GROUPON AND EXPEDIA: A COMPARISON OF TWO MODERN ONLINE TRENDS CREATING A PARALLEL TAX INQUIRY

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"Simplicity in modern taxation is a problem of basic architectural design. Present legislation is insufferably complicated and nearly unintelligible. If it is not simplified, half of the population may have to become tax lawyers and tax accountants."

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I. INTRODUCTION

Americans are surf-and-spenders. In 2011, we spent more than 200 billion dollars on online shopping, or, as the pastime is often phrased, shopping while surfing (the web). There is no denying that American shoppers have welcomed the online purchasing arena. Gone are the days of spending hours in store dressing rooms, trying on each item of clothing. No longer do we smell each candle in the aisle before choosing the best scent or examine each banana in order to find the ripest batch. Forgotten are the days of cutting coupons from the Sunday newspaper and of speaking with a hotel agent on the telephone to reserve a room.

Granted, that may be a bit theatrical. As to the latter two, though, the coupon-cutting and telephone-reserving have been largely replaced with the recent trends of Groupon, Inc. (“Groupon”) and Expedia, Inc. (“Expedia”). Groupon, featuring “daily deals” on prized items at discounted prices, and Expedia, offering one-stop travel booking, are both accessible with the click of your cursor. While undeniably convenient in their ease of access through the internet portal, these two online companies present a novel tax question: When a Groupon or Expedia purchase is made, should sales and hotel taxes, respectively, be remitted based on the full value of the item or service sold or, rather, the lower, discounted value? Stated in tax jargon, what is the appropriate tax base when calculating the Groupon sales tax and the Expedia hotel tax—the full or lower, discounted value?

When determining the proper tax base, the Groupon tax consideration asks whether the customer, when redeeming her Groupon for the item or service sold, should pay sales tax to the merchant based on the discounted amount she paid to Groupon or rather, the higher, full value of the item or service. In merely a varied application of the same tax inquiry, the Expedia consideration asks whether Expedia should remit hotel taxes to the hotel based on the discounted room rate.

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that Expedia negotiated with and paid to the hotel or instead, the higher, marked-up retail room rate paid by the customer to Expedia.⁶

Alongside setting forth a parallel tax question, the majority of regulatory and judicial bodies considering the Groupon and Expedia inquiries have rightfully determined that the appropriate tax base should comprise the lower applicable value. Regarding Groupon and other comparable daily-deal companies (“DDC(s)”), sales tax treatment of their daily-deal coupons is divided among the states, with a slight majority imposing sales tax based on the discounted value of the item or service sold.⁷ Likewise, as for Expedia and other online travel companies (“OTC(s)”), the majority approach is similar to Groupon’s, with several courts holding that Expedia and other OTCs must remit hotel taxes based only on the discounted room rate⁸ (yet, the majority approach leans less toward favoring taxation based on the discounted value when considering the increasing number of out-of-court settlements and the rise in legislative amendments, all imposing taxation based on the higher, retail room rate).⁹

This paper examines the tax treatment of Groupon and similar DDCs, as well as the tax treatment of Expedia and other comparable OTCs. Despite identifying certain differences between the tax controversies surrounding Groupon and Expedia, this article argues that the underlying controversies confronting both companies ultimately pose different versions of the same legal question: To what tax base do the applicable taxes apply—the discounted or higher, full value of the item or service sold? While a uniform treatment of this question is noticeably absent, the majority tax approach within both entities is the same—taxing the lower applicable amount. This paper contends that such an outcome reflects the proper normative treatment—in both situations the same legal question applies and, although based on differ-

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⁸ See Joseph Henchman, Taxation of Online Travel Services: Lawsuits Generally Not Succeeding In Effort to Expand Hotel Taxes to Online Travel Services, Tax Found. 1, 3 (May 2012), http://taxfoundation.org/sites/taxfoundation.org/files/docs/sr198_travel.pdf.

ent statutory regimes, the same answer should also apply: taxes should be calculated based on the lower tax base.

Part II of this paper discusses Groupon. It explains how Groupon operates, the tax question resulting from these operations, the varying regulatory approaches to answering this tax question, and the approach applied by a significant number of jurisdictions. Likewise, Part III discusses the same issues as they relate to Expedia. Parts II and III conclude with a discussion of the preferred lower tax base, supported by statutory interpretation and economic considerations. Finally, the paper concludes in Part IV.

II. Groupon

A. What is Groupon?

Founded in 2008, Groupon is among several “internet-based ‘deal-of-the-day’ discount coupon programs,” noted as being the “biggest and most widely subscribed to” along with LivingSocial.10 Through its website, Groupon offers “heavily discounted vouchers (or Groupons) on behalf of local vendors.”11 Groupons come in the form of many products and services, including food, dance lessons, scuba-diving lessons, and Lasik eye surgery.12 Similar business models have emerged and it is perhaps unsurprising that Facebook is reported to be “launching a similar program in key test markets.”13 Indeed, a May 2011 study conducted by Shop.org, a section of the National Retail Federation, found that 82% of online consumers are aware of websites like Groupon, LivingSocial, and Gilt City.14 Named by Forbes.com as one of the “fastest growing companies in Web history,”15 in 2011, Groupon sold

10 About Us, supra note 4; Sylvia F. Dion, State Tax Issues to Consider With ‘Groupons’ and Other Third-Party ‘Deal-of-the-Day’ Programs, BNA TAX MGMT. WKLY. ST. TAX REP., Mar. 23, 2012.
12 Id.
14 Martha Kessler, Groupon Craze, Other Online Daily Deals Raise Questions About How State Sales Tax Should Be Applied to the Activity, BNA TAX MGMT. WKLY. ST. TAX REP., Nov. 4, 2011.
1.62 billion dollars in these online coupons.\textsuperscript{16} With sales in the billions, it is unsurprising that states have focused their attention on Groupon and similar companies concerning how these online coupons are taxed.\textsuperscript{17} However, before considering the different ways in which sales tax can be applied to a Groupon item or service, it is first necessary to understand the mechanics of a Groupon sale.

A deal-of-the-day or “daily deal voucher” is defined as “a coupon purchased by a consumer from a third-party operator that is then redeemed for food, goods, or services at a reduced price at specific businesses.”\textsuperscript{18} When a daily deal voucher purchase is made, three parties interact: the customer who purchases the daily deal voucher (e.g., Buyer Bruce); the company that sells the daily deal voucher (e.g., Groupon); and the merchant that accepts the voucher (e.g., ABC Carwash).\textsuperscript{19}

The transaction among these three parties occurs in the following way: First, subscribers to Groupon receive a “‘Daily Deal’ e-mail” which describes the discounted products and services offered, oftentimes located in the subscriber’s local area.\textsuperscript{20} As Groupon proclaims, these deals are for “the best stuff to do, see, eat, and buy in 48 countries, and soon beyond.”\textsuperscript{21} Interested subscribers must act quickly, as Groupon specifies a limited time to buy the deal, oftentimes “only a few hours or days.”\textsuperscript{22} Second, once the minimum number of subscribers buys the offer, “the deal becomes effective, or as Groupon says, ‘the deal is on.’”\textsuperscript{23} Third, after buyers remit payment to Groupon using their credit card, Groupon sends them an electronic “voucher.”\textsuperscript{24} Finally, the customer may redeem their item by giving the “voucher” to the merchant “as a printed certificate or virtual mobile device coupon.”\textsuperscript{25}

\textsuperscript{16} Groupon is a Headache for State Tax Administrators, CITIZENS FOR TAX JUST. (Apr. 2, 2012, 2:00 PM), http://www.ctj.org/taxjusticedigest/archive/2012/04/groupon_is_a_headache_for_stat.php.
\textsuperscript{17} See id.; Dion, supra note 15.
\textsuperscript{18} Grace, supra note 7.
\textsuperscript{19} See id. at pt. I.
\textsuperscript{21} About Us, supra note 4.
\textsuperscript{22} Dion, supra note 10.
\textsuperscript{23} Id.
\textsuperscript{24} Id.
\textsuperscript{25} Id.
Once the initial online sale of the daily deal is complete and the buyer’s payment is processed, Groupon pays the agreed-upon percentage of the payment to the merchant.26 The percentage split varies among merchants’ contracts, but oftentimes, the customer’s payment is divided evenly between Groupon and the merchant, each receiving 50%.27 For example, considering Buyer Bruce mentioned previously, imagine that a full-service carwash is worth $40 at ABC Carwash. If ABC Carwash contracts with Groupon to offer a daily voucher of $20 for the service, an agreed-upon 50-50 split would necessitate Groupon and the carwash each receiving $10 upon the sale. Thus, ABC Carwash has received $10 for a sale worth $40, amounting to a $30 loss.28 Despite this loss, merchants like ABC Carwash continue to contract with Groupon, as such losses are outweighed by the “primary benefit” of “the potential to increase the merchant’s customer base and create repeat customers.”29 As one commentator noted favorably of the transaction, “The consumer gets 50 to 80 percent off, the merchant gets exposure and a guaranteed number of new customers, and Groupon collects 50 percent of the money earned.”30

While these stages of a Groupon sale can be fairly described as uncontroversial, one aspect of the process has generated much inquiry, forming the basis for this paper. Concerning the applicable sales tax for each item or service sold in the form of a daily deal, notably, Groupon does not charge sales tax upon the online purchase of these daily vouchers.31 Rather, Groupon requires merchants to assume responsibility for such taxes when a Groupon is redeemed.32 Indeed, “Groupon’s Merchant Account Terms and Conditions Agreement requires merchants to acknowledge that they are registered for sales tax collection purposes and will be responsible for collecting and remitting all applicable taxes.”33 When considering the effects of this requirement, one commentator states:

Groupon puts the onus of incredibly complex issues like taxation . . . on the merchant. These are issues that multinationals with armies of lawyers struggle with. If you’re running a small coffee shop, restaurant or nail

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26 Id.
27 Id.
28 For a similar example, see id.
29 Id.
30 Smith, Bergstrom, Yopp & Barnett, supra note 11.
31 Dion, supra note 10.
32 Id.
33 Id. (emphasis added).
salon, you likely have no idea what any of this stuff means. Because Groupons are so new, no one really does.34

This, in turn, has resulted in the tax implications explored in the next section.

B. The Tax Base: Differing Approaches to Groupon’s Situation

1. Resulting Tax Question

Flowing from Groupon’s requirement that merchants assume tax responsibility inevitably creates the conundrum of determining exactly what that sales tax is and how to calculate it. Returning to Buyer Bruce, consider the hypothetical outlined above: Buyer Bruce purchases for $20 a daily deal on Groupon for a full-service carwash at ABC Carwash. The full value of the carwash is worth $40. After ordering the full-service carwash at ABC Carwash, the total amount of the bill is $40. Bruce pays the bill by giving his Groupon to the cashier. Upon redeeming his Groupon, one of three things can occur regarding the collection of the applicable sales tax: (1) ABC Carwash will not collect sales tax from Bruce; (2) ABC Carwash will require Bruce to pay sales tax in cash; or (3) ABC Carwash will allow Bruce to use his daily deal for the total amount owed for the carwash, including the sales tax.35 Likewise, if ABC Carwash collects sales tax from Bruce, one of two things can occur regarding the calculation of the applicable sales tax: (1) ABC Carwash will calculate the sales tax based on $20, the discounted price that Bruce actually paid for the daily deal; or (2) ABC Carwash will calculate sales taxed based on $40, the full, undiscounted price of the service purchased.36

For some, these options may appear to set forth little, if any, meaningful difference. In other words, who cares, you ask. For several interested parties, the decision made by ABC Carwash, and all other participating merchants of Groupon, of whether and how much sales tax to collect from Groupon users, has significant effects.37 For

36 See Novack, supra note 5; Blair, supra note 35.
merchants, “[t]he ’stakes are high.’” If the merchant charges excessive sales tax on the Groupon purchase, there is the potential for class action lawsuits filed by angered customers. Indeed, a merchant who “collects tax when none was due” is said to have “over-collected” and is “at risk” of being subject to these lawsuits or even, “violating consumer protection laws.” Conversely, if a merchant does not collect enough sales tax on the Groupon purchase, “the retailer can be liable for sales tax, interest, and penalties.”

For states, there are significant effects in the form of lost revenue. “[S]tates are recognizing the potential for lost revenue because the existing rules on the impact of discounts on sales price could greatly diminish the sales tax base.” For Groupon and similar DDCs, the appeal of the daily-deal industry may decline if consumers are forced to pay sales tax on the full value of the Groupon item or service. As a result, for consumers, with the average local sales tax rate levying at 9.6% nationwide, it is clear that their pockets are directly affected by the decision. As the next section discusses, among those states that have offered formal guidance on the matter, the approach varies state-to-state, an outcome that may ultimately raise more questions than answers for these affected parties.

2. Varied Tax Treatment

Conflicting; contrary; erratic; incoherent; incompatible; irreconcilable; uncertain; unpredictable; unstable. These are just some of

58 Id.
60 Roll & Boeckel, supra note 37.
61 Id. See, e.g., Retail Sales Tax, WASH. ST. DEP’T OF REVENUE, http://dor.wa.gov/content/findtaxesandrates/retailsalestax/ (“The seller is liable to the Department of Revenue for sales tax, whether or not it is collected.”) (last visited Nov. 18, 2012).
62 Dion, supra note 10.
63 Id.
64 Novack, supra note 39.
66 See Novack, supra note 39.
67 See, e.g., Grace, supra note 7, at pt. IV; Dion, supra note 10; Roll & Boeckel, supra note 37.
the synonyms for “inconsistent”—a term that best summarizes the recent, yet minimal, state guidance instructing merchants on how sales tax should be applied to Groupon purchases. Considering this issue during a session of the ABA Section of Taxation meeting on May 11, 2012, one speaker reflected, “We’re in a definite gray area . . . with a lot of uncertainty.” Likewise, a former state tax official stated of the issue, “It is a bit of a mess, but that is true of a lot of breaking issues . . . there will be a period of time when retailers are in a difficult position.” To color the area greyer, because the question is so recent, only ten states have offered formal guidance on the matter. To affirm such uncertainty even further, it is notable that twenty-four states comprising the Streamlined Sales Tax Governing Board have attempted to reach an agreement on a uniform tax treatment of Groupon sales. However, this effort failed on May 24, 2012 “when the measure was narrowly defeated by a small group of states already administering different tax treatment schemes.”

While a uniform tax treatment among the states has so far proven elusive, the options are clear: of those states offering guidance on this issue, there are “two camps”: first, “those that impose tax on the full sales price,” and second, “those that impose tax on the discounted sales

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49 Id.
51 Kessler, supra note 14.
52 To configure this number, three recent sources on the issue were considered. Two of these sources confirmed that the following seven states have offered formal guidance: California, Illinois, Iowa, Kentucky, Maine, Massachusetts, New York. The remaining differences in the sources’ findings are indicated after each citation. See Steven Roll & Deborah Swann, In Search of New Revenue, States Eye New Types of Transactions and Funding Sources, BNA TAX MGMT. WKLY. ST. TAX REP., May 18, 2012 (concluding that nine states have issued formal guidance; includes Kansas and Texas where the latter source does not; does not include Mississippi where the latter source does). See also Grace, supra note 7, at pt. IV (concluding that eight states have issued formal guidance; includes Mississippi where the former source does not; does not include Kansas or Texas where the former source does). It is noted later in this paper that it is unclear whether Texas has offered formal guidance on the matter. A third source identifies Wisconsin as releasing formal guidance on the issue, making it the tenth state to do so after considering the aforementioned sources. See Discounted Certificates, Product Vouchers Not Subject to Wisconsin Sales Tax, ST. TAX TODAY, Aug. 9, 2012, available at 2012 STT 154-30.
54 Roll & Boeckel, supra note 37.
price.” Of the ten states that have offered guidance, six have instructed merchants to impose sales tax on the discounted sales price of the Groupon, narrowly claiming a majority on this issue. Consider again Buyer Bruce who purchased a $20 Groupon for a full-service wash at ABC Carwash, having a full retail value of $40. When Buyer Bruce redeems his Groupon, whether sales tax will be assessed on $20 or $40 will depend on which state ABC Carwash is located in.


57 See Blair, supra note 35.
If ABC Carwash is located in California, Illinois, Kentucky, Maine, Massachusetts, or Wisconsin ("the discounted value states"), Buyer Bruce will owe taxes based on $20, the discounted amount he paid for the daily deal. Of the guidance offered by these six states, Kentucky is claimed to "provide[ ] the best rationale for why it taxes only the amount paid for the daily deal voucher." The December 2011 edition of "Kentucky Sales Tax Facts" states:

> When a consumer redeems the voucher at the local business for a taxable product, the tax is due on the total price the customer paid for the voucher rather


64 Grace, supra note 7, at pt. IV(A). This article does not consider Wisconsin.
than the total value of the voucher . . . [because] the portion of the
purchase price of the voucher retained by the online company is consid-
ered an expense of the seller and part of gross receipts as provided in
[the Kentucky Revised Statutes].

In other words, Kentucky’s tax base includes “the amount retained by
(or paid to) the daily deal voucher operator.” Thus, at a Kentucky
ABC Carwash, the tax base is $20. Likewise, Illinois’ General Letter
Ruling can be read to apply the same rationale that “the tax base
should include all expenses of the retailer.”

While this guidance is seemingly direct, Buyer Bruce is not certain
to owe taxes based only on the $20 in these six states, as some have
twists to their general approach. For example, in Kentucky, Buyer
Bruce will owe taxes based on the discounted value of $20 only if:
(1) “the voucher indicates the discounted price” ($20); or (2) ABC
Carwash “know[s] and retain[s] documentation of the discounted
price.” If one of these two requirements does not occur, Buyer Bruce
will owe sales tax “on the total face value of the voucher,” the $40.
However, this rarely occurs, as “merchants who enter into a contract
with Groupon . . . are involved in establishing the specifics of the deal
offer and likely would be aware of and have retained documentation of
the discounted sales price.” Likewise, Illinois imposes a similar
knowledge requirement, stating that if the merchant knows how much
the customer paid for the Groupon, then the discounted amount is

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65 Id. (emphasis added); see also Kentucky Sales Tax Facts, supra note 60.
66 Grace, supra note 7, at pt. IV(A).
67 Id. (identifying the Illinois guidance as a “Private Letter Ruling”). However, the
State identifies the letter as a General Information Letter, which influences the legal
effect of the document, as stated above. See Ill. Gen. Information Ltr. ST 12-0009-GIL,
supra note 59 (stating that a General Information Letter “is not a statement of Depart-
ment policy and is not binding on the Department”). For clarification of the “all ex-
enses” language in the text, consider the following: “In responding to the taxpayer’s
inquiry of how to tax the use of daily deal vouchers, Illinois first states that its sales tax is
imposed on the gross receipts from sales of tangible personal property made in the
course of business. The letter goes on to define gross receipts as ‘the total selling price
. . . [defined as] the consideration for a sale valued in money whether received in
money or otherwise, including cash, credits, property . . . and shall be determined with-
out any deduction on account of the cost of the property sold, the cost of materials
used, labor or service cost or any other expense whatsoever.’” Grace, supra note 7, at pt.
IV(A).
68 See Dion, supra note 10 (citing the Kentucky revenue publication); Kentucky Sales
Tax Facts, supra note 60.
69 Dion, supra note 10; see Kentucky Sales Tax Facts, supra note 60.
70 Dion, supra note 10.
taxable.\footnote{Id; Blair, supra note 35 (citing Ill. Gen. Information Ltr. ST 12-0009-GIL, supra note 59); see also Sylvia F. Dion, Groupons, Sales Tax and More – The Issues Continue, The St. and Local Tax “Buzz” (Mar. 27, 2012), http://www.thestateandlocaltaxbuzz.com/2012/03/groupons-sales-tax-and-more-issues.html.} Otherwise, taxes are owed on the undiscounted full value.\footnote{Blair, supra note 35 (citing Ill. Gen. Information Ltr. ST 12-0009-GIL, supra note 59).} These requirements rarely have meaningful effects, though, as the purchase price is usually listed on the voucher.\footnote{Novack, supra note 39.}

Another twist to the discounted value states, set by California, provides that upon redemption of a daily deal voucher, “the retailers’ gross receipts subject to tax include the consideration paid by the customer for the [daily deal voucher] plus any additional cash, credit, or other consideration paid to the retailer when the product is purchased with the exception of sales tax.”\footnote{Special Notice: Application of California Sales Tax to Deal-of-the-Day Instruments, supra note 58 (emphasis added).} To illustrate the effect of California’s twist on the general rule, consider the following example:

[A] $50 deal-of-the-day is offered for $105 worth of custom picture framing. The customer redeems the coupon for a custom frame priced at $120 (i.e., the customer owes an additional $15 since the voucher only covers up to $105 worth of framing).\footnote{Dion, supra note 10 (citing a September 2011 Tax Information Bulletin). See Tax Information Bulletin, Publication No. 388, CAL. ST. BD. OF EQUALIZATION (Sept. 2011), http://www.boe.ca.gov/news/pdf/sep11TIB.pdf.}

Applying California’s guidance, “sales tax is due on $65—the $50 the customer paid for the voucher plus the additional $15.”\footnote{Dion, supra note 10; see Tax Information Bulletin, Publication No. 388, supra note 75.} Imagine that you are a single-owner frame shop in a state like Kentucky, Illinois or California—would the marketing advantage of selling your products on Groupon be worth having to understand and follow these tax requirements? Granted, the simpler alternative would tax the entire price or not tax the $15 at all—neither of which are preferable to a lower tax base, which comes, of course, with complexities like those in California.
Now, assume ABC Carwash relocates. If ABC Carwash operates in Kansas, Mississippi or Iowa ("the full value states"), the same Buyer Bruce will owe taxes based on $40, the full value of the item or service purchased. In Iowa, however, if the voucher states "its face the price paid by the purchaser," sales tax is owed only on the discounted value.80 Because "most vouchers do list the purchase price on the voucher," the discounted price will most likely be taxed.81 Iowa’s guidance simply reverses the construct of Kentucky’s—where Kentucky’s general rule taxes the discounted value, but only if the voucher states the discounted price or the merchant has knowledge and documentation of such price, Iowa’s general rule taxes the full value unless the voucher states the discounted price.82

Finally, if ABC Carwash is located in New York, noted as being "the most schizophrenic of all the states" in its application, Buyer Bruce may owe taxes on $20 or $40. If Buyer Bruce’s voucher is for a "specific service or product," he will be taxed based on the $20, the amount he paid for the voucher.85 However, if the voucher "has a stated face value," he will be taxed based on the $40, the undiscounted sales price.86 Confused yet? In a memorandum from the New York

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80 Dion, supra note 10 (citing Groupons – Iowa Sales Tax, supra note 79).
81 Grace, supra note 7, at pt. IV(2). As a result of the ultimate application of the Iowa rule, several articles have mistakenly included Iowa with those states that, as a general matter, assess taxes based on the discounted value of the voucher. See, e.g., Roll & Boeckel, supra note 37; Roll & Swann, supra note 52.
82 See Dion, supra note 10.
84 Grace, supra note 7, at pt. IV(2).
85 See id.
86 See id.
Department of Taxation and Finance, the terms “specific product or service voucher” and “stated face value voucher” are defined, albeit unconvincingly. Unlike Kentucky, Illinois and California, where the general rule is followed by a series of twists in New York the general rule is a twist in and of itself.

C. The Best Tax Approach

Before considering which state’s tax treatment of Buyer Bruce is most preferable, it is important to note that states’ consideration of the Groupon issue is not limited to these ten states. In addition to those ten states that have offered formal guidance regarding the tax treatment of Groupon daily deal vouchers, a March 2012 survey from the Streamlined Sales Tax Governing Board gathered the informal guidance of several states. As states continue to wrestle with how to tax Groupon and other DDC vouchers, it is clear that a resolution is needed. Fast. In the meantime, those states having yet to issue formal guidance on the matter should fall in line behind those states comprising a majority and do the following: require merchants to assess Groupon sales tax only on the discounted value.

87 See Sales Tax Treatment Relating to the Sale and Redemption of Certain Prepaid Discount Vouchers, No. TSB-M-11(16)S, supra note 83. See also Timothy P. Noonan & Lance E. Rothenberg, Taxing Groupon-Type Coupons: New York Tax Department Guidance, ST. TAX NOTES MAG., Oct. 17, 2011, available at 62 State Tax Notes 171; Martha Kessler, New York Addresses Sales Tax of Groupon-Like Vouchers, Coupons, BNA TAX MGMT. Wkly. ST. TAX Rep., Sept. 23, 2011 (stating that a “specific product or service voucher is a voucher without a specific stated value that may be redeemed only for a specified product or service or combination of products and/or services” and that a “stated face value voucher is a voucher with a specifically stated value, and when redeemed, the value of the voucher is applied toward the price of the products or services purchased by the customer.”).

1. **Statutory Interpretation**

As set forth above, of those states offering guidance on this issue, there are “two camps”: “those that impose tax on the *full sales price*,” and “those that impose tax on the *discounted sales price.*”90 Imagine that the labels of “full” and “discounted” are removed, leaving only “sales price.” Considering this term alone, some states’ definition of “sales price” necessitates the proper tax being assessed based on the amount that the consumer paid to Groupon for the item or service.

Consider North Carolina’s General Statutes, for example. North Carolina defines “sales price” as “[t]he total amount or consideration for which tangible personal property, digital property, or services are sold, leased, or rented. The consideration may be in the form of cash, credit, property, or services.”91 Based on this definition of “sales price” alone, one can rightfully conclude that the taxable value should be the *lower* amount—the total amount paid for the item or service sold by Groupon. After all, in the example above Buyer Bruce has only given $20 consideration for the car wash. Thus, based on statutory interpretation, the discounted price is the proper value to tax.

2. **Economic Considerations**

Apart from statutory interpretation, an economic solution to the Groupon debate should focus on the *consumer*, not the states’ or Groupon’s potential revenues or even the unfortunate position of merchants due to Groupon’s delegation of tax responsibility. When Buyer Bruce purchases a carwash in the form of a Groupon for $20, he should be taxed only on the $20 that he actually paid. Bruce bought the carwash from Groupon (favorably, at a discounted price) rather than from ABC Carwash itself (for the full price)—as a result, he should not be taxed as though he bought the service for full value at ABC

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90 Covering Corporate Income Tax Nexus, supra note 55 (emphasis added).
91 For further guidance of what the term “sales price,” specifically “credit” includes, see N.C. GEN. STAT. ANN. § 105-164.3(37)(a)(b) (West 2011).
92 N.C. GEN. STAT. ANN. § 105-164.3(37) (West 2011). In support of this position, other states have statutory language similar to North Carolina. See, e.g., S.C. CODE ANN. § 12-36-130 (2000) (defining “sales price” as “the total amount for which tangible personal property is sold, without any deduction for the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses, or any other expenses.”); TENN. CODE ANN. § 67-6-102 (West 2013) (defining “sales price” as “the total amount of consideration, including cash, credit, property, and services, for which personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, without any deduction for the following . . . ”).
Carwash. As one commentator noted, “[P]aying sales tax to a vendor after already paying for the good or service in a previous transaction disconnects the purchase from the tax incident—a disconnect that will undoubtedly lead to customer complaints.” 92 Put differently, sales tax “should be paid on the amount paid by the consumer, not some subjective value that the consumer didn’t pay.” 93 Otherwise, “angry customers [will] demand[,] to know why they’re paying tax on $80 for something they only paid $40 for.” 94

Until undecided states set forth formal guidance, merchants are left to simply estimate the proper tax amount; consumers will remain confused, possibly angered depending on the tax outcome; and Groupon will rest easy, thanks to its Merchant Account Terms and Conditions Agreement 95 relinquishing it of any tax concerns. As one author so fittingly stated, “If only Groupon could arrange a coupon for 50 percent off sales tax . . . Now that would be something.” 96

III. Expedia

A. What is Expedia?

Presenting a similar tax question, Expedia, a self-proclaimed “online travel agency,” 97 has recently caught the attention of many states, courts, and legislatures. 98 Online travel companies (“OTC(s)”) such as “Expedia, Hotels.com, Orbitz, Priceline, and Travelocity” attract consumers by “aggregat[ing] information that allows travelers to sort through hotels and book a room on a central website.” 99 As a result, OTCs have created a platform for “consumers to easily compare hotels based on different criteria (including price, location, and customer ratings) and at the same time book a reservation and pay for it.” 100

92 Kranz, Freeman & Yopp, supra note 13, at pt. II(B) (emphasis added).
94 Id. See also Buhl, supra note 50 (stating that taxing the full value of the Groupon good or service would be an “aberration” and that “it makes the most sense to apply the tax to what the consumer pays the retailer.”).
95 Dion, supra note 10.
96 Kranz, Freeman & Yopp, supra note 13, at pt. II(B).
97 About Expedia.com, supra note 4.
98 See Henchman, supra note 8.
100 Id.
Alongside benefiting travelers, OTCs also benefit hotels, allowing them to “reach a market . . . that they otherwise would not reach.”\textsuperscript{101}

Introduced by Microsoft in 1996, Expedia accumulated 3.45\textit{ billion dollars} in revenue and 29.1\textit{ billion dollars} in gross bookings in 2011 alone.\textsuperscript{102} Like Groupon, with revenues this great, it is unsurprising that attention has turned to Expedia and similar OTCs regarding the tax treatment of these transactions. Likewise, before considering the different ways in which hotel taxes can be applied to an Expedia purchase, it is first necessary to understand the mechanics of each sale.

First, consider the consumer who books a room \textit{directly} from a hotel or through a travel agent, termed the “[A]gency [M]odel.”\textsuperscript{103} In this scenario, a customer calls the hotel or a “traditional travel agent” to reserve a room and upon checkout, will “pay for the room and applicable occupancy taxes to the hotel based on the \textit{retail price} of the room.”\textsuperscript{104} For example, if the room rate is $200 per night with hotel taxes of 10\%, the traveler owes $20 in hotel taxes \textit{in addition to} the $200 room rate.\textsuperscript{105} The hotel retains the room rate and remits the hotel taxes to the government.\textsuperscript{106} Under this Model, whether the traveler books the room “directly with the hotel or via a travel agent [who is paid a commission by the hotel],” the hotel taxes are based on the retail price of the room,\textsuperscript{107} the $200.

Now consider the transaction in dispute, often termed the “[M]erchant [M]odel,” when a traveler reserves a hotel room through an OTC.\textsuperscript{108} Similar to the three participants of a Groupon voucher sale,\textsuperscript{109} an Expedia transaction involves: the customer who purchases the hotel room (e.g., Buyer Bruce); the company that sells the hotel room (e.g., Expedia); and the merchant that accepts the reservation upon redemption (e.g., Heartbreak Hotel).\textsuperscript{110} As shall be shown, although the tax obligation differs between Groupon and Expedia with

\begin{thebibliography}{11}
\bibitem{101} Id.
\bibitem{104} Id. (emphasis added).
\bibitem{105} Henchman, \textit{supra} note 8, at 3.
\bibitem{106} Id.
\bibitem{107} Mak, \textit{supra} note 103, at pt. II.
\bibitem{108} Id.
\bibitem{109} See, \textit{e.g.}, Henchman, \textit{supra} note 99.
\end{thebibliography}
respect to the party responsible for submitting the tax payment owed, such functional distinctions do not render Groupon and Expedia unrelated. Ultimately, the two entities share the common tax inquiry of what constitutes the proper tax base.

To illustrate, consider again Buyer Bruce, who, after having abandoned Groupon purchases due to the sales tax uncertainties, decides to travel to Key West, Florida to regain his peace-of-mind. Buyer Bruce visits Expedia’s website and selects a hotel from the options listed.\footnote{See id.} Of the hotels that Buyer Bruce may choose from, Expedia has already contracted with each hotel chain to obtain a discounted rate for the hotels’ normally higher-priced rooms.\footnote{See Henchman, \textit{supra} note 8, at 3.} Through these contracts, hotels sell the rooms to the OTCs at a lower, “wholesale” rate, after which, the OTCs sell the rooms to travelers at higher, “retail” rates.\footnote{See Mak, \textit{supra} note 103, at pt. II.} As a result, OTCs control the price charged to customers and thus, “the profit . . . [made] from the markup” between the wholesale price and the retail price.\footnote{Id.} In return, hotels can “reach a market” that without OTCs, “they would not otherwise reach.”\footnote{Henchman, \textit{supra} note 8, at 3.}

Upon booking a hotel room from Expedia, Buyer Bruce will make \textit{one} online payment to the OTC.\footnote{See id.} This payment includes: the \textit{room rate}, as agreed upon by Heartbreak Hotel; \textit{taxes} owed on this room rate; and the remainder, which Expedia retains as a \textit{service or facilitation fee}.\footnote{See id.} To finalize the transaction, \textit{after} Buyer Bruce enjoys his hotel stay in the Keys, Heartbreak Hotel will send a bill to Expedia for “the negotiated [lower] \textit{wholesale price}” of the room, which the OTC pays along with the “hotel occupancy tax on the \textit{wholesale rate}.”\footnote{See Mak, \textit{supra} note 103, at pt. II (emphasis added).} Then, the hotel “remits the taxes on the \textit{wholesale rate}” to the taxing authority.\footnote{Id. (emphasis added).} Consider the following illustration:

\begin{quote}
[A] hotel agrees to a contract whereby it will receive only $70 a night for any OTC-facilitated rentals of the normally $100-a-night room (plus $15 in tax). . . . If the traveler using the OTC website books the room at $90 a night inclusive of taxes and fees, $70 is forwarded to the hotel as a room charge, 15 percent of that amount ($10.50) is forwarded to the hotel to
\end{quote}

\footnote{111 See id.}
\footnote{112 See Henchman, \textit{supra} note 8, at 3.}
\footnote{113 See Mak, \textit{supra} note 103, at pt. II.}
\footnote{114 Id.}
\footnote{115 Henchman, \textit{supra} note 8, at 3.}
\footnote{116 See id.}
\footnote{117 See id.}
\footnote{118 See Mak, \textit{supra} note 103, at pt. II (emphasis added).}
\footnote{119 Id. (emphasis added).}
pay hotel taxes to the government, and the remainder ($9.50) is retained by the OTC as its service fee on the transaction.\textsuperscript{120}

Resulting from this transaction are three differences between Groupon and Expedia sales. While these differences are not significant to the ultimate inquiry of the appropriate tax base, the distinctions are nonetheless useful in understanding how the two entities operate. First, where the initial Groupon sale does \textit{not} include sales tax,\textsuperscript{121} the Expedia payment due at the time of booking \textit{includes} applicable hotel occupancy taxes, paid by Buyer Bruce to Expedia.\textsuperscript{122} Where Groupon imparts to the merchants the responsibility of collecting sales tax,\textsuperscript{123} "OTCs ‘calculate’ and are responsible for collecting the occupancy tax from the customer.”\textsuperscript{124} Second, as a result, when Buyer Bruce checks out from Heartbreak Hotel, he will not be charged any hotel taxes,\textsuperscript{125} unlike a Groupon customer who, in some states, will remit sales tax to the merchant upon redeeming his voucher.\textsuperscript{126} However, similarly, both the participating merchant and hotel in a Groupon and Expedia sale, respectively, are responsible for remitting the appropriate taxes to the government.\textsuperscript{127}

Finally, Groupon and Expedia transactions differ in the amounts represented by the ‘discounted’ and ‘full’ values. In an Expedia sale, the \textit{higher}, “retail” rate is the amount that the \textit{traveler} pays to Expedia,\textsuperscript{128} unlike Groupon where the higher rate represents the undiscounted value of the voucher.\textsuperscript{129} Likewise, in an Expedia sale, where the \textit{lower}, “wholesale” rate represents the contracted-for \textit{amount paid by Expedia} to the hotel chain,\textsuperscript{130} this same discounted value in a Groupon sale is the \textit{amount paid by the consumer to Groupon}.\textsuperscript{131} Despite these distinctions

\textsuperscript{120} Henchman, \textit{supra} note 8, at 3.
\textsuperscript{121} Dion, \textit{supra} note 10.
\textsuperscript{122} See Henchman, \textit{supra} note 8, at 3.
\textsuperscript{123} Dion, \textit{supra} note 10.
\textsuperscript{124} Mak, \textit{supra} note 103, at pt. II.
\textsuperscript{125} See id. (noting that while the hotel will not bill the customer for room rates or occupancy taxes upon checkout, it \textit{will} collect “[P]ayment for incidental (non-lodging) items such as long-distance telephone calls, pay-to-view premium movies, room service, or drinks from the minibar purchased during the visit.”).
\textsuperscript{126} See, \textit{e.g.}, Grace, \textit{supra} note 7, at pt. IV.
\textsuperscript{127} Dion, \textit{supra} note 10; Mak, \textit{supra} note 103, at pt. II.
\textsuperscript{128} See Mak, \textit{supra} note 103, at pt. II.
\textsuperscript{129} See Blair, \textit{supra} note 35.
\textsuperscript{130} See Blair, \textit{supra} note 35.
between the operation of Groupon and Expedia sales, a parallel tax inquiry has resulted: which base (the retail or discounted value) to tax.

B. The Tax Base: Differing Approaches to Expedia’s Situation

1. Resulting Tax Question

Flowing from Expedia’s responsibility to remit taxes to the participating hotels, like Groupon, is the conundrum of determining what the proper amount of the tax is and how to calculate it. As set forth, the Groupon inquiry asks whether the customer, when redeeming her Groupon for the item or service sold, should pay sales tax to the merchant based on the lower, discounted amount she paid to Groupon or rather, the higher, full value of the item or service. Concerning the OTC tax inquiry, the application of the same question is slightly different due to the different structure of the transaction at issue—the question does not consider what the customer remits upon hotel checkout (as an Expedia customer pays all applicable hotel taxes at the time of online booking). Rather, the question considers what amount the OTC must remit to the hotel, which includes the taxes that will eventually be paid to the taxing authority. However, both inquiries ultimately, in different form, ask the same question: what is the appropriate tax base?

Through OTCs’ contracts with hotel chains, the OTCs “agree to collect occupancy taxes on the rooms they sell at the rate they determine.” Unlike Groupon, where merchants must determine and collect sales tax, OTCs “have sole discretion in determining whether to apply the tax to the wholesale rate . . . as opposed to the retail rate.” As a result, when Buyer Bruce books a hotel room on Expedia, hotel taxes are assessed based on the lower, wholesale rate. However, if Buyer Bruce were to book the same room through the hotel directly or a traditional travel agent, hotel taxes would be assessed on the higher, retail rate of the room.

132 Novack, supra note 5.
133 See Mak, supra note 103, at pt. II.
134 Id.
135 Id. (external citation omitted) (external quotation marks omitted).
136 Dion, supra note 10.
137 Mak, supra note 103, at pt. II (emphasis added) (external citation omitted) (external quotation marks omitted).
138 See id.
139 See id.
The resulting tax discrepancies, based only on how the room was booked, have resulted in litigation, frequently claiming that OTCs “negotiate room prices with hotels at a wholesale rate, then charge travelers who book through their websites a higher retail rate. However, the companies remit taxes only on the lower wholesale rate.” For example, “the companies buy blocks of rooms for $100 each, sell them for, say $150, and pay the room tax only on the $100.” As a result of recent lawsuits “pitting state and local governments against the OTCs,”

142 courts are now deciding whether OTCs must remit hotel occupancy taxes based on either: (1) the lower, “wholesale” room rate paid by Expedia to the participating hotel; or (2) the higher, “retail” rate that the consumer pays to Expedia for the same room.

143 Similar to the Groupon inquiry, some may wonder whether these two options offer any meaningful difference. For two parties, the consequences of this tax decision are grave. For states, an estimated “$276 to $396 million in hotel tax revenue is lost each year due to the OTCs’ practice of taxing the ‘wholesale’ room rate instead of the retail room rate.” This is lost revenue that would have “promot[ed] tourism and in some cases, pa[id] for schools, law enforcement and other municipal services.” Conversely, for OTCs like Expedia, the difference is a matter of their own revenue. OTCs, advocating for taxation based on the wholesale rate, have argued that “the difference between the price they negotiate with hotels and what they charge customers on their

140 Henchman, supra note 8, at 3 (external quotations omitted).
141 Id. n.4 (external citation omitted) (external quotation marks omitted).
142 Mak, supra note 103, at pt. II.
143 See id.; Henchman, supra note 8, at 1-3. As noted in the example of an OTC transaction accompanying infra note 150, consumers pay the same price to reserve a hotel room through an OTC as they would booking with the hotel itself—in other words, the consumer is not receiving a discounted rate through the OTCs according to this example, such that a third consideration is warranted (e.g., a lower rate paid by the consumer to the OTC). Another noteworthy consideration concerning the OTC tax question facing courts is the limitation on OTCs’ ability to manipulate the total amount of taxes owed. Because hotel operators negotiate with OTCs for the highest amount possible for the wholesale rate, OTCs cannot unilaterally reduce the amount of the tax base. In effect, interested parties, hotel operators, function to benefit the tax authority by trying to increase the tax base.
144 Jess Reagan, Update on Online Travel Company Litigation, OFF. OF THE IND. ATT’Y GEN. (June 13, 2011), at 3, http://www.taxadmin.org/ftp/meet/11am/PPTs/Reagan_061211.pdf (emphasis removed); see also Mak, supra note 103, at pt. I (stating that “[t]he difference in tax revenue collectively amounts to roughly $ 340 [sic] million, assuming an average hotel occupancy tax rate of 12.62 percent, which was the average tax rate in the United States in 2008.”).
145 Jones, supra note 6.
websites represents a fee for ‘facilitating’ the transaction”—in other words, that this difference “should not be subject to hotel occupancy taxes.” Finally, unlike a Groupon sale, where the decision of whether and how much sales tax to assess directly affects customers, Expedia customers are not affected in such a manner. They pay the same hotel tax regardless of whether they book directly with the hotel or through an OTC. Rather, “[t]he difference is how that money is divided up later on.” For example:

[A] consumer pays a room rate of $100. A local occupancy tax of 10% tacks on another $10, and so the guest pays $110. But an [OTC] may have negotiated a discounted room rate of $80 with that hotel. A guest who booked through that third-party portal still pays $110, but the online company will give the hotel $80 for the room, plus $8 for the tax, keeping the remaining $22 as its fee. If the room had been booked directly with the hotel, the municipality would receive $10 in taxes.

As discussed in the next section, the varied tax treatment on this issue, like Groupon, may have ultimately raised more questions than answers.

2. Varied Tax Treatment

Remember the list of synonyms used to describe the inconsistent state guidance concerning the Groupon issue? Those terms are also well suited for the recent court decisions considering the taxation of Expedia sales. Unlike Groupon, where, if guidance is provided, the requisite sales tax treatment is set forth in each state’s Department of Revenue publications, it has primarily been the courts that have decided the amount of hotel taxes OTCs should remit to hotels. In May 2012, the Tax Foundation reported that cities and counties had filed around seventy lawsuits across twenty-five states and the District of Columbia. The Tax Foundation also reported pending cases in Ha-

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147 See Novack, supra note 39.
148 Jones, supra note 6.
149 Id. (external quotations omitted).
150 Id.
151 See, e.g., Dion, supra note 10 (citing several states’ Department of Revenue publications).
152 See Henchman, supra note 8, at 1.
153 Id.
waii,\textsuperscript{154} Maryland, Michigan, Montana,\textsuperscript{155} Pennsylvania, and Texas,\textsuperscript{156} As of September 2012, most of these seventy lawsuits are “either on appeal or still at the trial level.”\textsuperscript{157}

While each of these twenty-five states has their own governments and respective hotel occupancy statutes, collectively, the lawsuits typically:

[I]nvolve claims by the local governments that [OTCs] are in violation of their hotel occupancy tax ordinances due to a failure to pay the hotel occupancy tax on the amount of the transaction that accrues to the OTC, described . . . as a facilitation fee, service fee, commission, markup, or difference between the ‘retail’ and ‘wholesale’ rates.\textsuperscript{158}

States claim that because the OTGs’ “activities fall under existing statutes as ‘hotel operators’ or ‘hotel room wholesalers,’” the statute thus encompasses taxation of the OTC service fees.\textsuperscript{159} One summary of these claims states: “Customers pay one total amount to the [OTCs], which then is divided among the hotel, the government, and the [OTC]. The cities’ claim is essentially that some portion of the profit kept by the [OTC] is in reality ‘owed’ taxes.”\textsuperscript{160}

As of May 2012, the Tax Foundation reported that of the twenty-five states where lawsuits have been filed, OTCs had prevailed in eighteen states,\textsuperscript{161} finding that OTCs must assess taxes only on the lower, wholesale rates. Conversely, governments, at the time of the Report, had prevailed in only three states and the District of Columbia.\textsuperscript{162} Based on these numbers alone, it appears that, like Groupon, a critical

\textsuperscript{154} See Tom Gilroy, Hawaii Insists Online Travel Companies Pay $170 Million in Back Hotel Occupancy Taxes, BNA TAX MGMT. WKLY. ST. TAX REP., Apr. 1, 2011.


\textsuperscript{156} Henchman, supra note 8, at 2, 13. These states are not in addition to the twenty-five states mentioned previously. Id. Cities in Arizona have also recently elected to pursue litigation to recover hotel taxes from OTCs. See, e.g., Amy B. Wang, Chandler Added to Lawsuit vs. Online Travel Companies, AZCENTRAL.COM (Oct. 8, 2012, 10:58 PM), http://www.azcentral.com/community/chandler/articles/20121007chandler-added-lawsuit-vs-online-travel-companies.html.

\textsuperscript{157} Mak, supra note 103, at pt. I.

\textsuperscript{158} Henchman, supra note 8, at 6.

\textsuperscript{159} Id. at 4.

\textsuperscript{160} Id. at 5.

\textsuperscript{161} Id. at 3.

\textsuperscript{162} Id. For those cases that have rendered a decision on the merits, the Tax Foundation Report provided a summary of each in alphabetical order by state. While many of these cases are mentioned in this paper, the Report illustrates the rationales for each decision. See id. at 13-24.
mass of jurisdictions are imposing taxes on the relevant discounted amount. However, this OTC wins-to-losses ratio is somewhat distorted, as it does not consider the number of lawsuits that have been settled or dismissed on various procedural grounds, as discussed below.

Similar to Groupon purchases, where the sales tax assessed depends on the location of the merchant,\textsuperscript{163} the amount of hotel taxes that OTCs will be required to remit depends on the location of the participating hotel.\textsuperscript{164} As of the May 2012 Tax Foundation Special Report, courts in the following fourteen states have held that OTCs’ service fees are not subject to hotel occupancy taxes, or, in other words, that OTCs are required to remit taxes only on the lower, wholesale value of the hotel room paid by Expedia to the hotel: Alabama,\textsuperscript{165} California,\textsuperscript{166}

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\textsuperscript{163} See Grace, supra note 7, at pt. IV (discussing various states’ sales tax approaches to daily deal vouchers).

\textsuperscript{164} See Henchman, supra note 8, at 13-24 (providing a summary of court decisions, alphabetized by state, of the requisite tax amount OTCs must remit to participating hotels).

\textsuperscript{165} Id. at 14 (citing City of Birmingham v. Orbitz, Inc., No. CV 09-3607 JSV (Ala. Cir. Ct. Mar. 24, 2011), aff’d, No. 1100874 (Ala. Apr. 13, 2012) (stating that OTCs “are not hoteliers. . . . They provide a service to the public for which they are compensated by their customers. This compensation is not subject to the lodging tax.”)).

Florida,\textsuperscript{167} Georgia,\textsuperscript{168} Kentucky,\textsuperscript{169} Missouri,\textsuperscript{170} New Mexico,\textsuperscript{171} New


\textsuperscript{168} A Supreme Court of Georgia case is interpreted as positing that while “OTCs are not operators of hotels and are not obligated to pay taxes, [they] must remit any taxes they collect.” Henchman, \textit{supra} note 8, at 17-18 (citing Expedia, Inc. v. City of Columbus, 681 S.E.2d 122, 128 (Ga. 2009) (stating that “[s]ince Expedia has chosen to represent the room rate to the public as the price a customer must pay to secure his right to occupy the room, the City has no choice . . . but to tax the customer for the published room rate demanded by Expedia.”)). Ultimately, this opinion is interpreted as a win for the city, as it requires OTCs to remit hotel taxes, if collected, based on the higher, retail rate. \textit{See} Tom Gilroy, \textit{Georgia Supreme Court Reaffirms Hotel Occupancy Tax Due on Full Price of Rooms}, BNA TAX MGMT. WKLY. ST. TAX REP., May 20, 2011. Because Expedia and other OTCs do collect taxes from customers, as agreed upon in their respective contracts, the retail rate ultimately applies. \textit{See} William Hays Weissman, \textit{Taxing the Internet, Sort Of}, ST. TAX TODAY, Oct. 26, 2009, available at 2009 STT 204-3.

\textsuperscript{169} Henchman, \textit{supra} note 8, at 18 (citing City of Bowling Green v. Hotels.com, L.P., 357 S.W.3d 531, 533 (Ky. Ct. App. 2011) (stating that “[t]he OTCs did not provide physical accommodations within the City of Bowling Green.”)). The Kentucky Supreme Court later “denied a motion to rehear [the] case.” Jessica M. Karmasek, \textit{Courts Say Online Travel Companies Can’t Be Taxed}, LEGAL NEWSLINE (Mar. 9, 2012, 9:20 AM), http://legalnewsline.com/news/235454-courts-say-online-travel-companies-cant-be-taxed. The United States Court of Appeals for the Sixth Circuit also held that the services fees are not subject to hotel tax, on appeal from the U.S. District Court for the Western District of Kentucky. \textit{See} Henchman, \textit{supra} note 8, at 13 (citing Louisville/ Jefferson Cnty. Metro Gov’t v. Hotels.com, L.P., 590 F.3d 381 (6th Cir. 2009)).

\textsuperscript{170} Henchman, \textit{supra} note 8, at 18-19 (citing St. Louis Cnty. v. Prestige Travel, Inc., No. SC91228, 2011 Mo. LEXIS 198, at *11 (Mo. June 28, 2011) (stating that “it is clear the obligation to file the tax was placed solely on those ‘engaged in the business of operating a hotel or motel.’”))).

\textsuperscript{171} Henchman, \textit{supra} note 8, at 19 (citing City of Gallup v. Hotels.com, L.P., No. CV 07-644 JC/RLP, 2009 U.S. Dist. LEXIS 126818 (D.N.M. Mar. 1, 2010)).
York, North Carolina, Ohio, Oklahoma, Pennsylvania, and Texas. Conversely, courts in the following five states have held that OTC service fees are subject to hotel taxes, or, in other words, OTCs are required to remit taxes on the higher, retail rate paid


173 The Fourth Circuit held that OTC services fees are not subject to hotel tax, affirming the decision of the U.S. District Court for the Eastern District of North Carolina. See Henchman, supra note 8, at 13 (citing Pitt Cnty. v. Hotels.com, L.P., 553 F.3d 308, 314 (4th Cir. 2009)). The Court “held that hotel taxes are owed only by retailers that operate retail facilities, and that online travel companies are not hotel operators.” Henchman, supra note 99.


177 Henchman, supra note 8, at 22 (citing City of Goodlettesville v. Priceline.com, Inc., No. 3:08-cv-000561, 2012 U.S. Dist. LEXIS 21195 (M.D. Tenn. Feb. 21, 2012)). One article summarized the opinion as stating that “it was up to the cities to rework the current tax laws if they want to be able to go after the companies for taxes.” Karmasek, supra note 169.

by the customer to Expedia: Georgia,\textsuperscript{179} Illinois,\textsuperscript{180} South Carolina,\textsuperscript{181} Texas\textsuperscript{182} and D.C.\textsuperscript{183}

At first glance, it may appear that OTCs are prevailing on this issue, with a majority of courts finding that OTCs’ service fees are \textit{not} subject to hotel occupancy taxes, or, in other words, that OTCs are required to remit taxes only on the lower, wholesale value of the room. As in the case of Groupon, where a majority of states have required merchants to tax only the discounted value of the voucher, one could assert that the same is true for Expedia—that a critical mass is also imposing taxes only on the discounted value (in this case, the lower, wholesale rates). However, unlike Groupon, where the states’ respective Departments of Revenue answer the tax question, here, courts

\textsuperscript{179} Carr, \textit{supra} note 172 (citing City of Atlanta v. Hotels.com, L.P., No. S11A0508, 2011 Ga. LEXIS 386, at *6 (Ga. May 16, 2011)). Note that Henchman, \textit{supra} note 8, at 17, describes \textit{City of Atlanta} as \textit{not} subjecting OTC service fees to hotel tax. However, other sources confirm that \textit{City of Atlanta} held against the OTCs, holding that they owe hotel taxes on the higher, retail room rate. See, e.g., \textit{Georgia Supreme Court: Online Travel Companies Must Collect Hotel Tax On Retail Rate,} \textit{St. Tax Today,} May 17, 2011, \textit{available at} 2011 STT 95-11. For a Georgia case holding that OTC service fees are \textit{not} subject to hotel taxes, see Expedia, Inc. v. City of Columbus, 681 S.E.2d 122 (Ga. 2009).


\textsuperscript{181} Henchman, \textit{supra} note 8, at 21 (citing Travelscape, LLC v. S.C. Dep’t of Revenue, 705 S.E.2d 28 (S.C. 2011) (finding that OTC services fees are subject to hotel tax because OTCs are “engaged . . . in the business of furnishing accommodations.”)). See also Tom Gilroy, \textit{South Carolina Supreme Court Upholds Expedia $4.7 Million Sales Tax Assessment,} \textit{Tax Mgmt. Wkly. St. Tax Rep.,} Jan. 8, 2011.


have decided this inquiry. This has had implications not arising in the Groupon context.

As of June 15, 2011, sixteen cases were “dismissed for procedural reasons, such as failure to exhaust administrative remedies, denial of class certification, or lack of standing;” five cases were “dismissed without prejudice;” and in ten cases, “the [OTCs] have paid several million dollars to settle.” Indeed, nearly 9 million dollars “has been disclosed as paid in settlement of these OTC cases.” The rulings that favor the OTCs, though currently greater in number than those for the government plaintiffs, must be considered alongside these recent settlements between the OTCs and state and city governments. The opinions favoring OTCs are also deflated by the rising number of jurisdictions that are amending their hotel occupancy statutes and setting forth other guidance, requiring OTCs to assess taxes based on the higher, retail rate of the rooms. The North Carolina Legislature

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184 The Multistate Tax Commission is also involved, “providing two different approaches for states to choose from in its draft model statute on tax collection and remittance procedures for hotels and online travel companies.” Amy Hamilton, Online Travel Companies Voice Concerns with MTC Draft Model Statute, ST. TAX TODAY, Apr. 11, 2012, available at 2012 STT 70-1.

185 Setze, supra note 9.

186 Id.

187 Id.


189 In response, OTCs “have sued to stop other governments in the U.S. from imposing the higher levy.” See, e.g., Michael DeMasi, Priceline, Expedia Could Face Higher Occupancy Room Taxes in Saratoga Springs, THE BUS. REV. (Sept. 24, 2012, 2:58 PM), http://www.bizjournals.com/albany/news/2012/09/24/priceline-expedia-could-face-higher.html?page=all; Tom Gilroy, D.C. Law Requiring Online Travel Firms to Pay Hotel Tax on Full Price Takes Effect, TAX MGMT. Wkly. ST. TAX REP., Apr. 22, 2011. New Hampshire has published a Technical Information Release, claiming that taxes must be calculated based on the higher, retail rate of the room paid by the occupant. See New Hampshire DOR Provides Guidelines for Hotel Operators Using Online Booking Companies, ST. TAX TODAY, Jan. 10, 2008, available at 2008 STT 7-14. Bills “have also been introduced in a number of states in recent years, including such bills in 2011 legislative sessions as Raised Bill 6624 in Connecticut, Senate Bill 1577 and House Bill 1454 in Texas, Senate Bill 296 in
passed one example of such legislation in 2010 in response to “court decisions that local occupancy tax statutes did not cover the OTCs’ ‘facilitation’ fee.” 

Several OTCs filed suit seeking to block such amendments:

The lawsuit takes aim at North Carolina’s Department of Revenue, which in late December 2010 issued a notice on the amendments to modernize sales tax on accommodation rentals, and made it clear that the basis for calculating accommodation taxes includes “charges designated as facilitation fees and any other charges necessary to complete the accommodation rental.”

When considering all of the avenues affecting the Expedia tax question—court rulings, settlement agreements, and legislative responses—it is not improbable that the tides may turn in favor of states and municipalities in the not-so-distant future.

C. The Best Tax Approach

Regardless of which entity is currently prevailing (OTCs or governments), one must still consider which approach is better—assessing hotel taxes on the higher, retail room rate or instead, the lower, wholesale rate. As courts continue to wrestle with this issue, it is at least clear that a resolution is needed. And, like Groupon, fast. In the meantime, those courts with current OTC cases should mirror the Groupon regulatory majority imposing a lower tax base. When two modern trends such as Groupon and Expedia pose the same legal question, the solution should apply equally across both tax-generating bodies. As a result, undecided OTC cases should fall in line behind those courts comprising a “majority” and require that OTCs remit hotel taxes based only on the lower, wholesale room rate.

1. Statutory Interpretation

Similar to Groupon, where statutory interpretation supports the contention that the lower tax base should prevail, such analysis in the OTC context produces the same conclusion. Where the definition of “sales price” within the Groupon arena argued for a lower tax base, similarly, in the OTC realm, the statutory definition of “hotel opera-


190 Gilroy, supra note 9.

191 Id.

192 See Mazerov, supra note 189. For the opposing position that OTCs should remit hotel taxes based on the higher, retail rate, see Mak, supra note 103.
tor” supports the same. The Tax Foundation reported that of the seventy lawsuits filed as of May 2012, twenty-six cases rendered an opinion on the merits.\footnote{Henchman, supra note 8, at 6.} Of the fifteen cases where courts considered “whether [OTCs] are hotel ‘operators’ for purposes of hotel occupancy statutes,” twelve held for OTCs, finding that they are not hotel operators\footnote{Id. at 6 (citing City of Birmingham, at 25).} within the meaning of the applicable statute.\footnote{Id. at 8 (citing City of Birmingham v. Orbitz, Inc., No. CV-09-3607 JSV, 2011 WL 9753765 (Ala. Cir. Ct. Mar. 24, 2011); City of Santa Monica v. Expedia, Inc., No. SC108568 (Cal. Super. Ct. L.A. County Mar. 16, 2011); Orange Cnty. v. Expedia, Inc., No. 48-2006-CA-2104-O (Fla. Cir. Ct. Jan. 20, 2011); St. Louis Cnty. v. Prestige Travel, Inc., No. SC 91228, 2011 Mo. LEXIS 198 (Mo. June 28, 2011); City of Findlay v. Hotels.com, L.P., No. 441 F. Supp. 2d 855 (N.D. Ohio 2006); City of Phila. v. City of Phila. Tax Rev. Bd., No. 00764, 2011 WL 6961120 (Pa. Commw. Ct. Feb. 2, 2012); City of Goodlettesville v. Priceline.com, Inc., No. 3:08-cv-00561, 2012 U.S. Dist. LEXIS 21195 (M.D. Tenn. Feb. 21, 2012); City of Orange v. Hotels.com, L.P., No. 1:06-CV-413, 2007 WL 2787985 (E.D. Tex. Sept. 21, 2007).} One rationale for this finding, set forth by the Superior Court of Los Angeles County, California, states that “[o]ne cannot logically conclude . . . that because a hotel operator is required to furnish a receipt specifying the amount of taxes, therefore any entity that furnishes a receipt of some sort to the consumer must be an operator.”\footnote{Id. at 6 (citing City of Anaheim, at 25).}

Supreme Court, states that “‘the money [the OTC] retains is compensation for facilitating a reservation, not providing a sleeping room,’ outside the scope of a tax on amounts paid by hotel guests.” Based on such statutory analysis here as well as the considerations of “hotel operator,” one can rightfully conclude that the taxable value should be the lower amount—the “wholesale” room rate paid by Expedia to the participating hotel.

2. Economic Considerations

Like Groupon, alongside statutory interpretations supporting a lower tax base, economic considerations are also pertinent. Where the economic arguments within Groupon focused solely on the consumer, here, the solution is based, more or less, on reasonableness. In arguing that the assessment of hotel taxes should not include the OTC service fees, one commentator stated, “Occupancy taxes are based on the rate the hotel sets and receives, . . . not the profits, fees or commissions of its partners. . . . The facilitation fees are no more part of the hotel rate than the taxi that takes the guest from the airport or the tip they give the bellhop.”

When considering the fairness of taxing the OTC service fees, one may ask: why not tax all service fees, not just those of online companies? In addressing this question, one author posited, “because officials want to extract more revenue from out-of-state travelers and out-of-state businesses, the result is an effort to tax only services provided by out-of-state and Internet businesses.” Considering the fairness of this tax approach, the author argues convincingly that if OTCs are required to remit hotel taxes based on their service fees, then all service fees should be taxed:


198 Id. at 8 (citing St. Louis Cnty., at 6).
199 Jones, supra note 6 (emphasis added). It is noted that regarding the taxi and bell-hop examples, such payments are related to, yet distinct from, the cost of the hotel room (what is being taxed); whereas, here, a consumer is paying only for the hotel room, not for the OTC’s placement service. However, in some form, the consumer actually is paying for the OTC’s placement service (in a round-about-way), as the percentage of the consumer’s purchase price that the OTC does not remit to the state, the OTC retains as its service fee. See the example of an OTC transaction accompanying supra note 150.
200 See generally Henchman, supra note 8.
201 Id. at 5.
There is no principled basis for only taxing those services provided by Internet businesses. If state and local officials believe that [OTCs] should pay sales or excise tax based on the services they provide, the payment should only occur as part of a general taxation of all services. . . . By singling out only services provided by Internet-based travel companies, state and local governments are demonstrating that their true motivation is gouging revenue from out-of-staters, not fairness.202

Regarding OTCs’ customers, as noted previously, consumers have been less of the focus in the Expedia context than in Groupon—where the primary inquiry there concerned whether and how much sales tax Groupon customers should remit to merchants upon redemption of the voucher, the Expedia inquiry asks how much hotel taxes OTCs are required to remit to hotels. However, if courts in various states require OTCs to remit hotel taxes based on the higher, retail room rate, OTCs can pay their requisite damages and simply refuse to continue listing that particular city or state’s hotels on its websites.203 This will, of course, disadvantage those hotel chains, but it will also harm consumers who are unable to reserve hotels for that area with the convenience of OTCs. “The municipalities that bring these lawsuits are likely doing a disservice to persons, whether residents or out-of-towners, who would like to stay in a hotel.”204 State and city officials must “wonder whether they won the battle but will end up losing the war.”205

As one commentator noted, regardless of the solution, this approach to finding it is inefficient and cumbersome: “Whatever the solution, it should be a well thought-out, comprehensive approach, and not this case-by-case approach that is draining resources from the companies, the localities, and the courts.”206

202 Id. at 11 (emphasis added). It is noted that the government could argue that it is not taxing OTCs’ facilitation or service fees, but rather, is merely taxing the value of the hotel room as paid by the customer. However, as noted above, in some sense, encompassed within the value of the hotel room is the service fee, as, what the OTC does not remit of the consumer’s payment, it retains as such a fee. See the example of an OTC transaction accompanying supra note 150.


204 Weissman, supra note 168.

205 Id. For additional coverage on this topic, see, for example, James A. Amdur, Obligation of Online Travel Companies to Collect and Remit Hotel Occupancy Taxes, 61 A.L.R. 6th 387 (2011); Kerra J. Melvin, Technology, Travel Companies & Taxation: Should Expedia Be Required to Collect and Remit State Occupancy Taxes on Profits from Facilitating Hotel Room Rentals?, 8 Wash. J.L. Tech. & Arts 43 (2012).

206 Weissman, supra note 168.
IV. Conclusion

The Groupon and Expedia business models are at the forefront because they present an opportunity for cities, municipalities and states to raise revenue207—by Groupon, in the form of sales tax and by OTCs, in the form of hotel tax. The resulting difficulty has been deciding how to obtain such revenue, and namely, how to do so fairly. As one analyst said of the Expedia inquiry, it is immaterial whether Expedia or other OTCs qualify as a “hotel operator,” as many opinions do in fact consider—instead, “[i]f states or localities want to raise more revenue, they could just raise the rate rather than argue about which price to apply it to.”208

While increasing the tax rates is a possible alternative to increasing revenue (yet, still leaves the issue of determining the proper tax base), the point is this: there are other solutions to consider rather than the case-by-case, state-by-state approach being taken among those decision-makers of the Groupon and Expedia tax inquiries. Really, “given the fractured nature of state and local governments, it might require some sort of federal intervention. Although that is probably not a popular idea, the one thing that seems clear is that ultimately the status quo is going to have to change.”209 Whatever and however the change, in an area where two modern trends pose the same tax issue, at the least, the proper solution—a lower tax base—should be applied equally across both sectors—not only for consistency’s sake, but for taxpayers’ sake.

207 See id. (setting forth this consideration in the context of OTCs). Though, of opinion, the thought applies equally to the Groupon consideration as well.
208 Id.
209 Id. (emphasis added) (setting forth this consideration in the context of OTCs). Though, of opinion, the thought applies equally to the Groupon consideration as well.