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SHOULD PUBLIC BUDGETS FINANCE CONVENTION CENTERS?

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EXECUTIVE SUMMARY

The Bank is receiving an increasing number of requests from state and municipal governments to finance publicly owned convention centers. This paper suggests that few of these projects will bring the benefits expected and may impose fiscal burdens on states and municipalities that will make it more difficult to undertake other priority projects.

The financial results of publicly owned convention centers are alarming. In North America and Europe, where public ownership is the dominant model, more than 51% do more than 67% make no contribution to debt service and not cover direct operating costs.[1] This is significant in a business in which annualized capital cost accounts for about 75% of annualized cost. Operating losses and debt service can put significant pressure on state and municipal budgets and can force reductions in other municipal programs that have higher social priority.

The evidence suggests that public ownership often leads to "fiscal war" among governments. To attract business from other cities, governments charge low rates or provide space for free. This leads to retaliation. The competition has no limits since governments do not need to shut down the centers when operating revenues do not cover operating costs. States and municipalities finance the competition by levying taxes or cutting expenditure for other programs.

Government ownership is not the only alternative. The private sector can and does successfully own and operate freestanding convention centers. In Asia, private ownership is the dominant model, and more than 60% of convention centers there cover all capital and operating costs.[2] Private ownership of freestanding convention centers exists in both North America and Europe, although the percentage of private ownership is lower because of subsidized public sector competition.

I. The Economics of Convention Centers

Convention centers generally host trade shows, consumer shows, conventions, religious or political conferences, receptions, dances, banquets and other large assemblies. These services were originally, and still are, provided by large hotels that use meeting and exhibition space to generate sales of hotel room-nights and food and beverage services. The calculation of the financial benefit of hotel convention centers is straightforward. It is total revenue less total cost. The pricing of the individual services (exhibit and meeting space, hotel rooms, and food and beverage services) is not important as owners compare total revenue to total costs. Owners of hotel convention centers do not consider the

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[1] . These figures come from North America and Europe and include both public and private free-standing convention centers

[2] . These figures include the results from the three Asian countries that have public ownership: Japan, China and Thailand. The other Asian countries do not own or subsidize convention centers.

profits to other parties (such as tour operators, outside restaurants, local transportation companies) that the hotel convention center may generate.

In the 1950s, state and municipal governments became interested in the construction of convention centers of a scale larger than that offered by hotels. The purpose of these freestanding convention centers was to generate business tourism, stimulate urban activity and to replace deteriorated urban residential neighborhoods with commercial projects. The separation of the business of providing exhibition and meeting space from the business of providing lodging and food and beverage services made the pricing of meeting and exhibition space relevant. With the separation of the services, the convention center must finance its operations with the revenue it receives from the sales of meeting and display space, while others take the profits from the sale of lodging, food and beverages and other complementary goods and services. The total financial and economic benefits, however, are the same.

State and municipal governments believed that large public convention centers would bring additional profits to hotels and other businesses in the local area: restaurants, bars, tours, shows, and local transportation. In addition, state and municipal governments believed they would generate additional employment.

The Political Economy of Convention Centers

The entry of the public sector opened the possibility for various constituents to seek a subsidy from the private sector. A limited number of specific interests profit significantly from government investment in convention centers and lobby hard for the government to get involved. The principal beneficiaries are easy to identify: construction companies, large good quality hotels in the area, landowners in the area who may enjoy increases in property values and suppliers. While these groups might well invest in a convention center on their own, they are much better off if the government does it because they commit no capital, take no risk, and get most of the reward. If a convention center loses money, the government has no means to know whether the profits and employment benefits that the center generates cover the losses on operating and capital costs. The private beneficiaries have no incentive to recommend closing the center even if they would do so if they operated it themselves.

The political possibilities of convention centers are attractive. Convention centers lend themselves to the "rhetoric of new jobs, new spending, and economic multipliers [which] … for communities enduring job loss and downtown decay is politically hard to resist …." ([8] p. 58) Incumbents consider convention centers an indicator of local prestige. They accept designs far more elaborate than necessary for adequate functioning, and these designs cost more to build, operate and maintain. Incumbents inaugurate works.

Subsequent administrations foot the bill. In contrast, the citizens (who forego other public services to pay the capital costs and cover the operating losses or who pay increased taxes) are poorly informed, unorganized and little able to question "the bulky and seemingly substantial 'feasibility stud[ies] .. [p]roduced by a major national accounting firm … [and that] provide the rationale for more local convention-center space and images of community benefit." ([8], p.60) There is little organized political resistance.

Good intentions and political opportunity lead to excess capacity: too many, too large, sumptuary convention centers, many of which continue to operate at public expense when they should be shut down. States and municipalities enter fiscal wars providing ever-greater subsidies to gain market share at the expense of their neighbors.

Flawed Economic Justifications of Convention Centers

The method used in feasibility studies for convention centers is different from the method used in all other feasibility studies: there is no comparison of benefits to costs and no calculation of a rate of return. Virtually all feasibility studies justify the convention center on the basis of the impact on income and employment generated by tourism expenditure. This impact is calculated by the use of analytic expressions or locally adapted input-output matrices to calculate a multiplier effect. The multiplier impact comprises the gross spending of the visitors, the re-spending of the suppliers and workers who receive that income, and subsequent rounds of re-spending. These expenditures are substantially greater than the benefits that would be estimated by private investors since (1) they are gross expenditures and do not subtract the cost of resources used to supply the purchases and (2) they include the re-spending that a private investor would ignore since the share of this re-spending that he would receive would be negligible.

Economic feasibility studies for other kinds of projects ignore these re-spending effects. They assume that capital is scarce, and the decision to invest in one project precludes undertaking another project that would also generate expenditures and re-spending. Economic feasibility studies (cost-benefit analysis) compare only the direct results of projects without trying to compare the difference in re-spending effects.

To get an idea of the magnitude of the overestimate of financial benefits presented to government officials, we take an example from a recent study by one of the better consulting firms in the field. This study estimated that a convention center would generate an economic impact of US$ 38.5 million per year (US$ 22 million direct and US$ 16.5 million indirect) when it was operating at capacity. Omitting the indirect effect (the re-spending) and assuming that 25% of the direct expenditure results in profit (probably a generous estimate), the financial benefits perceived by private investors would be US$ 5.5 million, about 15% of the consultant's estimate of the impact (implicitly the benefit).

Multiplier analysis is based on the assumption that that the expenditure that causes the multiplier effect (in this case convention visitor expenditure) is not offset by a decrease in expenditure elsewhere (i.e. it is an "autonomous increase"). While the expenditure may be autonomous from the local point of view, it is usually not autonomous from the national point of view.[3] Attendees at most convention centers are national residents. Many are diverted from other freestanding convention centers or convention hotels where

[3] It would be autonomous for the country only if the conventioneers came from other countries.

they would have spent similar amounts. When demand is diverted, what one municipality gains, another municipality loses. The benefit for the national economy is much less than the benefit that the municipality receives, and there may be no net benefit at all.[4] Thus the financial and employment benefits from the national point of view are less than the benefits calculated from the point of view of a specific municipality. When economic transfers are take into account, the financial benefit to the nation of the convention center in the study cited as an example will be much than US$ 5.5 million, a significant decrease from the consultant's estimate of US$ 38.5 million.

Economic analysis takes a national point view. Economic analysis does not recommend projects that merely transfer income from one group to another. Municipal governments, encouraged by flawed analysis may think they have an economically feasible project when, in fact, most of the benefits come at the expense of some other center or sector of the economy.

The flaws in convention center studies go beyond the methodological. The local impacts themselves are systematically overestimated. Heywood Sanders of the University of Texas did an ex-post review of 30 convention center feasibility studies done by major national accounting and economic consulting firms and found that they substantially and systematically overestimated either the number, or the average stay, of attendees or both. ([7], [8] and [9]) He states that he has never seen a study that does not recommend the construction or expansion of convention center. Don Jewell, former President of the International Association of Assembly Managers, states, "An economist who has conducted feasibility studies through-out the United States once admitted that in his many years of experience he had never submitted a totally negative report. This is not intended, in any respect, to suggest dishonesty or misrepresentation…. Almost without exception, the assignment is not to determine if a facility should be built, but how large a facility should be built." ([4], p. 47)

From an economic point of view, private investors may actually tend to over-invest in convention centers. A private investor is concerned only with his own profit. If it comes at the expense of some other center, it is of no consequence to him. From the economic point of view, the competition between private investors can be healthy because it brings about qualitative improvement. There is a limit to over-investment since the private sector will consider the risks of undertaking a new investment and will shut down a convention center when operating costs exceed operating revenues including the profits in complementary businesses. The public sector will keep operating.

Public Ownership and Private Management

The critical decisions for convention centers are taken at the time of the initial investment. The investment decision implies that the location will be attractive to the

[4] Even if conventioneers would not have gone to a meeting or exhibition in another center, they would have spent the money in some other way. This alternative expenditure would have had re-spending effects. Thus, the positive impact in one region is likely to be offset by a negative impact in another region as the spending is diverted.

segment of the market sought[5], that the capacity proposed will be used frequently enough to justify its cost[6], and the architecture is appropriate for the market sought and cost-effective. It is important that people with business experience and their own money at stake take responsibility for the investment decision and the risk it implies. "Overly optimistic estimates for occupancy and revenues are two of the most common causes responsible for disappointing performances of many public assembly buildings…. Regardless of whether private or public management prevails, experience indicates that little can be done to increase the level of occupancy or revenue substantially beyond industry norms." ([4], p. 49)

While private management cannot make a success of a facility that should not have been built, it can help municipalities overcome some common problems. These problems include overstaffing with political appointees or public employees not wanted elsewhere, providing space to constituents without charge, lack of culture of providing service to lessees and attendees, inflexibility in hiring and purchasing practices, and no data to evaluate and adjust their operating and marketing efficiency to those of other properties. The current industry trend in North America is towards private management.

II. The Role of the Public Sector and the Bank

The public sector has an interest in seeing that economically viable projects are carried to fruition. It is possible that economically viable convention centers will not be undertaken because (1) it is difficult for private investors to organize the groups that would get the profits from sales generated by convention visitors, (2) private investors do not include employment benefits in their decisions to invest, and (3) capital markets may not provide loans with sufficient term so that a center's cash flow can cover amortization. If a project is economically viable, the government can provide support sufficient to make the project privately profitable.

a. Criteria for Screening Convention Center Proposals

Certain factors are essential to the viability of a convention center. Analysts can quickly see if a proposed convention center has any prospect of economic feasibilility by confirming that it meets all the following criteria.

i. The municipality proposed is reasonably close to an airport that receives a large number of direct flights from a number of different cities.

[5] In the case of most public centers, this segment is the segment of large regional, national and international meetings and shows. This segment generates the hotel stays and other expenditure that generates the impact. There are other segments that are more profitable for the convention center itself. These include the consumer show market and local niche markets.

[6] "Almost without exception meeting planners find it advantageous to keep their conventions in hotels as long as possible. Only when the demand for meeting rooms, plenary sessions, and exhibition space exceed those found in hotels do most planners begin to seriously consider public venues." (Jewell, p. 62)

ii. The proposed location for the convention center is within a few blocks of a sufficient number of good quality hotel rooms that can be years in advance for use by a single group at a discounted rate.

iii. There is a demonstrated private interest in investing a convention center (either on its own or as part of as a public/private partnership).

iv. The municipality has a significant amenities and attractions whose desirability is not affected by climate. (If the convention center is primarily targets trade shows, location in major population or industrial centers, is more relevant).

If the proposed location does not have these characteristics, the proposal has little prospect for success. If the location does have potential, the following principles should guide public action.

i. The private sector should own and operate the convention center.

ii. If private investors will not undertake an economically viable convention center without government support, the government can provide an incentive which should be, at most, the value of benefits that are not captured by private investors.

iii. All government support should be up-front in the form of a capital subsidy, which might take the form of providing land or providing infrastructure. It is undesirable for the public sector to provide direct or indirect operating subsidies.

b. <u>Government Actions</u>

With these principles in mind, governments and the Bank could support

1. Studies:

   a. to analyze alternatives that include pooling arrangements for large convention hotels that would take advantage of video transmission for very large meetings and transportation between hotels for the many sub-meetings characteristic of large conferences;

   b. to estimate the economic benefits of the convention center;

   c. to identify the groups who receives them, and

   d. to determine the amount of benefits that are not likely to captured or recognized by the private sector. This last amount is the basis to calculate the maximum amount of public subsidy that is economically justifiable.

2. Institutional support to put together consortia of investors who capture the benefits not included in profits on the rental of exhibition and

meeting space, food service and equipment rentals. A consortium of the principal beneficiaries would be likely to include: a construction company, a company that specializes in event production, nearby hotels and restaurants, members of the Chamber of Commerce who have an interest in access to space for display, local land interest that may have an interest in the appreciation of property value in the area. There may be other minor investors such as travel agencies and operators or operators of attractions who may obtain profits from the operation of convention centers.

3. Studies to establish a regulatory framework or security package for prospective owners. The principal feature of the framework or security package would be a guarantee on the part of the public sector not to build competing facilities in the market area for a specified number of years.

4. Contracting of an investment bank to organize a Build-Own-Operate Concession in which bidders propose the capital subsidy that they require to build and operate a convention center. It is logical to consider only proposals that request less than the maximum justifiable subsidy. The successful bidder would provide a performance bond for the amount of the capital subsidy for five years of operation.

III. In Summary

State and municipal governments will be pressured by specific local interests to invest in convention centers. The investments will look politically attractive and will be supported by feasibility studies that present economic impacts based on multipliers rather than economic benefits based on sound economic analysis. Bank staff should be aware of the flaws in this analysis and insist on private ownership and management. The number of cases where public participation is justified is probably very small, and the Bank can quickly screen for projects that have at least some prospect of viability. Once these opportunities have been detected, a sound analysis of economic benefits and beneficiaries can help delimit the nature and amount of public support.

The maximum amount of subsidy is determined by the profits earned by groups that do not invest in the convention center and by the amount of employment benefits. Employment benefits are defined as the wages received by groups working in enterprises that directly receive expenditures of the convention visitors less the wage they would have received if no convention center had been build. If the workers were previously informally employed or unemployed, the opportunity cost (shadow price) is assumed to be earnings in the informal sector. The benefits and employment effects must be adjusted for economic transfers.

I. CHARACTERISTICS OF CONVENTION CENTERS

A. Sizes, Services and Facilities

Convention centers are freestanding, flat-floor facilities suitable for meetings or exhibits. The meeting rooms they provide are typically larger than those that could be found in the largest hotel in the area where they are located. Convention centers generally host trade shows, consumer shows, conventions, religious or political conferences, receptions, dances, banquets and other large assemblies. In Europe, convention centers are called "congress centers".

An exhibition hall (often called a "trade fair" in Europe) contains 25,000 to over 1,000,000 square feet of contiguous flat-floor space with a 25-to-35 foot-high ceiling. In Canada and Europe, exhibition halls are often freestanding[7], but in the United States, they almost always form part of convention centers.[8]

A convention center contains one or more exhibition halls and a large number of meeting or "breakout rooms". The current industry standard for meeting/ballroom to exhibit space is 20 percent. Space is usually provided for a kitchen, a separate ballroom or banquet hall and occasionally a theater-style assembly center. Entry lobbies are usually sized to accommodate attendee registration. Interior lobbies, for entry to ballrooms or banquet halls, often serve as pre-function areas and are sized to host receptions or cocktail parties for guests before a banquet, ball or assembly event.

Although the convention centers vary in size from 1,000m² to more than 100,000m², average sizes in Asia, Europe and North America are quite similar. The average exhibition space per venue in 2000 in Asian was 20,631m² [9], 20,388m² in Europe, and 19,000 m² in the USA.

B. Ownership of Convention Centers

The ownership of freestanding convention centers is quite different in North America, Europe and Asia. While public ownership accounts for the majority in North America and Europe, more than 60 % of convention centers in Asia are privately owned (See Table 1).

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[7] In Europe, most congress centers do not have dedicated exhibition space.

[8] A merchandise mart is a particular kind of exhibition hall that is not considered in this study. A merchandise mart is typically a mid- or high-rise building with offices and permanent showrooms for consumer product displays and a modest amount of permanent exhibit space (30,000 to 50,000 square feet) on the ground floor. Cities that do not have a merchandise mart often host a large number of merchandise mart-type events in their convention centers and exhibition halls.

[9] According to Cat Publications and *Tradeshow Week*.

Table 1
Freestanding Convention Centers & Exhibition Hall
Ownership Structure (2000)

ENTITY	NORTH. AMERICA	EUROPE	ASIA
Private	36%	15%	60%
Public	64%	85%	40%

Source: [1], pp. 16-17.

1. Public Ownership

Convention center services (meeting and exhibition space) were originally, and still are, provided by large, private hotels in order to generate sales of hotel room-nights and food and beverage services. In North America in the 1950s, governments became interested in the construction of convention centers of a scale larger than that offered by hotels. Governments believed that large public convention centers would generate business tourism, stimulate urban activity, replace deteriorated urban residential neighborhoods with commercial projects, and generate additional employment. These convention centers target the regional, national and international convention and trade show markets to generate overnight visitor expenditure.

In Europe, the development of freestanding meeting and exhibition space followed a different logic. The public sector in Europe invests in convention centers primarily to promote the exports of regional production by providing a venue to display goods. Some of the countries also are interested in supporting their tourist industry.

The development of freestanding convention centers in Asia is relatively recent and has taken a different path. Only in China, Japan and Thailand does the public sector invest in, or subsidize, convention centers. Government owned centers are even more focused on the promotion of foreign trade than European centers.

2. Private Ownership

Private investment in freestanding convention centers in the US has focused on niche markets. Publicly owned convention centers compete for large, regional, national or international meetings and trade shows that bring visitors who stay over night and whose expenditure generates the economic impact and employment that municipal governments seek. In most cases, private centers cannot compete in this market because the public sector is willing to provide space below cost. There are exceptions, however. One private model extends the traditional hotel model in which the hotel incorporates meeting space to leverage room and food and beverage sales.

One example of the extended hotel model is the strategy used by the owners of the Opryland hotels in Tennessee, Texas and Florida. Opryland has combined the idea of resort, golf and entertainment with significant exhibition space development to attract conventions. It provides venues at different locations, so that annual conventions may rotate among them. They help produce the events, so that organizing groups can contract much of the administrative work once and have conventions at different places in different years. Another extension of the hotel model is used by the Mandalay Bay Group, which is constructing a one million square foot convention center adjacent to its namesake property in Las Vegas primarily to fill hotel rooms mid-week and enhance gaming revenue. The Mandalay Bay Group has 11,000 hotel rooms in three properties adjacent to its new convention center.

Other niche opportunities arise because many public convention centers refuse to book space for activities that do not generate overnight stays in the hope that some large event will book the space. The most important niche of this sort (consumer shows of boats, automobiles, gardens and flowers, etc.) target the residents of the area. These shows generate few overnight stays but are generally profitable since they generate a large amount of revenue for the convention center through admission fees, food service, and parking. A second niche is the merchandise mart niche. Manufacturers that wish to display consumer products often can not get access to public convention centers because of booking policy. These manufacturers band together to jointly invest in exhibition and meeting space. Two other niches are centers that focus on conference markets outside the metropolitan area and the one-day and fly-in and fly-out meetings. Cost is key to successful private centers. One private owner of various centers retrofits bankrupt mall discount stores and associates with real estate developers who provide land at below market rates in order to have a convention center anchor other tenants.

In Asia, it is common for private developers to invest in convention centers as part of mixed-use developments typically containing hotel, office, residential and retail components. In these cases, the investor's focus is on the joint return: the bottom line of convention center operation and the operating results of the related businesses.

Private chambers of commerce and consortia of private interests invest in meeting and exhibition space to display and promote the production of their region. This form of marketing is common in both Asia and Europe. Private investors are interested in the financial results of the convention center, but they are also interested in the results of the sales they generate. Private convention centers do not have to be profitable to be viable if the owners cover their losses with profits from other sales related to the convention business.

C. Ownership, Design and Capacity

Ownership has an impact on the number and size of convention centers. Publicly owned convention centers are larger than privately owned convention centers. The average exhibition space for all U.S. and Canadian exhibit space is 175,125 sq. ft. while the average for privately owned space is 152,832 sq. ft. ([1], pp.10-11)

Public involvement leads to more convention centers being constructed. There are 243 large convention centers in the U.S. and Canada, 227 in Europe, but only 55 in Asia. The large number of public convention centers in North America and Europe has led to significant excess capacity. The occupancy rates for leading venues are low in both

European and North American, approximately 50% to 65%.([1], p. 28) The rates for venues in secondary cities are significantly lower.[10]

These low occupancy rates are reflected in price competition to attract business (low rental rates) in North America and Europe and large financial losses. Data on occupancy rates are not available for Asian markets. One reason for the smaller number of convention center in Asia is that the public sector (except in China, Japan and Thailand) does not invest in and support centers as they do in Europe and North America.

Public investment in, and ownership of, convention centers has provided more than enough capacity. Publicly owned municipal centers in North America and Europe, competing for a relatively fixed number of conventions and trade shows, aggressively discount their rental rates or make space available free. This has made it increasing difficult for private facility owners to compete. In general, the public sector's has an advantage in access to capital at a lower cost than the private sector (through tax-exempt bonds) and to public subsidies to cover operating expenses and shortfalls. This has discouraged private ownership in all but niche markets.

II. FINANCIAL ASPECTS OF CONVENTION CENTERS

A. Sources of Financing

The sources of financing the convention centers are different in Asia, Europe, and North America. There are differences due to ownership and systems of municipal finance on each continent.

As Asian venues are developed by real estate companies, sometimes in partnership with trade-related associations, international tradeshow producers or government agencies, the facilities are generally financed with private equity, bank debt and, sometimes public capital in joint ventures. The few convention centers owned by public entities in Asia are financed in part with local and federal grants and subsidies.

In Europe, most convention centers are financed through bank loans backed by government repayment promissory notes. The European Community occasionally has provided the public sector free-and-clear grants to develop or expand venues.

In the US, two-thirds of funds for financing for convention centers comes from tax-exempt publicly issued bonds. The private sector generally finances convention centers with bank debt, bonds or asset-backed securities, as well as equity contributions.

Table 2

Sources of Financing For Construction Of Convention Centers
And Exhibition Halls In the US

[10] The occupancy figures themselves can be misleading as there is no standard definition. Many multi-exhibition hall convention centers report themselves "occupied" if only one of their exhibition halls are in use.

Type	(%)
General Obligation Bonds	42.7%
Revenue Bonds	21.4%
Private Bonds	4.0%
Redevelopment Bonds	2.3%
Private Donations	2.3%
Other	27.3%

Source: [3], p. 200.

Box 1
Bonds Financing Municipal Convention Centers in USA

General Obligation Bonds. General Obligation bonds are secured by the full faith and credit of the borrowing government agency. These bonds are guaranteed by a municipality's general fund. General Obligation bonds are considered the most secure form of municipal debt.

Bonds Secured by Dedicated Taxes/Revenue Streams. This type of financing is secured by specific taxes on revenue streams. It is common for the revenue streams to be attached to commercial activities that will be driven partially by the convention facility (e.g. room tax). Supporting revenues have come from a wide range of related activities: airport departure tax, alcohol and tobacco tax, car rental tax, admissions, food & beverage and general sales tax, hotel/motel room tax, utility tax, construction industry/building trades surcharges lottery and gaming revenues parking, taxi and ticket surcharges.

Lease/Revenue Backed Bonds These bonds are secured by the pledge of a municipality to cover debt service but are not assigned a dedicated tax revenue stream. Typically part of the venue revenue will be used to pay the debt service. This approach gives municipalities flexibility to meet debt service commitments from any available revenues. These bonds are considered riskier than General Obligation securities and bonds secured by dedicated taxes/revenue streams as they are generally tied directly to facility performance. Occasionally, bonds issued under this approach are referred to as "Certificates of Participation."

B. Public-Private Partnerships

Public-private partnerships have been used for developing convention centers in urban renewal/revitalization. The relative participation of public and private sector depends on the land appreciation that may be captured by the private sector. When private developers are able to capture most of the appreciation, public sector participation is in general not required. However, when investment costs are large and the appreciation may take time to materialize, public sector involvement may be necessary. In the U.S., most public-private partnerships are designed to allow the private sector to increase its participation in the appreciation, while in Europe the partnerships are designed to reduce the costs of private investment.

Box 2
Public-Private Partnership in the US
Convention Centers Undertaken To Revitalize Run-Down Urban Areas

As financial returns of development projects in these areas are often insufficient to attract private investment, the public sector often uses the following incentives to attract private sector participation:

Tax Increment Financing. A portion of the incremental property tax revenue than comes from the appreciation of real estate in development and redevelopment projects goes to the repayment of project costs.

Real Property Tax Credit. A tax credit that investors in development projects can deduct from their corporate taxes, personal income taxes, banking corporation taxes or insurance corporation taxes. The credit is based on the numbers of jobs created and the property taxes paid.

Real Property Tax Abatement Municipalities reduce tax rates to offset increased assessments due to improvements to business and commercial property.

Infrastructure Improvements. Municipalities invest in public space, parking and streetscape quality to make private investment more attractive.

C. Sources of Revenues

The income for convention centers and exhibition halls comes principally from rental of exhibition and meeting space, and the provision of food, beverage, and event services. Convention centers also obtain revenues from parking, utilities (such as electricity, and telecommunications), catering and equipment rentals. The prices and composition of revenues at major European centers are similar to those of North American venues. Prices and revenues at major Asian centers are higher because there are not as many subsidized venues competing for conventions ([1], p.28]). Asian prices per square foot are higher, and the pricing structure differs as Asian centers charge the same rate for move-in and move-out days as for show days ([1], p.28]). In addition, Asian facilities increase revenues by providing and charging for enhanced service levels associated with large full-time staffing. Asian venues also generate important food and beverage revenues through catering large functions and having a variety of on-site restaurants.

Table 3
Revenues Structure for Major Venues in North America and Europe

ITEM	Participation In Total Revenues %	Revenues Per Sq. Ft. Of Exhibit Space (2001$)
Rentals	25% to 35%	$8 to $10

Food & Beverage	25% to 35%	$8 to $10
Event Services[11]	15% to 25%	$6.50 to $8.50
Vendor Commissions	1% to 5%	$1 to $3
Parking	5% to 15%	$2 to $4

Sources: [1], p23.

1. Rental Revenues

Rental income for convention centers and exhibition halls is of two types: (1) rentals for large conventions and trade shows that attract visitors from out of town, and (2) rentals for consumer shows and other events that attract local residents. The two types of rentals behave differently as a consequence of convention center booking policy.

Rentals rates are used as a tool to attract convention and trade shows that bring out-of-town visitors. These rates rarely cover operating costs.[12] Rental rates are determined primarily by: (1) the number of days required to move in, present the event, and move out, (2) the amount of exhibit, meeting-room and ballroom space used, (3) specific dates or season of the year and (4) the number of hotel rooms occupied and (5) how far in advance of the event date the agreement is signed or the deposit is paid.

Rental rates for consumer shows are generally higher, since most municipalities do not compete to attract these shows. Consumer shows attract local visitors who do not stay in hotels or generate additional expenditure. Consumer shows generally contribute more to the convention center's bottom line than do trade shows and association meetings. They generate admission fees from attendees and higher rental fees from exhibitors. Most publicly managed centers are reluctant to book them. Private managers of public centers, trying to increase operating revenues by booking consumer shows. They are often constrained in doing so by public policy, which restricts dates for locally oriented events in order to avoid conflicts with the marketing of dates for trade shows and association meetings. Booking policy has a strong influence on the mix of events and the financial results of centers.

Governments do not seek the consumer show niche and private investors have profitably gone in. Exhibition halls built for consumer shows are simpler and less expensive in design that the standard exhibition hall. They are often referred to as "big box" venues because they are large, unadorned contiguous exhibit halls. Unlike convention centers, they tend to be located in suburban locations.

2. Food and Beverage

Until the mid-1980's, many major centers did not have banquet halls or preparation kitchens. Today convention centers in attractive destinations and large markets may earn

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[11] Some venues combine hall rental with event services when reporting financial results

[12] It is not meaningful to compare the rate schedules of different centers because posted rates are discounted, and hotels often supplement the rent by rebating some of the hotels room charge to allow centers to reduce the posted rate.

as much as 50 percent of their net operating revenues from food and beverage sales. Products are offered from pushcarts, portable stands, sidewalk cafes, food courts, branded food outlets, cafeterias, and formal, white-tablecloth banquets offering five-course, restaurant quality meals. Food and beverage revenues are often a net amount to the center, derived as a percentage of gross revenues generated by concessions and event caterers.

3. Event Services

Revenues from event services such as electricity, plumbing, telephone, security, audiovisual equipment, set-up, medical and cleaning and rubbish, are important to convention centers and exhibition halls, and are one of the means by which centers have been able to increase operating income to offset declining rental revenues.

4. Other

Other income may be derived from parking, vendor commissions (i.e., on concierge, Internet, retail, and other vendor sales), sponsorship revenue (from beverage companies, travel agencies and television programmers, etc.) and from revenue generated by placement of advertisements in center publications and on signage throughout the facility.

D. Structure of Costs

Operating expenses for convention centers and exhibition halls include salaries and wages, utilities, selling, general and administrative expenses, and maintenance, repairs and supplies. Additionally, contractual services/non-reimbursable event costs and insurance are associated with facility operations and are primarily fixed in nature.

Table 4
Cost Structure in North America

LINE ITEM	% OF TOTAL EXPENSES	PER SQ. FT. OF EXHIBIT SPACE (2001$)
Salaries, Wages and Benefits	35% to 45%	$9.50 to $11.50
Utilities	10% to 15%	$4.50 to $6.50
Selling, General and Administrative	10% to 15%	$2 to $5
Maintenance, Repairs and Supplies	5% to 10%	$1 to $3
Contractual Services/Non-Reimbursable Event Costs	10% to 15%	$9 to $11
Insurance	5% to 10%	$1 to $3
Other Operating Costs	5% to 10%	$1 to $3

Source: [1], p. 23.

The cost structure of European centers differs from that of North American centers because a large number of the leading venues run their own events, a rare business model in North America. This tends to make the salaries, wages and benefits higher in Europe.

The structure of costs is also different in Asia. North American and European venues employ a fraction of the number of full-time staff employed by Asian facilities and rely heavily on temporary workers. In addition, in some locations in North America, labor is unionized, resulting in substantially higher wages than those paid by non-union Asian venues. Even though Asian facilities have substantially more full-time personnel per facility than North America and Europe (the Hong Kong Convention and Exhibition Center employs approximately 1,300 full-time workers, nearly half of whom work in the food and beverage department), they have lower overall operating expenses because of the relatively low cost of labor ([1], pp28-29).

Box 4
Operating Revenues and Expenses of a Typical Convention Center
(millions of US$)

Operating Revenues		
Rentals	$1.0	29%
Food and Beverage	1.0	29%
Event Services	0.6	17%
Parking	0.4	11%
Other	0.5	14%
Total Revenues	**$ 3.5**	**100%**
Operating Expenses		
Salaries, Wages and Benefits	$1.6	40%
Utilities	0.6	15%
Selling, General and Administrative	0.5	12%
Non-reimbursable Event Costs	0.5	12%
Maintenance, Repairs and Supplies	0.3	8%
Insurance	0.3	8%
Depreciation and Replacement	0.2	5%
Total Expenses	**$4.0**	**100%**
Net Operating Income	$(0.5)	(12%)

Source: [6], p. 79.

E. The Financial Results of Convention Centers

The majority of publicly owned convention centers in North America and Europe operate at a loss. Few contribute to debt service or to reserves for major repairs or replacements. Nevertheless, some centers do cover all operating costs and contribute to debt service. These centers are usually in major markets in the most attractive destinations, with the best management, citywide marketing efforts, and an unconstrained ability[13] to control food, beverage, and event service delivery. An estimated 10% to 20% of *major*[14] European venues owned by municipalities are able to cover operating expenses and debt service ([1], p. 37). The limited participation of profit-driven venue management companies in municipal facilities in Europe has contributed to this low percentage of profitable *major* facilities ([1], p. 37).

Private freestanding venues in Europe (i.e., not contained in or attached to a hotel) are generally owned by chambers of commerce and other local business associations, and are motivated primarily by enhancing trade and business activity. These organizations receive no public sector funding, and pay attention to venue profitability. These facilities generally achieve break-even or a slight profit.

An estimated 40-50% of the total major venues (public and private) in Asia are able to cover operating expenses, debt service and are profitable ([1], p. 37). Their rental rates are higher than in the United States and Europe, driving profitability. This is primarily because there is less competition with subsidized facilities and because investors are trying to earn a profit. In addition, operating expenses (labor costs) are lower.

The International Association of Assembly Managers carried out a survey of the financial results of its members. The survey defined direct operating revenue as revenue generated by facility activity such as income from rentals, food and beverage, rental services, merchandise sales and parking and does not include income received from dedicated taxes, subsidies or interest earned. The survey defined direct operating expenses as costs involved in operation and maintenance of the facility and do not include depreciation, taxes, interest paid or amortization.

Table 5 shows that only 4.4% of the respondents expected that direct operating revenue would cover operating expenses, debt service, and generate a profit. More than half indicated that direct operating revenue would not cover operating expenses.

The actual results are worse than the above table indicates because the direct operating expenses reported by convention centers do not reflect all operating costs. Unreported costs are paid by other public sector entities. Sixty-three percent of reporting convention centers indicated that other agencies/departments provided services such as heating, ventilation, and air conditioning; maintenance and repairs; grounds keeping; cleanup; utilities; salaries; insurance; accounting and other services. In about a third of these

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[13] The ability to provide these services is limited by some municipalities because they do not want to compete with local restaurants, bars and hotels.

[14] Percentages based on major centers are not comparable with the results from the IAAM, which is a survey of all centers.

cases, the other agencies provided these services without charge or at a charge less than full cost. In addition, convention and visitors bureaus may pay some or all of the marketing cost. Seventy-eight percent of reporting convention centers indicated that they did not have to pay taxes (such as property tax or tax on possessory interest).

Table 5

Expected Financial Results of Reporting Convention Centers and Exhibition Halls

Direct operating revenue will cover debt, operating expenses and make a profit	4.4%
Direct operating revenue will cover debt and operating expense, but will not make a profit	8.9%
Direct operating revenue will cover operating expenses And contribute to debt service	20.0%
Direct operating revenue will cover operating expenses	15.6%
Direct operating will not cover operating expenses	51.1%

Source: [3]. P. 205.

F. Paying for the Operating Deficit

Convention centers must obtain funds to pay the operating expenses that revenue does not cover. If the center depends on an annual budget appropriation, the facility must await the outcome of the competition for funds with other government departments providing more vital community services and will be subject to the recurrent budget cutbacks that governments experience. This can result in costly unanticipated shutdowns of operations, violations of lease agreements and other contracts, negative public relations, and erosion of market share. In the U.S., a number of convention centers are supported by a dedicated source of income (such as the hotel room tax) to give the center financial stability. A variety of taxes have been used to finance public facility operations. In North America, forty-nine percent of reporting convention center/exhibition halls in the IAAM survey responded that they received dedicated tax or other support to help cover the operating costs.

G. Repaying the Debt and Other Capital Costs

Sixty–six percent of the convention centers that responded to the IAAM's survey stated that *direct operating revenues were not sufficient to make any contribution to the repayment of the debt* that financed the capital cost of the convention center or exhibition hall. This is not a minor matter because the annualized cost of capital is about 10% of capital cost, whereas annual operating costs range from 2% to 4% of capital cost.[15] Public financial planning does not always provide adequate funding or reserves for replacement of capital equipment and for periodic capital renovations or updating required to retain a center's marketability.

The following table presents the sources that sixty-five of the reporting facilities used to repay the debt. The table shows that hotel/motel taxes, general revenues, and sales taxes were the principal sources for repayment.`

[15] Edwin S. Mills, "Should Governments Own Convention Centers?", Heartland Policy Study, No. 33. Chicago, Illinois, January 21, 1991.

Table 6
Source of Income to Retire the Debt

Hotel/Motel Tax	48.5%
General Fund Appropriations	41.5%
Income from Facility Operations	27.7%
Government Grants	17.5%
Sales tax	6.3%
Private Contributions	4.8%

Source: IAAM

H. Factors Critical to the Financial Success of Convention Centers

Most specialists agree that there are four key factors that are necessary, but not sufficient, for financially sound convention centers. First is location with frequent service by air from a large variety of origins. Successful convention centers are generally within twenty miles of international airports, close to railway stations and major highways. In Europe and Asia the successful venues are typically developed in gateway cities, national capitals and manufacturing centers. In Europe, because of its size and population density, frequent train service is also important.

The second element is proximity (walking distance) to large blocks of high quality hotel space that can be blocked years in advance for use by a single group at a discounted rate. In North America, convention centers focused on tradeshows and association meetings favor downtown areas near blocks of hotel rooms.[16] They are generally in established commercial districts or, particularly in Asia, part of a large, mixed-use project to develop trade or create critical mass. In Asia they are within walking distance of large blocks of Western chain-associated hotels. It is important that the hotel space already exist or built in parallel with the convention center as part of a contractually based public-private partnership agreement. It should not be assumed that the private sector will be induced to build hotels. There are numerous examples of cities having to invest in hotels when the private sector did not invest as assumed, Boston, Chicago and Philadelphia being recent examples.

Third is location in a tourist destination with significant support amenities (i.e., restaurants, retail, entertainment, etc.), where seasonality is not determined by climatic conditions. Location in areas that have cultural and tourist attractions makes convention centers more marketable for conventions and association meetings. This is somewhat less true for trade shows in which the cost of moving the items to be displayed may offset the enticement of a distant but attractive area. It should be noted, however, if the

[16] In North America, centers focusing on consumer shows favor suburban locations because their market is local and does not need overnight lodging.

attraction is seasonal, the demand for the venue is likely to coincide with the high season for tourism. If this is the case, tourists and conventioneers will compete for the same accommodations and there will be little incremental impact generated by the convention center. If the area is not attractive to tourists off-season (usually because of climatic conditions) it is unlikely to be attractive to conventioneers either.

The fourth element is proximity to large manufacturing centers, population centers with large concentrations of professionals or large consumer markets. Proximity to these centers affects the cost to exhibitors of putting on shows and the cost to attend them. The cost of events is the sum of convention center charges, transportation costs for exhibitors and attendees, lodging, restaurant, and other costs. Proximity to regional industrial concentrations is important for trade shows. Proximity to concentrations of professionals is important for association meetings, and proximity to areas with large populations with high household income is important for consumer shows. There are niche operations that are exceptions to this general principle. The Sands/Venetian and the Mandalay Bay Group have developed centers in Las Vegas in combination with casinos and the Gaylord Entertainment has developed centers in conjunction with Opryland hotels in Tennessee, Texas and Florida based on access to the company's own golf courses and resort facilities.

III. THE RATIONALE FOR PUBLIC SECTOR INVOLVEMENT

The provision of space for meetings, trade exhibits and other assemblies is an economic service for which people are willing to pay. These services were originally, and still are, provided by large hotels that use meeting and exhibition space to generate sales of hotel room-nights and food and beverage services. The calculation of the benefit of hotel convention centers is straightforward. It is total revenue less total cost. The pricing of the individual services (exhibit and meeting space, hotel rooms, and food and beverage services) is not important as owners compare total revenue to total costs. The owner of a hotel convention center does not consider the profits to other parties (such as tour operators, outside restaurants, local transportation companies) that the hotel convention center may generate.`

In the 1950s, the public sector (state and municipal governments) became interested in the construction of convention centers of a scale larger than that offered by hotels. The purpose of these freestanding convention centers was to generate business tourism, and stimulate urban activity. In some cases, the public sector believed it could stimulate economic activity in decaying urban areas where the privates sector would not invest.

The separation of the business of providing exhibition and meeting space from the business of providing lodging and food and beverage services made the pricing of meeting and exhibition space relevant. With the separation of the services, a convention center must finance its operations with the revenue it receives from the sales of meeting and display space, while others take the profits from the sale of lodging, food and beverages and other complementary goods and services. The total financial and economic benefits, however, are the same.

Economic theory suggests that these space and meeting services should be supplied to the point at which the incremental willingness to pay for additional capacity is equal to the incremental cost. As long as there is not some market failure, private markets should be able to provide sufficient capacity providing services up to the point that incremental willingness to pay (as approximated by revenues) covers incremental costs (as approximated by operating costs and required return on investment).

It is clear from the financial results presented, that investment in convention centers in both North America and Europe has gone well beyond the point where incremental revenue equals incremental cost and that most convention centers suffer significant financial losses. The countries where this has occurred are ones in which public ownership is the dominant form of ownership. Since the private sector has proved willing to invest and operate both hotel and freestanding convention centers without public subsidy, it is worthwhile examining the reasons for public investment, ownership, and operation.

The accepted rationales for public intervention (although not necessarily ownership) are natural monopoly, market failure, or merit want. Convention centers do not have declining average costs, so they are not natural monopolies. They do not provide services that satisfy “merit wants”. Therefore the rational for public intervention should be based on market failure. There are three possible market failures that might cause the private sector to provide too little space: the first is positive externalities generated by convention centers. The second is failure of the financial markets to provide financing with a term long enough to permit the private center to invest, and the third is the transaction costs associated with getting information, organizing investors, and controlling risk.

A. Externalities

The principle externality that convention centers are the profits in hotels, restaurants, bars, stores, places of entertainment etc. generated outside the convention center that would not have otherwise occurred. These are externalities because they increase the income (one of the variables in the utility function) of economic agents who do not use or supply the convention center. Private investors have recognized that these opportunities exist and, in many cases, have moved to internalize them. The original model for the convention center, the convention hotel was designed to internalize most of the benefits from visitor spending. Casino hotels have built freestanding convention centers to capture mid-week hotel and gaming business. Private consortia include convention centers in mixed-use developments to drive the associated businesses. It is possible that the private sector cannot internalize all the benefits and this may justify public support or subsidy. It does not necessarily justify public ownership.

B. Failure in the Financial Markets

There is a second form of market failure that may be relevant. The financial markets may not have developed sufficiently to permit borrowers to obtain the credit for the ten or twenty year period necessary to allow cash flow to cover debt service. This may prevent the private sector from supplying the socially desirable amount of meeting and exhibition space. Insufficient term for credit is undoubtedly a problem in most of the Bank's member countries and may justify some sort of government intervention to extend the term of credit. It does not, however, imply that the public sector should own convention centers.

C. Transactions Costs Associated with Getting Information, Organizing Investors, and Controlling Risk

One final problem is that private interests who could benefit may not have the information or organization to properly evaluate opportunities for investment in convention centers and organize themselves into a consortium to capture the benefits. In addition, certain investments such as the development of convention centers to recover deteriorated urban areas imply substantial risk and require measures to mitigate risk such as the inability to obtain the assemble the property necessary or ensure the compatibility of land use (zoning) that are not easy for the private sector. Developing information necessary to identify the benefits for various possible partners in consortium has a cost and there are significant transaction costs in organizing. Solution of these problems requires public involvement, but it does not imply that the best solution is for the public sector to own the convention center.

D. Multiplier Impact and Employment Generation

Virtually all studies of convention centers done for the public do not focus on externalities, transaction costs and financial terms. They justify the convention center on the basis of their impact on income and employment. The method used to justify the centers differs from the method used in other feasibility studies: there is no comparison of benefits to costs and no calculation of a rate of return.

Convention center focus on impact, which is estimated by the use of analytic expressions or locally adapted input-output matrices to calculate a multiplier effect. They generally calculate two multiplier effects: one caused by the construction and operation of the convention center and a second caused by the spending of the convention visitors and exhibitors. The studies argue that the visitors to convention centers spend hundreds of dollars per day in the local economy. They calculate the total multiplier of these visitors to show the large impact of the convention center.

Feasibility studies for other projects do not calculate the multiplier effect of a capital investment or interpret this effect as a benefit. Feasibility (benefit-cost) analysis assumes that investment capital is scarce and that the decision to make an investment in a convention center will displace another investment, perhaps a hospital or a school, that would also have had a multiplier effect. By deciding to invest in a convention center, the municipality gets one investment multiplier effect, but loses the investment multiplier effect of the alternative investment.

Feasibility studies should not take the multiplier impact of the spending of convention visitors and exhibitors as a benefit either. The multiplier impact comprises the gross spending of the visitors, the gross re-spending of the suppliers and workers who receive that income, and subsequent rounds of re-spending. These expenditures are substantially greater than the benefits that would be estimated by private investors since (1) they are gross expenditures and do not subtract the cost of resources used to supply the purchases and (2) they include the gross re-spending again without subtracting the cost of supplying that respending.

A private consortium that was able to capture all visitor expenditure would not take gross revenue as a measure of its profit (benefit); nor would it take the re-spending of its suppliers an employees a measure of its benefit since its share of this re-spending would be negligible. Economic analysis does not take the multiplier as a benefit either. The multiplier concept implicitly assumes that the resources used to attend visitors are idle and are not bid away from others uses. This usually is not true. Use of these resources has an opportunity cost.

To get an idea of the magnitude of the overestimate of financial benefits presented to government officials, we take an example from a recent study by one of the better consulting firms in the field. This study estimated that a convention center would generate an economic impact of US$ 38.5 million per year (US$ 22 million direct and US$ 16.5 million indirect) when it was operating at capacity. Omitting the indirect effect (the re-spending) and assuming that 25% of the direct expenditure results in profit (probably a generous estimate), the financial benefits perceived by private investors would be US$ 5.5 million, about 15% of the consultant's estimate of the impact (implicitly the benefit).

Multiplier analysis is based on the assumption that that the expenditure that causes the multiplier effect (in this case convention visitor expenditure) is not offset by a decrease in expenditure elsewhere (i.e. it is an "autonomous increase"). While the expenditure may be autonomous from the local point of view, it is usually not autonomous from the national point of view.[17] Attendees at most convention centers are national residents. Many are diverted from other freestanding convention centers or convention hotels where they would have spent similar amounts. When demand is diverted, what one municipality gains, another municipality loses. The benefit for the national economy is much less than the benefit that the municipality receives and there may be no net benefit at all.[18] Thus the financial and employment benefits from the national point of view are less than the benefits calculated from the point of view of a specific municipality. When economic transfers are take into account, the financial benefit to the nation of the

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[17] It would be autonomous for the country only if the conventioneers came from other countries.

[18] Even if conventioneers would not have gone to a meeting or exhibition in another center, they would have spent the money in some other way. This alternative expenditure would have had re-spending effects. Thus, the positive impact in one region is likely to be offset by a negative impact in another region as the spending is diverted.

convention center in the study cited as an example will be much than US$ 5.5 million, a significant decrease from the consultant's estimate of US$ 38.5 million.

Economic analysis takes a national point view. Economic analysis does not recommend projects that merely transfer income from one group to another. Municipal governments, encouraged by flawed analysis may think they have an economically feasible project when, in fact, most of the benefits come at the expense of some other center or sector of the economy.

The use of multipliers and input-output analysis reflects the public sector's desire to generate employment. Public authorities often look to convention centers to absorb unemployed labor. A proper benefit-cost analysis would reflect the employment benefit by valuing labor input at its true economic cost, rather than the nominal wage (shadow price the inputs). This would reveal that the social profitability of a convention center is higher than the private profitability. This analysis, however, also has to take a national point of view. Since the spending of national visitors for the convention center will come at the cost of other spending in the economy, it will have a negative employment effect in some other part of the economy. This effect must be considered.

E. Biases in Benefit Estimation

The flaws in convention center studies go beyond the methodological. The local impacts themselves are systematically overestimated. Heywood Sanders of the University of Texas did an ex-post review of 30 convention center feasibility studies done by major national accounting and economic consulting firms and found that they substantially and systematically overestimated either the number, or the average stay, of attendees or both. ([7], [8] and [9]) The two most common methods used are (1) surveys of convention and meeting planners about there interest in meeting in a particular city and (2) the quantification of a set of factors the consultant believes central to a convention centers success. The consultant applies many assumptions with these methods, He states that he has never seen a study that does not recommend the construction or expansion of convention center.

Don Jewell, former President of the International Association of Assembly Managers, states, "An economist who has conducted feasibility studies through-out the United States once admitted that in his many years of experience he had never submitted a totally negative report. This is not intended, in any respect, to suggest dishonesty or misrepresentation…. Almost without exception, the assignment is not to determine if a facility should be built, but how large a facility should be built." ([4], p. 47)

From an economic point of view, private investors may actually tend to over-invest in convention centers. A private investor is concerned only with his own profit. If it comes at the expense of some other center, it is of no consequence to him. From the economic point of view, the competition between private investors can be healthy because it brings about qualitative improvement. There is a limit to over-investment since the private sector will consider the risks of undertaking a new investment and will shut down a convention center when operating costs exceed operating revenues including the profits in complementary businesses. The public sector will keep operating.

F. Convention Centers Generate Tax Revenues that Cover Financial Losses

Public authorities often argue that convention centers do not cost the municipality as much as they appear to because part of the money is recaptured in sales taxes, income taxes, property taxes and special taxes such as hotel-room taxes. These arguments need to be carefully evaluated.

The expenditures of visitors out of the area will increase revenue from sales and local income taxes, but as long as the visitors are from within the country, the increase will be offset by a decline in sales and income tax revenues on the expenditure that the visitor would have made in some other jurisdiction. Many studies include the taxes on the expenditures of "day-trippers" from the same region, the taxes on their purchases will not cause a net increase locally.

Special taxes, such as hotel, restaurant, and car rental taxes affect more than just convention visitors. These taxes do no necessarily represent the contribution of convention visitors to the cost of the convention center and may have perverse effects. If they are new levies, they raise the price of lodging near the convention center, which makes the convention center less marketable. The only tax system that would provide market discipline is to finance the operating deficit and debt service with a tax on the rooms of only convention attendees. This is a real market test of the financial viability of the convention center and avoids spurious claims that tax revenues are a boon while tapping tax revenues that are unrelated to the convention centers performance.

The appreciation of property values near the convention center reflects the increase in profitability of adjacent businesses. This increase in profitability is usually at the cost of some other area (perhaps outside the region) making it a transfer from a national point of view. As a practical matter, many municipalities exempt or reduce property tax rates in the area of the convention center in order to induce complementary investment, so there is little, if any, incremental revenue from the property tax.

Any potential tax benefit in Bank member countries should be evaluated in light of the efficiency of tax system (assessment, billing, and compliance). It should be noted an increase in tax revenue (even one only on hotel rooms used by convention attendees) does not justify government investment and ownership. A private convention center would generate at least as much tax revenue.

G. The Political Economy of Convention Centers

Publicly owned convention centers provide significant financial gains to a limited number of specific interests that lobby hard for the government to get involved. The principal beneficiaries are easy to identify: construction companies, large good quality hotels in the area, landowners in the area who may enjoy increases in property values and suppliers. While these groups might well invest in a convention center on their own, they are much better off if the government does it because they commit no capital, take no risk, and get all the reward but the convention center profits (if any).

The political possibilities of convention centers are attractive. Convention centers lend themselves to the "rhetoric of new jobs, new spending, and economic multipliers [which] … for communities enduring job loss and downtown decay is politically hard to resist …." ([8] p. 58) Politicians consider convention centers an indicator of local prestige. They accept designs far more elaborate than necessary for adequate functioning These designs cost more to build, operate and maintain. Incumbents inaugurate works; subsequent administrations foot the bill. In contrast, the citizens (who forego other public services to pay the capital costs and cover the operating losses or who pay increased taxes) are poorly informed, unorganized and little able to question "the bulky and seemingly substantial 'feasibility stud[ies] .. [p]roduced by major national accounting firms … [that] provide the rationale for more local convention-center space and images of community benefit." ([8], p.60) There is little organized political resistance.

If the convention center loses money, the government has no means to know whether the profits and employment benefits that the center generates cover the losses on operating and capital costs. It is likely to overestimate the value of these benefits if it takes multiplier estimates as their measure. The private beneficiaries have no incentive to recommend closing the center even if they would do so if they operated it themselves.

There is a remarkable divorce between the results forecast by studies and the reality. "Just as there is no mechanism for evaluating, critiquing, or independently assessing the feasibility studies, there is rarely a local institution or process for evaluating the performance or impact of convention centers. When centers fail to produce the attendance, hotel use, and visitor spending predicted, there is little political accountability and no real performance review. Convention center failure or underperformance … is followed by more consultant studies, which in turn call for even more: more exhibit space; more hotel rooms (increasingly with public subsidy); more amenities, and more public investment … to support the competitive position of the convention center." ([9], p. 209)

Good intentions and political opportunity lead to excess capacity: too many, too large, sumptuary convention centers, many of which continue to operate at public expense when they should be shut down. States and municipalities provide ever-greater subsidies to simply reassign convention and trade shows among competing centers. These are essentially engaged in a fiscal war to gain market share at the expense of their neighbors.

H. The Economic Consequences of Public Intervention

There is no shortage of convention centers. There are too many. The problem is clearly over-investment by the public sector. Most public convention centers do not cover costs and do not expect to cover them. There is no clear financial limit to restrain public supply. The public sector is not forced to close when revenues do not cover cost, because it can cover losses with tax revenues. Shutting down a center will be opposed by all those who benefit and could be politically embarrassing. The only groups likely to object to running large deficits are defuse interests that cannot get funds for other public objectives. These groups may have a difficult time getting information on the true extent of losses because many of the costs of operation are not on the convention centers books.

The consequences of public involvement in terms of income distribution are likely to be unfavorable. The principle beneficiaries construction companies, large hotels, land interests and suppliers who are not poor. The generated jobs for the unemployed and unskilled are likely to be small and are generated at the cost of jobs in other sectors or other regions. The cost in terms of other government investments and programs for social purposes may be significant.

I. Public Ownership and Private Management

The current industry trend in North America is towards private management of publicly owned facilities. While private management cannot make a success of a facility that should not have been built, it can help municipalities overcome some common problems. These problems include overstaffing with political appointees or public employees not wanted elsewhere, providing space to constituents without charge, lack of culture of providing service to lessees and attendees, inflexibility in hiring and purchasing practices, and no data to evaluate and adjust their operating and marketing efficiency to those of other properties.

The critical decisions for convention centers are taken at the time of the initial investment. The investment decision implies that the location will be attractive to the segment of the market sought[19], that the capacity proposed will be used frequently enough to justify its cost[20], and the architecture is appropriate for the market sought and cost-effective. It is important that people with business experience and their own money at stake take responsibility for the investment decision and the risk it implies. "Overly optimistic estimates for occupancy and revenues are two of the most common causes responsible for disappointing performances of many public assembly buildings…. Regardless of whether private or public management prevails, experience indicates that little can be done to increase the level of occupancy or revenue substantially beyond industry norms." ([4], p. 49) The current industry trend in North America is towards private management.

Box 3
Private convention center management companies

Private management companies are a common arrangement for managing convention centers in the U.S.

[19] In the case of most public centers, this segment is the segment of large regional, national and international meetings and shows. This segment generates the hotel stays and other expenditure that generates the impact. There are other segments that are more profitable for the convention center itself. These include the consumer show market and local niche markets.

[20] "Almost without exception meeting planners find it advantageous to keep their conventions in hotels as long as possible. Only when the demand for meeting rooms, plenary sessions, and exhibition space exceed those found in hotels do most planners begin to seriously consider public venues." (Jewell, p. 62)

They are less common in Europe and Asia. Private management companies typically charge a base fee with a variable incentive fee tied to benchmarks, such as gross revenues, attendance levels and number of events. The tax bill of 1986 places restrictions on fees to management companies that run publicly owned facilities financed by tax-exempt bonds. The majority of US management contracts fall under these guidelines. These include variable fees cannot be greater than base fees, contracts with term lengths over five years must include an "out clause" after the third year, incentive fees and bonuses can only be tied to revenue and event metrics. Neither profits nor cost savings from the facility operation can be distributed to the management company or its personnel.

J. The Role of the Public Sector and the Bank

The public sector has an interest in seeing that projects that are economically viable from a national point of view are carried to fruition. It is possible that economically viable convention centers will not be undertaken because (1) it is difficult for private investors to organize the groups that would get the profits from sales generated by convention visitors (to internalize the externalities), (2) private investors do not include employment benefits in their decisions to invest, and (3) capital markets may not provide loans with sufficient term so that a center's cash flow can cover amortization. If a project is economically viable, the government can provide support sufficient to make the project privately profitable.

1. Criteria for Screening Convention Center Proposals

Certain factors are essential to the viability of a convention center. Analysts can quickly see if a proposed convention center has any prospect of economic feasibilility by confirming that it meets all the following criteria:

i. The municipality proposed is reasonably close to an airport that receives a large number of direct flights from a number of different cities.

ii. The proposed location for the convention center is within a few blocks of a sufficient number of good quality hotel rooms that can be blocked years in advance for use by a single group at a discounted rate.

iii. There is a demonstrated private interest in investing a convention center (either on its own or as part of as a public/private partnership).

iv. The municipality has a significant amenities and attractions whose desirability is not affected by climate. (If the convention center is primarily targets trade shows, location in major population or industrial centers, is more relevant).

If the proposed location does not have these characteristics, the proposal has little prospect for success. If the location does have potential, the following principles should guide public action.

v. The private sector should own and operate the convention center.

vi. If private investors will not undertake an economically viable convention center without government support, the government can provide an incentive which should be, at most, the value of benefits that are not captured by private investors.

vii. All government support should be up-front in the form of a capital subsidy, which might take the form of providing land or providing infrastructure. It is undesirable for the public sector to provide <u>direct or indirect operating subsidies</u>.

2. Government Actions

With these principles in mind, governments and the Bank could support:

i. **Studies**

b. to analyze alternatives that include pooling arrangements for large convention hotels that would take advantage of video transmission for very large meetings and transportation between hotels for the many sub-meetings characteristic of large conferences;

c. to estimate the economic benefits of the convention center;

d. to identify the groups who receives them, and

e. to determine the amount of benefits that are not likely to captured or recognized by the private sector. This last amount is the basis to calculate the maximum amount of public subsidy that is economically justifiable.

ii. Institutional support

a. to put together consortia of investors who capture the benefits not included in profits on the rental of exhibition and meeting space, food service and equipment rentals. A consortium of the principal beneficiaries would be likely to include: a construction company, a company that specializes in event production, nearby hotels and restaurants, members of the Chamber of Commerce who have an interest in access to space for display, local land interest that may have an interest in the appreciation of property value in the area. There may be other minor investors such as travel agencies and operators or operators of attractions who may obtain profits from the operation of convention centers.

iii. Studies

a. to establish a regulatory framework or security package for prospective owners. The principal feature of the framework or security package would be a guarantee on the part of the public sector not to build competing facilities in the market area for a specified number of years.

iv. Contracting of an investment bank

a. to organize a Build-Own-Operate Concession in which bidders propose the capital subsidy that they require to build and operate a convention center. It is logical to consider only proposals that request less than the maximum justifiable subsidy. The successful bidder would provide a performance bond for the amount of the capital subsidy for five years of operation.

IV. CONCLUSION

State and municipal governments will be pressured by specific local interests to invest in convention centers. The investments will look politically attractive and will be supported by feasibility studies that present economic impacts based on multipliers rather than economic benefits based on sound economic analysis. Bank staff should be aware of the flaws in this analysis and insist on private ownership and management. The number of cases where public participation is justified is probably very small and the Bank can quickly screen for projects that have at least some prospect of viability. Once these opportunities have been detected, a sound analysis of economic benefits and beneficiaries can help delimit the nature and amount of public support.

The maximum amount of subsidy is determined by the profits earned by groups that do not invest in the convention center and by the amount of employment benefits. Employment benefits are defined as the wages received by groups working in enterprises that directly receive expenditures of the convention visitors less the wage they would have received if no convention center had been build. If the workers were previously informally employed or unemployed, the opportunity cost (shadow price) is assumed to be earnings in the informal sector. The benefits and employment effects must be adjusted for economic transfers.

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