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To: The Honorable Glenn Wakai, Chair
and Members of the Senate Committee on Economic Development, Tourism, and Technology

The Honorable Rosalyn H. Baker, Chair
and Members of the Senate Committee on Commerce, Consumer Protection, and Health

Date: Wednesday, February 7, 2018
Time: 1:15 P.M.
Place: Conference Room 414, State Capitol

From: Linda Chu Takayama, Director
Department of Taxation

Re: S.B. 2657, Relating to Transient Accommodations Tax

The Department of Taxation (Department) appreciates the intent of S.B. 2657 and offers the following comments for the Committee's consideration.

Summary of S.B. 2657

The stated purpose of the bill, which is effective on July 1, 2018, is to impose the transient accommodations tax (TAT) on each person's share of income when accommodations are booked through an online travel agency, international or domestic wholesale travel company, or booking platform. To achieve this purpose, the bill makes the following amendments to chapter 237D of the Hawaii Revised Statutes (HRS):

Definitions

- "Travel agency" is defined as having the same meaning as in HRS section 468L-1, which defines travel agency as any person who for compensation acts as an intermediary between a purchaser and seller of travel services.
- "Transient accommodations remarketer" replaces the definition of "transient accommodations broker" and is defined as any person who operates or markets transient accommodations through wholesale travel companies, online websites, online travel agencies, online booking agencies, or booking platforms that advertises, books, or collects

payment for transient accommodations or time shares.

- "Gross rental" or "gross rental proceeds" in HRS section 237D-1 is amended as including the gross amount collected from the consumer, including booking fees, cleaning fees, lodging fees, transient fees, and other fees, but excluding fees for ground transportation, airfare, meals, excursions, tours, or other items included in a travel package other than accommodations.

Imposition of TAT

- The TAT will be imposed on transient accommodations remarketers and travel agencies who collect payment for transient accommodations.
- When transient accommodations are furnished through transient accommodations remarketers or travel agencies at noncommissioned negotiated contract rates, the TAT will apply to each person with respect to that person's portion of the proceeds.

Registration

- Transient accommodations remarketers and travel agencies will be required to register with the Department.

Allocation of funds

- TAT collected from transient accommodations remarketers and travel agencies will be allocated to the counties and placed into a tourism impact fund

Background

Under current law, the imposition of the TAT on transient accommodations sold through a travel agency or tour packager varies depending on whether the transaction was on a commissioned or noncommissioned basis. In Travelocity.com, L.P. v. Director of Taxation, 135 Hawaii 88 (2015), the Hawaii Supreme Court explained that a "commission" is a "fee paid to an agent or employee for a particular transaction, usually as a percentage of the money received by the transaction." Travelocity, 135 Hawaii at 111 (quoting Black's Law Dictionary 327 (10th ed. 2014) (internal quotations omitted). The court further explained that a "noncommissioned rate" is "an amount of money paid to an entity or person other than an agent or an employee." Travelocity, 135 Hawaii at 111. The court clarified that unlike a commissioned transaction, in which a fee is usually paid as a percentage of the income received, in a noncommissioned transaction, a hotel has no means of knowing what the travel agent's mark-up will be. In sum, when a hotel pays a travel agent for a room on a commission basis, the room rate is readily definable, but in a noncommissioned transaction, the hotel has no means of knowing the travel agent's markup and actual room rate. Id.

When transient accommodations are furnished through arrangements made by a travel agency or tour packager at noncommissioned negotiated contract rates, the TAT is imposed solely on the operator on its share of the proceeds. There is no tax imposed on the travel agency's or tour packager's share of proceeds. In comparison, when transient accommodations are furnished through a travel agency or tour packager on a commissioned basis, the TAT is imposed on the gross proceeds of the operator, including the commission paid to the travel agency or tour packager. Similarly, when transient accommodations are sold directly by the operator, the TAT is imposed on the gross proceeds of the operator. Accordingly, the TAT imposed on a unit will differ depending

on whether the unit was sold directly by the operator, sold by a travel agent or tour packager on a commissioned basis, or sold by a travel agent or tour packager on a noncommissioned basis.

For example, if a room is sold for $100 to a guest directly by a hotel, the hotel will owe $10.25 in TAT (10.25 percent of $100). Similarly, if a room is sold for $100 by a travel agency who earns a $20 commission on the transaction, the hotel will owe $10.25 in TAT (10.25 percent of $100). If, however, the same room is sold for $100 by an online travel company (OTC) who has a noncommissioned agreement with the hotel and keeps $20 from the transaction, the hotel will owe $8.20 in TAT (10.25 percent of $80); the $20 kept by the OTC is not subject to TAT. If a room is sold through a booking platform and the guest is charged $105, which includes a $5 fee charged by the booking platform directly to the guest and a $100 rate set by the operator from which $20 is paid to the booking platform as a fee, the operator will owe $10.25 in TAT (10.25 percent of $100). These concepts are illustrated in the following table:

Type of Transaction	Amount Paid by Guest	Amount Kept by Travel Agency	Amount Kept by Operator	TAT Base	TAT Due
Direct sale by hotel	$100	$0	$100	$100	$10.25
Sold by travel agent on commissioned basis	$100	$20	$80	$100	$10.25
Sold by travel agent on noncommissioned basis	$100	$20	$80	$80	$8.20
Sold by booking platform (separate fees charged to guest and operator)	$105	$25 ($5 from guest and $20 from operator)	$80	$100	$10.25

Comments

First, the Department notes that although this bill achieves its stated purpose of imposing TAT on each person's share of income when transient accommodations are booked through a travel agency at noncommissioned negotiated contract rates, the bill will also increase the base for TAT on certain commissioned transactions. The bill, by imposing the TAT on all travel agencies and transient accommodations remarketers and expanding the definition of gross rental proceeds, will result in situations in which the TAT is imposed on the commission income twice—once on the operator and a second time on the travel agency.

For example, if a room is sold for $100 to the guest, $20 of which is paid to the travel agency as a commission, the operator will be subject to TAT on $100 and the travel agency, if it has nexus, will be subject to TAT on $20. The base of the TAT will therefore exceed 100 percent of the total charged to the customer (*i.e.*, although the customer is charged $100, the base of the TAT will be $120). In comparison, the base of the TAT for noncommissioned transactions will only be 100 percent of the total charged to the customer because of the provision in the bill that each person in a noncommissioned transaction is only liable for TAT on that person's share. The Department notes

that a similar provision that each person is only liable for TAT on that person's share in a commissioned transaction is not advisable, as it will result in a decrease in TAT, as commissions would not be subject to TAT if the travel agency does not have nexus.

The Department therefore suggests amending HRS section 237D-2 so that the TAT is only imposed on travel agencies and transient accommodations remarketers who arrange or book transient accommodations at noncommissioned negotiated contract rates. As explained above, imposition of the TAT on travel agencies and transient accommodations remarketers for commissioned transactions is unnecessary because the commission is already subject to tax as part of the operator's base. The Department suggests the following language for HRS section 237D-2:

> Every operator, and every transient accommodations remarketer[~~,~~] or travel agency who [~~collects whole or partial payment for transient accommodations~~] arranges transient accommodations at noncommissioned negotiated contract rates, shall pay to the State the tax imposed by subsection (a), as provided in this chapter.

Second, the Department notes that the amendment to the definition of "gross rental" in Section 2 of this bill adds a broad catchall for "any other fees collected," but also broadly limits the catchall by excluding "other items included in a travel package, other than accommodations." To avoid ambiguity, the Department suggests amending the definition to read:

> . . . . gross sale or gross charges collected from consumers, including but not limited to booking fees, cleaning fees, lodging fees, transient fees, or any other fees collected, but does not include fees collected for ground transportation, airfare, meals, excursions, tours, or other [~~items included in a travel package, other than accommodations,~~] fees unrelated to the transient accommodations, . . .

Third, the Department notes that if general excise tax and/or TAT are visibly passed on to the customer, those amounts are not subject to TAT. Accordingly, for consistency, the Department suggests amending the definition of "gross rental" in Section 2 of this bill to exempt TAT that is visibly passed on to the customer by a travel remarketer or travel agency:

> The words "gross rental" or "gross rental proceeds" shall not be construed to include the amounts of taxes imposed by chapter 237 or this chapter on operators of transient accommodations, transient accommodations remarketers, or travel agencies and passed on, collected, and received from the consumer as part of the receipts received as compensation for the furnishing of transient accommodations.

Fourth, the Department notes that this bill requires all transient accommodations remarketers and travel agencies to obtain a certificate of registration under HRS section 237D-4. Only transient accommodations remarketers and travel agencies who book rooms at noncommissioned negotiated contract rates, however, should be subject to the TAT and required to obtain a certificate of registration. Additionally, the bill does not require travel agencies or transient accommodations remarketers to pay any fee for registration. The Department suggests a one-time fee of $15, similar to the amount for registration of transient accommodations of six or more units. The Department also notes that the amendment requiring transient accommodations remarketers and travel agencies to register the physical address of each transient accommodation in the State is confusing and its purpose is unclear. Accordingly, the Department suggests adding a new subsection in HRS section 237D-4 to read as follows:

> Each transient accommodations remarketer or travel agency, as a condition precedent to entering into an arrangement to furnish transient accommodations at noncommissioned negotiated contract rates, shall register with the director. The travel agency or tour packager shall make a one-time payment of $15 for each registration, upon receipt of which the director shall issue a certificate of registration in such form as the director determines, attesting that the registration has been made. The registration shall not be transferable and shall be valid only for the transient accommodations remarketer or travel agency in whose name it is issued.

Fifth, the Department respectfully requests that the bill is amended to apply to tax years beginning after December 31, 2018 to allow sufficient time to make the necessary form and computer system changes.

Finally, the Department has concerns regarding the new allocation provision in HRS section 237D-6.5. This allocation may result in the disclosure of confidential taxpayer information as there may be a limited number of taxpayers that fall within the categories of "transient accommodations remarketers" and "travel agents" that are subject to TAT. If the Legislature intends to increase the TAT allocation to the counties, the Department suggests amending HRS section 237D-6.5(b)(4).

Thank you for the opportunity to provide comments.

TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
TWENTY-NINTH LEGISLATURE, 2018

ON THE FOLLOWING MEASURE:
S.B. NO. 2657, RELATING TO TRANSIENT ACCOMMODATIONS TAX.

BEFORE THE:
SENATE COMMITTEES ON
ECONOMIC DEVELOPMENT, TOURISM, AND TECHNOLOGY, AND ON
COMMERCE, CONSUMER PROTECTION, AND HEALTH
DATE: Wednesday, February 7, 2018 **TIME:** 1:15 p.m.

LOCATION: State Capitol, Room 414

TESTIFIER(S): Russell A. Suzuki, Acting Attorney General, or
Mary B. Yokota, Deputy Attorney General

Chairs Wakai and Baker and Members of the Committees:

The Department of the Attorney General has concerns about this bill because it may be challenged as violating the federal Stored Communications Act (SCA), 18 U.S.C. § 2701, et seq., that protects the privacy of online communications.

This bill defines a "transient accommodations remarketer" as including a person or entity that operates or markets transient accommodations through "online websites, online travel agencies, online booking agencies, or booking platforms[.]" (Page 9, lines 13-20). The bill, at section 4, page 10, lines 10 – 16, requires that each transient accommodations remarketer register the name and physical address of each transient accommodation with the Director of Taxation as a condition precedent to engaging or continuing in the business of furnishing transient accommodations.

The SCA protects communications held by: (1) an electronic communication service (ECS) which is “any service which provides to users thereof the ability to send or receive wire or electronic communications.” § 2510(15); or (2) a remote computing service (RCS), which is “the provision to the public of computer storage or processing services by means of an electronic communications system.” § 2711(2). If an entity is deemed to be an ECS or RCS, a governmental entity may not compel the ECS and/or RCS to provide stored wire or electronic communications and records absent a subpoena, warrant, court order, or the authorized consent of the ECS and/or RCS.

In *HomeAway.com, Inc. v. City of Portland,* Civ. No. 17-00091-MO (2017), the City of Portland conceded that the SCA preempted ordinances that required: (1) operators (as that term is defined in the Portland ordinances) to state their names, affiliated companies or brands, addresses, and other information "to facilitate the collection of the short-term rental tax as the Division may require"; and (2) operators to state certain information upon registration of doing business and the prominent display of a Certificate of Authority from the Revenue Division by those seeking occupancy.

To avoid a challenge under the SCA, we suggest that this bill be amended to provide that transient accommodations remarketers obtain prior written consent from their operators and plan managers to disclose all information required in chapter 237D, Hawaii Revised Statutes, or that the department be required to obtain a subpoena prior to disclosure of the information requested in this bill.

Thank you for the opportunity to provide comments.

COUNTY COUNCIL

COUNTY OF MAUI
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WAILUKU, MAUI, HAWAII 96793
www.MauiCounty.us

February 6, 2018

TO: The Honorable Glenn Wakai, Chair
Senate Committee on Economic Development, Tourism and Technology

FROM: Mike White
Council Chair

SUBJECT: **HEARING OF FEBRUARY 7, 2018; TESTIMONY IN SUPPORT OF SB 2657, RELATING TO TRANSIENT ACCOMMODATIONS TAX**

Thank you for the opportunity to testify in **support** of this important measure. The purpose of this bill is to ensure the State receives the full amount of transient accommodations tax ("TAT"), calculated based upon the full or gross rental price paid by the visitor, whether that amount is collected by a local Hawaii operator, travel agent, wholesale travel company, or online by an online travel agency or booking platform.

The Maui County Council has not had the opportunity to take a formal position on this proposed bill. Therefore, I am providing this testimony in my capacity as an individual member of the Maui County Council.

I **support** this measure for the following reasons:

1. When chapter 237D, Hawaii Revised Statutes ("HRS") was originally passed, it did not contemplate the variety of methods that would be developed to market and sell transient accommodations, or the number of parties involved. The proposed bill brings the HRS up to date with current technology, including online websites and booking methods.

2. As a result, the State does not collect the full amount of TAT from accommodation remarketers like Expedia, Pleasant Hawaiian Holidays, Delta Vacations, VRBO, Travelocity, or Orbitz. If an accommodation sells for $200 per night, for example, the remarketer will generate their portion of the revenue by negotiating a net rate of say, $150. While remarketers are required to pay the general excise tax on their $50 share, they are not responsible for collecting or paying TAT on their share. Some companies collect the TAT from the visitor and keep it, and others do not collect TAT.

3. Through the way the law is currently written, TAT only needs to be paid to the State on the hypothetical $150 paid to the accommodation operator, not the full $200 market rate, despite consumers paying taxes on the higher amount. Remarketers who tax the TAT on the higher amount currently pocket the difference between taxes collected and what is required to be paid to the State.

4. Rough calculations indicate the State is likely missing out on upwards of $1,100 of revenue per hotel room, per year. The proposed bill taxes gross proceeds collected from consumers, including applicable fees, thus closing the current loophole for remarketers.

5. The proposed bill rightfully holds each party involved in a transaction explicitly accountable for the payment of the TAT on their portion of proceeds, whether it be local operators, travel agents, wholesale travel companies, or online booking agencies or platforms. This brings fairness to the applicability of the TAT in such transactions.

6. From Fiscal Year 2007 to 2017, the four counties collectively received a mere $2.2 million increase in TAT, while expenses for fire, police, and park services alone have increased by more than $260 million. The proposed bill remits additional revenue to the counties to help support services and infrastructure vital to the booming visitor industry.

For the foregoing reasons, I strongly **support** this measure.

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LEGISLATIVE TAX BILL SERVICE

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: TRANSIENT ACCOMMODATIONS, Attach Liability to Intermediary

BILL NUMBER: SB 2657

INTRODUCED BY: BAKER, ENGLISH, GALUTERIA, HARIMOTO, INOUYE, KIM, NISHIHARA, RUDERMAN, S. Chang

EXECUTIVE SUMMARY: Clarifies that the transient accommodations tax shall be calculated based on the gross rental price paid by a visitor. Specifies that the transient accommodations tax is to be collected from operators or transient accommodations intermediaries that collect whole or partial payment for transient accommodations. Trying to expand the tax base in such a manner may have the unintended effect of discouraging those who would like to bring tourists to Hawaii and take care of them here.

SYNOPSIS: Adds a new definition of "travel agency" to section 237D-1, HRS, by cross-referencing section 468L-1, HRS.

Amends the definition of "gross rental" in section 237D-1, HRS, to clarify that it applies to the gross sale or gross charges collected from consumers, including but not limited to booking fees, cleaning fees, lodging fees, transient fees, or any other fees collected, but does not include fees collected for ground transportation, airfare, meals, excursions, tours, or other items included in a travel package, other than accommodations.

Changes the definition of "transient accommodations broker" in section 237D-1, HRS, to "transient accommodations remarketer" and defines one as any person or entity, including but not limited to persons who operate or market transient accommodations through wholesale travel companies, online websites, online travel agencies, online booking agencies, or booking platforms, that offers, lists, advertises, or accepts reservations or collects whole or partial payment for transient accommodations or resort time share vacation interests, units, or plans.

Amends section 237D-2, HRS, to impose the tax upon every operator, transient accommodations remarketer, or travel agency who collects whole or partial payment for transient accommodations.

Amends section 237D-4, HRS, to impose a registration obligation on a transient accommodations remarketer or travel agency the same as on an operator or plan manager. Does not, however, require a remarketer or travel agency to pay a license fee.

Makes corresponding changes in nomenclature throughout chapter 237D, HRS.

EFFECTIVE DATE: July 1, 2018.

STAFF COMMENTS: This bill appears to be a reaction to the Hawai'i Supreme Court's decision *In re Travelocity.com, L.P.*, 346 P.3d 157 (Haw. 2015). The Travelocity case dealt with

hotel rooms provided under a "merchant model." To illustrate what this model is and what the case held, suppose a hotelier wants to rent out a short-term rental for $110. An online travel company (OTC) contracts to rent the room for $100, at which point it becomes the OTC's obligation to pay the $100 whether or not the OTC is able to find a tourist to put in the room. If the OTC is successful in finding a tourist, suppose the OTC charges the tourist $120 (something the hotelier wouldn't know and isn't told).

In this situation, the Department of Taxation assessed the OTC for TAT and GET on the $120, although the hotelier was paying TAT and GET on the $100. Our supreme court held that the OTC was not a hotel operator and was not liable for the TAT. The court also held that the OTC was subject to the GET, but that the room was provided at noncommissioned negotiated contract rates, triggering an "income splitting" provision providing that each of the parties involved is to pay the GET on what they keep. Thus, the OTC would pay GET on $20, which is the spread between the tourist's price ($120) and the room rent that was paid to the hotelier ($100).

The concern that this bill seems to address is that TAT is now being paid on only $100 when the tourist has parted with $120 for a hotel room.

Stepping back for a second, consider Attorney General Opinion 65-6, from the days before the TAT even existed. There, the Attorney General considered the taxability of a local travel agent earning money in Hawaii for organizing a tour to the mainland including sending a local tour conductor with the group, and, conversely, a mainland travel agent organizing a tour to Hawaii. The Attorney General held that our GET applied to the local travel agent's commissions, even if they were earned partly because of the local tour conductor's services outside Hawaii; and, conversely, that it did not apply to the mainland travel agent's commissions, even if the mainland agent sent a tour conductor here.

The result appeared to be largely practical: if the state attempted to tax an out-of-state travel agent with no presence or only a fleeting presence within Hawaii, difficult federal constitutional questions would be presented.

That problem still has not gone away even with the technological advancements we now have. If the only connection an OTC has with Hawaii is a software platform used by Hawaii hotels and other customers, questions of practicality and constitutionality will be presented. These questions cannot be legislated away. If we attempt to grab and wring dry the travel agents and tour companies that have set up a branch in Hawaii when we can't do the same to travel agents and tour companies that never set foot on our shores, we run the very practical risk of discouraging those who want to take care of their tourist customers in Hawaii while employing local people, and encouraging those who stay offshore, take our tourists' money, and contribute much less to our culture and economy.

Digested 2/6/2018