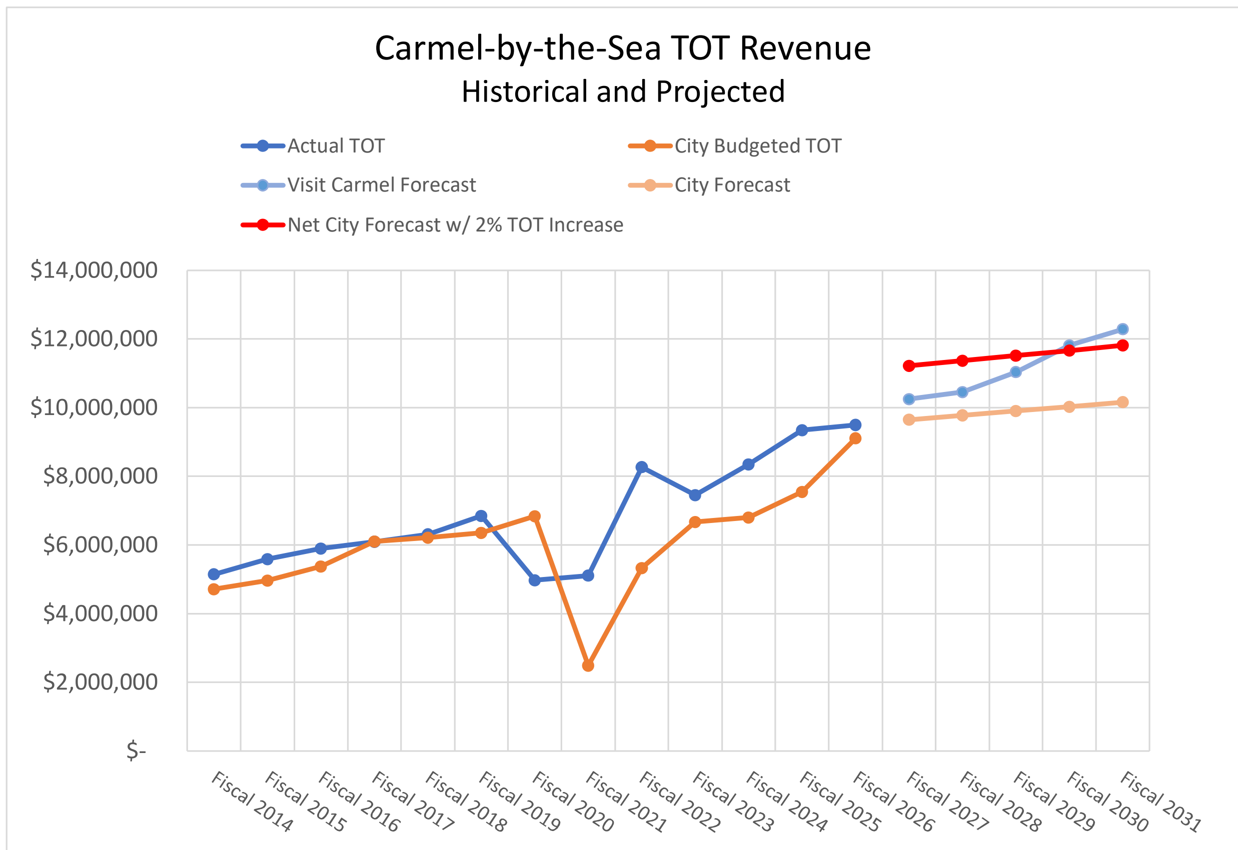
At the time of the City Council meeting in May of 2024, the prior 12 months had produced $7,741,000 in TOT. The Innkeeper Association requested an opportunity to show that TOT would grow by more than 10% over the next 12 months due to reinvestment. It exceeded this goal, and grew to $9,048,000, or 17%. Through the end of 2025 it has grown to $9,520,000, a 23 % increase in less than two years. Currently, more than 150 hotel rooms are currently under renovation or scheduled for renovation in the coming year, which is expected to produce the same ADR, RevPAR and TOT growth.

Exhibit F

Projected TOT Revenue Compared to Historical Growth Performance

Five Year Forecast

	FY 25-26 Estimated Actual	FY 26-27 Projection	FY 27-28 Projection	FY 28-29 Projection	FY 29-30 Projection	FY 30-31 Projection
Revenues						
Property	9,445,000	9,680,988	9,923,013	10,171,088	10,425,366	10,686,000
Sales tax - Bradley Burns	4,092,183	4,166,843	4,279,348	4,394,890	4,513,552	4,635,418
Sales tax - Local Meas. C	6,900,734	7,023,597	7,220,258	7,422,425	7,630,253	7,843,900
Transient Occupancy Tax (TOT)	9,526,737	9,650,584	9,776,042	9,903,130	10,031,871	10,162,286
Charges for Services	2,725,019	3,436,094	3,532,305	3,631,209	3,732,883	3,837,404
Other Revenues *	4,600,827	4,662,030	4,792,567	4,926,759	5,064,708	5,206,520
Revenue Total	**37,290,499**	**38,620,137**	**39,523,532**	**40,449,502**	**41,398,633**	**42,371,527**



Using the City's own budget framework, the Visit Carmel and Innkeepers Association analysis suggests that projected TOT revenues can meet or exceed current expectations without a 2% increase in the tax rate.

In recent years, the City's budgeting approach has not consistently incorporated Visit Carmel's forward-looking forecasts. As a result, the current 5-year projection assumes approximately 1.3% annual growth in TOT before any rate change. By comparison, actual TOT growth since the formation of the HID in 2013 has averaged approximately 5.7% annually.

This difference in assumptions appears to be a key driver of the perceived need for a tax increase. Incorporating a broader range of forecast inputs may provide a more complete picture of expected revenue performance.

Importantly, our analysis also accounts for potential demand impacts, including an estimated 14% erosion of the incremental revenue from a higher TOT rate, as outlined in Exhibit E.