



Booking Travel Online May be Costing States Half a Billion in Revenue

40-Plus States and Cities Have Filed Lawsuits Against Online Agencies

BY MEG WAGNER

Feb. 5, 2011

You're planning a trip. You log onto your favorite travel-booking site, pull out your credit card, type in your name, address, security code.

Congratulations: You've just rented a room with a view for \$250 a night.

Not all of that goes to the hotel, of course. A commission of \$25 is probably going to the travel site.

But it's that commission, that extra \$25, that may be costing states across the country millions and millions in revenue -- at a time when states are facing massive budget deficits.

More than 40 lawsuits have been filed across the country -- from Florida to Texas, from Myrtle Beach, S.C., to Oakland, Calif. -- to force online travel booking sites to pay taxes on the full amount paid by the consumer, not simply the amount the hotel receives.

Online travel companies maintain it's the room, not the commission, that should be subject to the tax.

The Two Sides Line Up

According to the Center on Budget and Policy Priorities (a policy organization that works "on fiscal policy and public programs that affect low- and moderate-income families and individuals"), every year the country loses as much as half a billion dollars when customers book rooms through online services.

At the end of last year, North Carolina passed a law mandating that these websites collect taxes on the full sale price. The N.C. Department of Revenue estimates that the state will gain \$4.9 million in the 2011-2012 fiscal year.

Paul Stone, president and CEO of the North Carolina Restaurant and Lodging Association, said he thinks this new law will have a positive impact on the state's economy. The additional revenue can go toward marketing and state services, and actually help increase tourism, he added.

"It's kind of logical," he said. "If the state has this revenue, it can better promote itself as a great tourist destination."

Andrew Weinstein uses a different logic.

Calls to Expedia and Orbitz were directed to Weinstein, spokesperson for the Interactive Travel Services Association, a trade organization representing online travel sites. He maintains that extending the hotel occupancy tax to the commissions "just doesn't make sense."

"It's like applying a car tax to boats," he said. "It's using a tax in a way it was never intended to be used."

Additionally, Weinstein said the courts have ruled "overwhelmingly" in favor of the travel companies.

Online Sites Are Winning the Battle

Of the lawsuits that have been filed, 15 have been settled. Twelve ruled in favor of the sites; two, from Atlanta and San Antonio, had split decisions; and only one, from South Carolina, ruled against the companies.

A verdict from an April 2009 case in Pitt County, N.C. – which came down before the state passed its law -- noted that the travel companies "in the present case do not physically control or furnish the rooms they advertise," nor do they "supply' or 'provide' rooms to visitors." Because of this, the court ruled in favor of the online travel companies.

"We have the legal track record on our side," Weinstein said. "It's common sense, and the courts can see that."

The Tax Foundation, a tax research group whose mission "is to educate taxpayers about...the size of the tax burden borne by Americans," also maintains that the tax should apply only to the cost of the hotel room.

"Let's pretend I book a block of rooms for a trip I'm planning with my buddies," said Joseph Henchman, tax counsel for the group. "I pay the price of the rooms and the tax on those rooms."

He explained that when he resells the rooms to his friends, he can mark up the price, but the taxes he paid on the rooms don't change. He believes this is the dynamic of travel websites.

"At no time are they the owner of the room," he said.

Political Hot Potato?

But Michael Mazerov, senior fellow at the Center on Budget and Policy Priorities, doesn't see it that way.

"A real estate agent doesn't buy the house and resell it to you," he said. "They act as a broker, but they are still taxed. This is no different."

Mazerov also said the issue is not only a matter of what's legal, it's also an issue of policy.

"From a legal standpoint, it may very well be the case that the laws are written now in such a way that these companies are not obligated to collect a tax on the markup price," he said.

Legal Fight: A Waste of Money?

"But as a policy issue, there is no doubt in my mind that the tax should be due."

To clear up any legal confusion and avoid further court cases, some states, such as North Carolina and New York, have recently reformed their laws to ensure that travel websites are required to collect tax on the price to the consumer.

Mazerov believes states that already have such laws in place are right to take the battle to the courtroom.

But John Stephenson of the National Tax Payers Union, a nonprofit group dedicated to lowering taxes, doesn't believe a legal fight is an "economically sound" idea. High litigation costs can eat up even more of the states' budgets, he said.

"When these cases go to court, both parties are fighting tooth and nail," Stephenson said. "There's so much time and money being wasted here."

Stephenson opposes the tax, but he also sees this as a much bigger, more political issue.

He believes this battle is the result of city and state government budget deficits. Rather than attempt to collect more revenue through hotel taxes, he said governments should find more long-term solutions to their revenue problems.

"The only reason our governments are going after these companies is that they need revenue," he said. "Instead, they need to reduce spending and keep taxes more manageable."

Additionally, Henchman, of the Tax Foundation, fears economic repercussions in extending the tax.

He said that in extreme cases, travel websites can "turn off" cities that have been particularly aggressive in their fight to extend the hotel tax.

He speculated that if a city becomes too firm, a booking website can choose to stop business with that community. This means a customer who searches for hotels in that area will yield no results, and no rooms can be purchased in that city through the website.

"That can't be good for anybody," he said. "In this economy, the last thing a city needs is to lose tourists and travel revenue."

The Battle Continues

The legal fight is far from over. While some cases have been decided, more are pending, and both sides of the debate feel optimistic about their prospects.

"We've done well in court in the past, and I predict that the courts will continue to side with us," Winestein said.