

City of Galveston
Online Travel Companies Hotel Occupancy Tax Audit Report
City Auditor Executive Summary

May 8, 2013

The City Auditor discovered on August 5, 2011 ongoing class action litigation between 173 Texas cities and Online Travel Companies (OTC's) such as Expedia, Hotels.com, Hotwire, Priceline, and others. The ongoing litigation is in relation to the 173 Texas cities claim that OTC's had deprived each city of hotel tax revenue. The basis of the claim is that OTC's are obligated to collect and pay hotel occupancy taxes on the total amount that hotel guests pay for rooms instead of the lower amount that the OTC's pay hotels for the right to resell the rooms.

Scope

The scope of our audit is two-fold. The First is to determine if the City of Galveston has been deprived of hotel occupancy tax revenue from the OTC's. The Second is to determine the dollar amount due to the City of Galveston if indeed the City of Galveston has been deprived of hotel occupancy tax revenue from the OTC's.

Fieldwork Performed

1. The City Auditor analyzed the City of Galveston Code of Ordinances to determine if a specific amount had been defined in which hotel occupancy tax is to be levied upon. The City Auditor is taking the position that if the City of Galveston did define a specific amount in which to levy and collect hotel occupancy taxes, then any business plans prohibiting this to occur is depriving the City of Galveston to collect all hotel occupancy tax revenues as originally intended.
2. The City Auditor mailed out questionnaires to 30 hotels located in Galveston, Texas on December 1, 2011. The questionnaires asked each hotel for an estimate of the percentage of gross receipts collected from occupancy of rooms sold to online booking companies like Expedia, Hotels.com, Hotwire, Priceline, etc. for the time period between July 1, 2010 and June 30, 2011. The questionnaire also stated that the information provided to the City of Galveston from each hotel would be held confidential to the extent that the law allows.

Summary of Results

1. The City Auditor has concluded that the City of Galveston did define and establish a specific amount that hotel occupancy taxes are to be levied and collected. The City of Galveston Code of Ordinances, Part II, Chapter 33 – Taxation, Article III, Section 33-86 Definitions states: *“Consideration means the cost of the room in such hotel only if the room is one ordinarily*

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used for sleeping, and is two dollars (\$2.00) or more per day, but shall not include the cost of any food served or personal services rendered to the occupant of such room not related to the cleaning and readying of such room for occupancy.” The key words in this definition are “Consideration means the cost of the room in such hotel”.

2. Based upon the questionnaires returned, the City Auditor calculated that the City of Galveston is being deprived by the OTC’s of approximately \$250,000 annually in hot tax revenues. These calculations are kept confidential as stated in the questionnaires sent out to the hotels. The OTC industry began in the year 2000 according to research performed on the Internet, therefore equating to a total approximate loss of hotel occupancy tax revenues to the City of Galveston in the amount of 3 million dollars to date.

City Auditor’s Recommendations

1. The City Auditor recommends that this audit report be referred to the City Attorney’s Office.
2. The City of Galveston’s Code of Ordinances should be revised, if possible, so that all hot tax revenues associated with OTC transactions are collected up front at the time the OTC’s pay the hotels for the right to resell the rooms.
3. The City Auditor recommends that the Mayor and City Council determine an allocable percentage to be divided between tax, municipal fines, and audit fee reimbursement in the event of a lump sum collection from the OTC’s.
4. The City Auditor recommends that approval be given to seek a “Finder’s Fee” payment pursuant to HB 2048 from the Texas State Comptroller if collection or a judgment is received from the OTC’s.

City Managers Response

The City Auditor, Attorney, Manager, and Finance Director met to review the potential for a initiative focused on the OTCs, and the timing, available staff, and needed budget for such an initiative. Based on that review, staff is advising we

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