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Sacramento says online travel sites may owe millions

Virtual taxes very real for city

Sacramento Business Journal - by Mark Anderson Staff writer

The city of Sacramento is going after the nation's best-known online travel sites for money it says should have been paid to the city over much of the past decade.

The complaint is that when customers book hotel rooms through online travel companies, the sites charge room taxes based on the retail rate, and then pay the taxes based on what they sell to hotels at the wholesale rate. Sacramento argues the entire tax charged should be passed along to the city.

And it's not alone.

The city of Anaheim last month won a $21.3 million judgment in an administrative hearing from Expedia, Orbitz, Priceline, Travelocity and others.

Similar suits are brewing in Texas, where a federal judge authorized a class action case. Los Angeles is also interested in collecting its alleged unpaid tax, and San Francisco has been working on the issue for a year.

The Anaheim case involved 11 online travel companies, including Expedia, Priceline.com, Travelocity and Orbitz Worldwide Inc.

Sacramento's argument is that the companies collected a tax, and they must pass that tax from the taxpayer to the local entity.

"They are charging taxes on the retail price and they are disbursing what they would pay on the wholesale price for transient-occupant tax," said Eileen Teichert, Sacramento city attorney. "We are very much pursuing this."

The city of Sacramento has not sued, because it is working with the reservation companies to see if they can prove they remitted the correct amount. It is focusing on the same 11 companies as Anaheim.

"We are exhausting our administrative remedies," Teichert said. The city has been looking at the issue for about a year, and it engaged outside counsel, the law firm Kiesel Boucher Larson LLP in Beverly Hills, to do the work. Kiesel Boucher Larson represented Anaheim.

"They collected the tax on retail price and remit the tax on wholesale price," said Bill Larson, partner with the Kiesel Boucher Larson.

California has a "privilege tax structure," which means that the person getting the privilege pays the tax, Larson said. In the case of room taxes, the person renting the room has the privilege of occupancy and therefore pays the tax.

All travel companies contacted referred calls to the Interactive Travel Services Association and Art Sackler, its executive director. Sackler did not return calls seeking comment.

In other cases, Sackler has argued that online companies have no role to play in the day-to-day operation or management of hotels, and therefore they are not lodging retailers subject to the tax.

The Anaheim award was the result of an administrative hearing, but it seemed more like a trial, Larson said. There were hundreds of exhibits and eight days of hearings.

The travel companies are seeking to overturn the Anaheim decision. Anaheim's position is that the travel companies should pay the judgment first and then seek their appeals.

The winning argument in Anaheim, Larson said, was that the online travel companies are merely collection agents, and the taxes they collect should be passed through.

"They have concocted a strategem of collecting higher taxes and keeping them," Larson said.

The city of Sacramento's position is that online travel companies are keeping a portion of hotel room taxes that belong to the city.

Using Sacramento as an example, the online travel companies collect the local 12 percent room tax from the customer based on the retail price. If the customer reserves a $100 room, the company collects $112 for the room and the tax. When the online company books that customer into a room, it is at the wholesale price, say $50, plus the 12 percent room tax on $50, which is $6. Sacramento is arguing that the $12 collected is a tax, and it cannot become part of the company's profit. Once collected as a tax, it has to pass through to the levying agency.