

San Francisco Chronicle

S.F. treasurer asks for hotel tax probe

Leal says city could be collecting more from third-party Internet travel sites that sell rooms at deep discounts

David Armstrong, Chronicle Staff Writer
Wednesday, October 22, 2003

San Francisco Treasurer Susan Leal has asked the city attorney's office to investigate whether cash-strapped San Francisco should be collecting more hotel tax revenue from popular Internet travel sites such as Expedia.com, Hotels.com and Travelocity.com.

Such Web sites typically buy blocks of hotel rooms at a low wholesale rate and sell them online to consumers for more than they paid for the rooms but less than the hotels would charge the consumer directly.

City officials say that, at a minimum, the third-party sites are paying taxes on the lower wholesale room rate. But they suspect the Internet sites may not be paying taxes on the higher commercial rate.

Leal said she doesn't know how much money the city may be losing. But she wants to find out.

Leal, who is a candidate for mayor, said she believes any shortfall from taxes on the city's 32,000 hotel rooms would be small, "but we are looking at it as a potential source of revenue. In the last couple of years, it (third-party Internet bookings) has just started to pick up."

An executive with Expedia.com declined to comment Tuesday. Officials with Hotels.com and Travelocity.com did not return telephone calls.

An industry expert, who requested anonymity, said third-party Web sites typically pay taxes on the lower room rate and pocket the difference.

The 14 percent hotel tax is an important source of revenue for San Francisco. The city took in \$132 million from the hotel tax in 2002, funneling millions into the general fund, convention facilities, and funding for arts and cultural groups, among other things.

Julie Van Nostern, head of the tax division in the city attorney's office,

confirmed that City Hall is looking into the matter. Van Nostern said the city has not decided whether it would take any legal steps to capture more hotel tax revenue if the funds are being withheld.

Industry observers said they could not think of a U.S. city that has used legal action to recover hotel tax revenue from Internet sites, and several insiders expressed misgivings about doing so.

"People in business buy wholesale and sell retail. That's an established method of doing business," said Deborah Reinow, vice president for tourism at the San Francisco Convention and Visitors Bureau. "Wholesale is a big part of the business in San Francisco or anywhere," she said, adding that tour operators, conventioners and others also often buy blocks of hotel rooms as part of travel packages.

"You've heard of Adam Smith and the invisible hand of the market. This is just that as a pure play," said industry analyst Anwar Elgonemy, of Jones, Lang LaSalle, a hotel consultancy. "I don't think it's illegal."

John Handlery, executive vice president and general manager of San Francisco's Handlery Hotels Inc. and next year's chairman of the San Francisco Convention and Visitors Bureau, said that if the city required third-party Web sites to pay more taxes, they would pass the higher cost on to consumers.

"Now would not be the time to raise rates," he said, referring to the long-slumping tourism business, San Francisco's leading generator of revenue.

Locally and nationally, online hotel booking is a growing area of e-commerce, attracting bargain-hunters in search of discounted rooms.

In addition to Web sites such as Hotels.com, Expedia.com and Travelocity.com, many hotels, especially major chains, maintain proprietary Web sites that use interactive features and customer loyalty points to attract travelers in lieu of steep discounts.

Tom Callaghan, of PFK Consulting's San Francisco office, estimates that 15 percent of hotel rooms in the Bay Area are booked online. Nationwide, 13 percent of hotel rooms will be booked online this year, with bookings split almost evenly between branded hotel sites and third-party sites, according to Connecticut online travel research firm PhoCusWright.

That number is expected to grow. By 2005, 22 percent of all U.S. hotel rooms will be booked online, said PhoCusWright consultant Bill Carroll, a visiting professor at the Cornell University hotel school. They will not necessarily be booked through third-party sites, he said.

"The chains have become very aggressive with their sites," Carroll said. "The Marriotts, the Hiltons and the Starwoods have made their sites very useful, with loyalty points awarded for booking with them."

Locally and nationally, hoteliers are using both their own sites and third-party sites to fill rooms that might otherwise sit empty in the soft U.S. economy.

Over the past three years, San Francisco hotels in particular have been hard hit by the dot-com implosion, the aftermath of the Sept. 11 terrorist attacks, the war in Iraq and last spring's outbreak of SARS, or severe acute respiratory syndrome.

Hotel occupancy rates in the city, which peaked in the high 80 percentile in the boom years of the 1990s, dropped to 60 percent after Sept. 11. This August, however, the citywide occupancy rate hit 83.1 percent, up 11.3 percent from August 2002, though the average daily room rate fell to \$130.41, down 2.9 percent from \$134.34 a year ago.

E-mail David Armstrong at davidarmstrong@sfchronicle.com.