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UPDATE TO INTERIM PROJECT REPORT 2005-131: APPLICATION OF THE TRANSIENT RENTAL TAX TO ACCOMMODATIONS PURCHASED VIA THE INTERNET

Statement of the Issue

Internet room providers perform a valuable service by allowing people to easily compare prices and make room reservations. Hotels benefit from the added promotion and the extended distribution chain offered by these companies. But using an Internet connection to make a reservation does not, by itself, determine the legal responsibility to collect and remit transient rental tax. Recent questions about the application of the transient rental tax to accommodations purchased via the Internet have arisen due to a shift by Internet room providers to a new business model, the “merchant model,” that is described below.

Interim Report Number 2005-131, by the Committee on Government Efficiency Appropriations, reviewed the business practices used by Internet companies that offer to reserve hotel rooms for guests. The Report’s central issue was whether transient rental tax is due on the amount collected by an Internet hotel room provider, or the amount collected by the hotel. The issue is unresolved. This update recaps arguments for and against the application of the tax to Internet room providers and notes significant developments since publication of the 2005 Interim Report.

Discussion

The Transient Rental Statutes at Issue

Florida’s transient rental tax is imposed at the state and local levels by parallel, but not identical, statutory provisions.¹

¹ **A the state level, section 212.03, F.S., imposes state transient rental tax as follows:**

(1) It is hereby declared to be the legislative intent that every person is exercising a taxable privilege who engages in the business of renting, leasing, letting, or granting a license to use ... any hotel....

(2) The tax provided for herein shall be in addition to the total amount of the rental, shall be charged by the lessor or person receiving the rent in and by said rental arrangement to the lessee or person paying the rental, and shall be due and payable at the time of the receipt of such rental payment by the lessor or person, ... who receives said rental or payment....

At the local level, subsection 125.0104(3), F.S., authorizes a local tourist development tax (TDT) as follows:

(3)(a) It is declared to be the intent of the Legislature that every person who rents, leases, or lets for consideration any living quarters or accommodations in any hotel ... is exercising a privilege which is subject to taxation under this section....

(c) The tourist development tax shall be levied, imposed, and set by ... at a rate of 1 percent or 2 percent of each dollar and major fraction of each dollar of the total consideration charged for such lease or rental.

(f) The tourist development tax shall be charged by the person receiving the consideration for the lease or rental, and it shall be collected from the lessee, tenant, or customer at the time of payment of the consideration for such lease or rental.

(g) The person receiving the consideration for such rental or lease shall receive, account for, and remit the tax to the Department of Revenue at the time and in the manner provided for persons who collect and remit taxes under s. 212.03....

Background - The Merchant Model²

As the phrase is used here, Internet room providers are independent third parties that offer to reserve a room using either the “agent,” or the “merchant” business model. Travel agents have been allowed computerized access to search hotel room inventories and to book discounted hotel rooms in the name of, and for the account of, other people (i.e., as intermediaries) since the 1970s. The agent model calls for the hotel to compensate the agent with a commission based on a room rate set by the hotel. The room rate is subject to tax without any reduction for the commission.

Under the “merchant” model, the Internet room provider (merchant) enters into contracts with hotels to offer rooms to the public. The hotel agrees to make rooms available for booking at a negotiated rate. The negotiated rate cannot be disclosed to the public. The merchant agrees to pay the hotel the negotiated room rate and to also forward money it collects from the customer to pay applicable taxes. The merchant advertises the Internet room rate and discloses separate charges for taxes and service fees to the customer. The Internet room provider acts as the merchant of record in booking the room and initiates a charge to the customer’s credit card for the full room rate plus the disclosed line items. The guest receives confirmation of the reservation from the merchant. When the hotel sends the merchant an invoice for the room after the guest’s stay, the merchant pays the negotiated room rate and the tax due on that amount. If no invoice is sent, the merchant may keep the money.

The Issues

Internet room providers read the Florida statutes such that, without regard to who receives payment from a guest, tax is measured by the amount paid to a landlord for the right to use transient accommodations. They argue that the tax is an occupation tax levied on people engaged in the business of renting transient accommodations.³ The taxable incident is not the isolated receipt of the rental payment, but the exercise of the privilege – the assemblage of activities consistent with ownership. Under this line of reasoning, money received to facilitate a booking, process a reservation application, or provide a similar service, is not subject to tax when a company lacks a ownership interest in the hotel room. This position extends to the tax treatment of customer charges variously labeled as “tax reimbursements,” “tax recovery charges,” or “taxes and fees.” Additionally, the argument goes, tax is not due at the time money is paid to the Internet room provider by the guest. Instead, it should be remitted by the hotel, as landlord, once the negotiated room charge is forwarded to the hotel after the guest’s stay.

Countering this argument, local governments contend that Internet room providers using the merchant model are sales tax dealers and that the transaction is a taxable “sale.”⁴ In return for the required payment from guests, hotels provide real property, tangible personal property and services and Internet room providers step into the shoes of the hotel when they receive the payment from the guest. They contend that dividing the sale of a hotel room into discrete transactions ignores the sale’s singular nature.⁵ They are concerned that allowing intermediaries to shoehorn customary hotel services into the non-taxable category will erode the tax base. Finally, they argue that transient rental tax is due at the time of collection, not later when the hotel is paid the negotiated rate.

The Florida Department of Revenue does not take an official position on whether tax is due on the amount collected and retained by Internet room providers. The agency does not take a position on whether tax is due on the additional charges variously labeled as “tax reimbursements,” “tax recovery charges,” or “taxes and fees.” It does not take a position on whether tax should be remitted at the time the customer pays for the reservation.

² For a detailed description of the merchant model, see, *Columbus, Georgia v. Expedia*, Civil Action No. SU-06-CV-1974-7 (Superior Court, Muscogee County, Ga, Sept. 22, 2008).

³ *Gaulden v. Kirk*, 47 So.2d 567 (Fla. 1950); *Florida Hotel and Motel Ass’n, Inc. v. Dep’t of Revenue*, 635 So.2d 1044 (Fla. 1st DCA 1994); see also, *Florida Rev. Comm’n v. Maas Bros., Inc.*, 226 So.2d 849 (Fla. 1st DCA 1969).

⁴ Section 212.02(16)(b), Florida Statutes, defines “sale” as including: “[t]he rental of living quarters or sleeping or housekeeping accommodations in hotels, apartment houses or roominghouses, or tourist or trailer camps....”

⁵ See, *Florida Hotel and Motel Ass’n, Inc., supra*; *American Tel. & Tel. Co. v. Dep’t of Revenue*, 764 So.2d 665 (Fla. 1st DCA 2000).

The 2005 Interim Report concluded that, “remitting taxes on the discounted rate paid by the Internet intermediaries to the hotels and not on the higher amounts actually paid by the customer occupying the room is in violation of Florida law.” Report, p. 27.

Litigation in Florida⁶

Orange County, Florida, self-administers the local tourist development tax (TDT). It brought a lawsuit against several Internet room providers looking to determine whether tax is due “on the difference between the wholesale price and the retail price they receive for the rooms when they re-sell them.”⁷ The trial court dismissed the case, ruling that the county must complete audits first. The appellate court reversed the trial court. The opinion did not suggest who might eventually win, only that the county is entitled to know whether it can lawfully assess the TDT before attempting to audit the companies. The Internet room providers have asked the Florida Supreme Court to review that ruling. In the meantime, absent reversal by the Supreme Court, the trial court can proceed and it may answer the question within the next several months.

Legislation

The 2005 Interim Report recommended legislation requiring the tax be paid prospectively on the total charge made to a guest using one of two options. Under the working-group proposal mentioned in the Report, an Internet room provider can collect tax on the total amount paid by the guest. It can then remit its share of transient rental tax on its fee and pay the hotel the balance of tax due on the negotiated room rate when it pays for the room. Or, the Internet room provider can tell the hotel the total amount paid by the guest and pass along the tax due on that amount for the hotel to pay. The proposal was not taken up in the 2005 regular session.

CS/SB 2788 and HB 7147 were offered during the 2008 legislative session. These bills would eliminate tax on the amount retained by Internet room providers. "Consideration," "rental," and "rent" were defined to exclude payments received by an unrelated person “for facilitating the booking of reservations for or on behalf of a lessees or licensees at hotels. . . .” The bills defined an "unrelated person" as one who is not in the same affiliated group of corporations pursuant to federal law. This constraint recognizes that shared control over the intermediary and the hotel means that the room rate is not the product of an arms-length bargain and can be lowered to avoid tax.

However, the federal definition does not assure that only Internet room providers who negotiate bona fide arms length contracts with hotels will enjoy the exclusion. Moreover, these bills may exclude fees charged by property management companies and other third-party agents on which tax is currently due and remitted.

⁶ Lawsuits in other states, when not disposed of on procedural grounds, often “are based on the specific language of each jurisdiction’s taxing scheme and on the variety of causes of action pled....” *Orange County v. Expedia, Inc. et al.*, Case No. 5D07-2787 (Fla. 5th DCA 6/13/2008), *appeal pending, Expedia Inc. et al. v. Orange County*, Case No. SC08-1536 (Fla. Supreme Court). Numerous challenges have been brought by local governments throughout the United States. None can dispose of the issue in Florida given the state’s unique statutes and judicial precedent.

⁷ *Orange County*, at 2.