

Law Offices of John A. Strain

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*CERTIFIED SPECIALIST TAXATION LAW
CALIFORNIA BOARD OF LEGAL SPECIALIZATION

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September 13, 2017

By Email

City of Manhattan Beach
City Council
1400 Highland Avenue
Manhattan Beach, California 90266

Re: Shade Hotel Transient Occupancy Tax

Dear Council Members:

The agenda for the September 19 Council meeting includes an appeal by Shade Hotel from a determination of the Director of Finance related to the application of the City's TOT tax to Shade Hotel. That determination is summarized in a letter from Bruce Moe to Michael Zislis dated December 8, 2016 (a copy of which is enclosed with this letter).

That determination relates primarily to "no show" fees and "cancellation" fees — in other words, to amounts charged and collected from customers who did not in fact occupy a room at the Hotel. Referring to the applicable Municipal Code terms (i.e., the definitions in Section 8.20.010(e)), the Director concludes that these fees are "rent" for the "right to use or possess" the rooms.

We believe those Municipal Code terms clearly compel the opposite conclusion. The main question is whether these fees are charged for "the right to actual use or possession." The Director's determination did not mention the key word. An individual who makes a reservation does not thereby obtain a right to "actual" use or possession. That right is granted when the guest completes the registration process at the time of check in. For example, at that time there is the possibility that the room might be unavailable for one reason or another. Although the Hotel would always take steps to be sure its customer is satisfied, those steps would not involve any right to "actual" use or possession of the unavailable room.

Shade Hotel has 38 guest rooms and is generally fully occupied. The City is taking the position — we believe unreasonably — that a cancellation or no-show would entitle the City to receive TOT tax with respect to more than 38 rooms.

At the very least, these Municipal Code terms are vague. Simple fairness says that the Hotel should not be obligated to pay over a tax amount where it could not reasonably have determined that such tax should be collected. A vague tax is also an unconstitutional tax.

Moreover, the City lacks the legal authority to impose a tax on anyone who has no "nexus" with the City. Consider, for example, a resident of New York (or London) who makes

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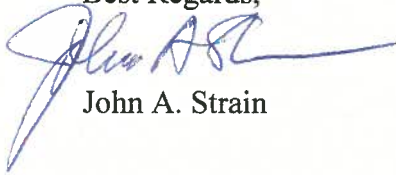
City of Manhattan Beach
City Council
September 13, 2017
Page 2 of 2

plans to visit Manhattan Beach and then needs to cancel his trip. Clearly, there is no tax "nexus" allowing the City of Manhattan Beach to impose a tax on that individual. The word "actual" in the Municipal Code was apparently inserted due to the constitutional limitation. It is not proper for the City to put the Hotel in the position of trying to collect a tax, on behalf of the City, that the City is not entitled to collect itself.

The audit and ruling also raises issues regarding other charges, such as "pet fees." The Director concludes that, regardless of how Shade Hotel applies such payments (in that case, for necessary cleaning charges), the payment is still made for the right to use or occupy the room. We are frankly rather mystified by that conclusion. Specific charges for things like cleaning or breakage are imposed for exactly those specified reasons. They are not kennel occupancy fees (and TOT tax does not apply to kennel fees). The City's assertion that these are for the right of use or occupancy of a room doesn't change the actual character of such charges.

It is our understanding that the scheduled Council meeting is our final appeal right at the City and that any further challenge will require the Hotel to pay the disputed amount and then sue for a refund. In the event of an adverse ruling, please confirm that our understanding of the procedure is correct.

Best Regards,



John A. Strain

Encl.

Copy (w/encl.): Mr. Bruce Moe (by hand delivery)
Mr. Michael A. Zislis (by email)
Ms. Shaunna Hatcher (by email)



TOT

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December 8, 2016

Mr. Michael Zislis
The Zislis Group
321 12th St Suite 112
Manhattan Beach, CA 90266

Re: Shade Transient Occupancy Tax Hearing
Notice of Taxes Due: \$22,597.46

Dear Mike:

Thank you for meeting us to discuss the transient occupancy tax (TOT) audit results for Shade Hotel. It was helpful to understanding your perspective of the application of the tax as it relates to ancillary rents collected by the hotel.

You have informed us that hotel management was unaware and did not believe that TOT applies to: cancellation and no-show fees, room upgrade fees, early and late departure fees, and pet fees. Based on this belief, Shade did not collect TOT for those charges. Shade further believes that the City has not made it clear what charges are subject to TOT. Finally, Shade believes that because the taxes were not collected, they should not be liable for the taxes due to the City.

After our meeting, I reviewed several documents, including the City's hotel tax ordinance and the audit results for all hotels and motels in Manhattan Beach. I found the following information useful:

- 5 of the 12 hotels audited were found to have no deficiencies, meaning TOT was collected appropriately for all fees, including pet fees, cancellation and no show fees
- 7 hotels with deficiencies underreported taxes of between \$99.70 to \$22,597.46
- 8 of 12 hotels reported pet fees for TOT purposes as required
- 10 of 12 hotels collected TOT on no-shows
- Of the 7 with deficiencies, 6 have complied with the audit findings and remitted TOT

This information indicates that while there may be some misperceptions on the application of the TOT by hotels, it is not universal, particularly with five hotels reporting TOT completely accurately, while most others had only minor underreporting errors. Nonetheless, the City will accept your suggestion of clarifying the charges subject to TOT in an effort to assist the hoteliers' collection and reporting. The audit process itself has assisted in awareness as well.

In reviewing the City's TOT ordinance, I paid special attention to the definitions which indicate those charges for which the TOT is to be collected. The following further reinforces collecting the tax on these charges:

Cancellation and No-Show Charges

With regard to cancellation and no show charges collected by the hotel, the City's TOT Ordinance (Section 8.20.010 (e)) includes definitions of "rent" and "occupancy" that state the following:

"Rent" shall mean the consideration charged, whether or not received (emphasis added), for the occupancy of space in a hotel valued in money, whether to be received in money, goods, labor, or otherwise, including all receipts, cash, credits, property, and services of any kind or nature, without any deduction therefrom whatsoever."

The code also states that *"'Occupancy' shall mean the actual use or possession, or the right to actual use or possession, (emphasis added) of any room, or portion thereof, in any hotel for dwelling, lodging or sleeping purposes by the same individual or individuals for a consecutive period of thirty (30) days or less."*

The cancellation and no-show charges being contested are a form of rent for which the guests, while they did not physically occupy the space, had acquired the right to use or possess the rooms by virtue of the reservation with the hotel. Rents (cancellation and no-show fees) were collected on those rooms. Therefore, the TOT should have been collected by Shade.

Pet Fees

I am aware that Shade's position on this charge is that it is a cleaning fee not subject to the TOT. However, regardless of Shade's application of that revenue for that specified purpose, this is a mandatory charge for the privilege of occupancy. As such, it is subject to TOT.

The auditor noted that pet fees were reported appropriately in years 2012-2014, but were not reported for the period of January 1, 2015 to December 9, 2015. Then, for the period of December 10 to December 31, 2015, TOT on pet fees was collected (this coincided with a change of accounting systems by Shade, which appears to have resulted in the appropriate collection in the categories of room upgrade, early departure and pet fees). This would seem to indicate an understanding that TOT applies to pet fees, but that perhaps the accounting systems were not adequately identifying the taxability of certain rents.

Page 3 of 3

Other areas for which TOT was not collected on rents received include room upgrade fees, early departure fees, and late departure fees. Again, these are mandatory charges for the privilege of occupancy. These are clearly rents as defined in the Municipal Code for which TOT should have been collected.

I understand Shade's position is that this is not a case of Shade collecting the taxes and failing to remit to the City; Shade simply did not believe the TOT applied to these charges, and therefore did not collect the TOT. However, regardless of the reasons for non-collection, the taxes are within the definitions of the Municipal Code and should have been collected. As a result, as the Tax Administrator for the City of Manhattan Beach, I have determined that the taxes are due and payable to the City by Shade Hotel. Those taxes total \$22,597.46. **Please remit payment to the City no later than December 27, 2016.**

If you wish to appeal my decision, you may do so as prescribed in the Municipal Code (below):

8.20.090 - Appeals.

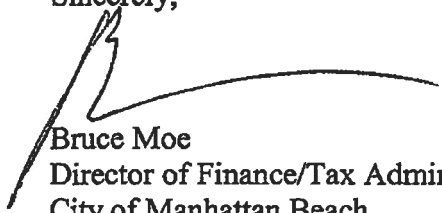
Any operator aggrieved by any decision of the Tax Administrator with respect to the amount of such tax, interest, and penalties, if any, may appeal to the Council by filing a notice of appeal with the City Clerk within fifteen (15) days after the service or mailing of the determination of the tax due. The Council shall fix a time and place for hearing such appeal, and the City Clerk shall give notice in writing to such operator at his last known place of address. The findings of the Council shall be final and conclusive and shall be served upon the appellant in the manner prescribed in this chapter for the service of the notice of hearing. Any amount found to be due shall immediately become due and payable upon the service of the notice.

The full the City's Uniform Hotel/Motel Occupancy Tax Code (Chapter 8.20) is available online at:

https://www.municode.com/library/ca/manhattan_beach/codes/code_of_ordinances?nodeId=TIT8FIRETA

Please don't hesitate to contact me if you have questions.

Sincerely,



Bruce Moe
Director of Finance/Tax Administrator
City of Manhattan Beach

cc: City Manager Danaj
City Attorney Barrow
City Clerk Tamura
Revenue Services Manager Charelian