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Five Important SALT Issues Affecting Hotels

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Hotel operators face a myriad of state and local tax challenges given the unique nature of the hospitality business. In addition to dealing with state taxes, such as sales and use, income/franchise, and property tax, hotels in many jurisdictions are also required to collect and report an industry-specific hotel tax. Most states impose tax on the charges for room occupancy and also allow cities and/or counties to impose their own taxes on room occupancy charges. The revenue from these local taxes is often dedicated to building stadiums, facilities, and/or infrastructure to increase tourism in the area. This common taxing structure places substantial filing and compliance obligations on the internal tax departments of hotels. Dykema state and local tax (SALT) attorneys can help navigate these issues in an efficient and cost-effective manner.

Following is a summary of a few current state and local tax issues affecting hotel operators and how our experienced attorneys can assist with the resolution of these issues.

Sales and Use Tax

Hotels buy a considerable amount of items: computers, software, software maintenance, real property services, food, cable TV, internet access, bedding, furniture, amenities, towels, and many other items. The sales and use tax implications on these purchases are significant.

Hotel Amenities

Some states allow an exemption from tax on items that are purchased for resale. The purpose of the exemption is to prevent tiered or double taxation on the same good or service. The exemption implements the public policy that a consumption tax (i.e., sales tax) should be imposed on the ultimate consumer.

Depending on the jurisdiction, hotels may be able to buy certain items tax-free using this sale for resale exemption. For example, the Texas 3rd Court of Appeals held (2013) that a hotel was due a refund for sales tax paid on certain consumable amenities (e.g., shampoo, soap, pens and notepads) that were transferred to its hotel guests. The items were considered “resold” because the hotel guests paid consideration for the amenities as part of the total room occupancy charge. The Texas Comptroller now acknowledges that hotels are exempt on their purchases of amenities, but now takes the position that hotels must charge their guests sales tax on the value of the amenities. That is, hotels must charge sales tax on the “resale” of the amenities. The Comptroller’s position is arguably unsupported by statute and currently in dispute.

As this issue plays out in Texas and other jurisdictions, Dykema can provide tremendous value to hotels by developing strategies, analyzing risks, monitoring case law, counseling and advising hotels about tax issues, and taking action to resolve disputes with taxing authorities.

Software, Maintenance, and Software as a Service

Advances in technology have greatly impacted the hotel industry. Guests use the internet and smartphones to book rooms, make payments, review properties, and monitor reward points. As a result, the hotel industry has

invested a tremendous amount of money in the hardware and software needed to interact with its customers in a web-friendly environment. This changing technology has correspondingly led to ambiguity with respect to state taxes. If a hotel’s software is stored on a server in one state, but the software is used to book rooms at a hotel in another state, which state can or will impose use tax on the cost of the software? Is there an allocation of the cost/tax based on multi-state use? What if the software is hosted in a cloud environment by an

unrelated third party? What if the hotel doesn’t purchase software at all, but a service resulting from the use of the software? Hotels routinely face these questions—and many more.



Dykema SALT attorneys can help hotels navigate and resolve issues by providing information, identifying risk, defending hotels under audit, negotiating settlements, and litigating significant issues, if necessary.

Dykema SALT attorneys have the specific knowledge and experience needed to help hotel clients address these questions in the context of multistate operations. Beyond that, Dykema attorneys can help hotel clients build and implement a strategy for resolving tax-related issues with various state tax departments.

Hotel Occupancy Tax

As previously mentioned, hotel operators in many jurisdictions are required to collect and remit taxes from guests based on charges for room occupancy. Unlike sales tax, local hotel taxes are often collected directly by the cities and counties imposing the taxes. Hotels then are confronted with the challenge of reporting hotel receipts and taxes to multiple jurisdictions for the same tax type and the same period.

Audits

Local taxing jurisdictions often have audit and review powers. As a result, hotels often deal with both state and local government audits. This can become an even more rigorous burden when jurisdictions hire third-party audit firms to conduct the audits. Each of these audits may involve different audit plans and policies making it extremely difficult for hotels to streamline their recordkeeping and reporting practices. Dykema SALT attorneys can help identify and implement recordkeeping procedures to mitigate these audit risks.

Exemptions

While the hotel occupancy tax may seem straightforward in terms of applicability, the recordkeeping and reporting requirements necessary to comply with the tax are often quite complex. There are three main exemptions for the hotel tax: 1) permanent residents; 2) government employees traveling on official business; and 3) certain non-profit employees or volunteers traveling on behalf of the charity. Jurisdictions differ on the type of information hotels are required to maintain in order to support these exemptions. Most states require that guests fill out an exemption certificate. Beyond that, states differ on the

type(s) of supporting documentation that must accompany the certificate. Must the government or exempt entity pay the hotel directly for the room? Is the permanent resident exemption based on the person paying the bill or the person actually occupying the room? If the guest is a volunteer (not an employee) what information is needed to prove that the stay related to official charitable business? These issues are critical because auditors will often focus directly on these transactions. Through audit sampling, a few mistakes can significantly increase a proposed audit liability.

Dykema SALT attorneys can help hotels navigate and resolve these issues by providing information, identifying risk, defending hotels under audit, negotiating settlements, and litigating significant issues, if necessary.

Online Booking Companies

Recently, there has been litigation involving the hotel tax responsibilities of online booking companies. One of the main questions is whether online booking companies are renting rooms or simply providing a service to hotels. This leads to another question regarding the amount upon which the hotel tax is based. Is the hotel tax based on the net amount received by the hotel or the gross amount the online booking

company charges the guest? The answers to these questions may vary depending on the jurisdiction. Many of these questions remain unanswered as litigation is ongoing in multiple states. The impact of these issues on hotel operators cannot be overstated.

Dykema SALT attorneys can keep hotels informed about the progress and ramifications of ongoing litigation in applicable states. Moreover, Dykema SALT attorneys are available to draft and review contract language, negotiate terms, interact with state tax administrators, and resolve conflicts, if any.



Dykema attorneys can help hotel clients build a strategy for resolving tax-related issues and then implement that strategy with various state tax departments.

Property Tax

Dykema provides property tax advice and counsel to hotel clients who own or lease their real and personal property. With a fully mobile work force and attorneys licensed in multiple jurisdictions—operating from 12 offices located in California, Illinois, Michigan, Minnesota, Texas and Washington, D.C.—we assist our hotel clients with their property tax issues across the country. Our lawyers are experienced in filing property tax appeals in all available forums, including state treasury departments, tax tribunals and other state and local courts and agencies with a very strong track record of successful outcomes.

We offer our property tax assessment appeal services to clients on either a contingent fee arrangement or a competitive hourly rate basis depending on the situation of the client, the merits of the case and the client's desires. Our reputation for competence and our credentials in tax appeal work are well known—as is our success in obtaining tax refunds and reductions and delivering value to our clients.

Audits & Compliance

Hotel operators face a challenging audit and compliance environment. It is especially difficult for operators with hotel properties in multiple jurisdictions. The number of governmental departments and subdivisions that these hotels touch, on tax issues alone, can be overwhelming. Each of these state and local governmental agencies may employ audit policies and procedures that impose different recordkeeping responsibilities. Even when the recordkeeping requirements are only slightly different from one jurisdiction to another, the most sophisticated hotel operators can run into problems.

One example involves the requirement by certain jurisdictions that hotel operators provide credit card numbers to verify payment by exempt entities. This is a significant problem because hotels are not allowed to keep or divulge certain credit card information in order to comply with Payment Card Industry (PCI) Security Standards. The PCI Security Standards Council has published requirements limiting the type of credit and/or debit card information a hotel may keep and where that information may be stored. In some instances, the PCI requirements may be in direct conflict with an auditor's record requests.

Dykema SALT attorneys have dealt with these issues across multiple states and local jurisdictions, and are therefore uniquely qualified to help hotel operators meet these challenges. Specifically, our SALT attorneys can interface with government auditors on all levels, negotiate alternative transactional proof, facilitate informal settlements, and protest unfair audits.



Kelly Bagnall
Director, Hospitality &
Gaming Industry Group
Dallas, Texas
214-462-6426
kbagnall@dykema.com



Drew McEwen
Austin, Texas
512-494-4078
name@dykema.com



Kevin Oldham
Austin, Texas
512-494-4155
koldham@dykema.com



Carl Rashid, Jr.
Detroit, Michigan
313-568-5422
crashid@dykema.com



Mary Hennessey
Detroit, Michigan
313-568-5310
mhennessey@dykema.com