

September 10, 2018

ABC Hotel  
123 Main St.  
San Diego, CA 92101

**Subject: California Supreme Court Ruling on Transient Occupancy Tax**

Dear Hotel Operator:

The California Supreme Court in *In re Transient Occupancy Tax Cases*<sup>1</sup> issued an opinion (“Opinion”) that may impact your hotel’s payment of Transient Occupancy Taxes (TOT) and Tourism Marketing District (TMD) assessments to the City of San Diego (City). The Opinion affects those hotels who sell rooms through third parties like online travel companies (collectively referred to as “OTCs”) under the “merchant model” (see **Attachment A**) and who have a rate parity agreement<sup>2</sup> with one or more OTCs.

In essence, for any rooms sold through an OTC, your hotel must remit TOT and the TMD assessment based on the minimum retail rate you require an OTC to charge its customer, otherwise known as the rate parity amount.<sup>3</sup> Before the Opinion, hotels had only remitted occupancy taxes to San Diego on the wholesale room rate,<sup>4</sup> resulting in underpayment of TOT and TMD assessments.

It is our understanding that many hotels have indemnification agreements with OTCs in which the OTCs have agreed to indemnify the hotels for any TOT and TMD assessment liability that results from the underpayment of TOT and TMD assessments in these circumstances. Thus, to the extent that you have indemnity agreements with any of the OTCs,<sup>5</sup> they may ultimately be obligated to pay these additional amounts of TOT and TMD assessments.

The purpose of this letter is to ensure that (1) you are complying with the Opinion and the City has been made whole for past TOT and TMD assessment underpayments resulting from erroneously calculated remittances to the City, and (2) on a going-forward basis, the City is

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<sup>1</sup> *In re Transient Occupancy Tax Cases*, 2 Cal. 5<sup>th</sup> 131 (2016)  
([www.sandiego.gov/sites/default/files/tr\\_in\\_re\\_transient\\_occupancy\\_tax\\_cases.pdf](http://www.sandiego.gov/sites/default/files/tr_in_re_transient_occupancy_tax_cases.pdf))

<sup>2</sup> The Supreme Court described “rate parity” provisions as meaning “any provisions in hotel-OTC contracts that set the ‘floor’ room rate the OTCs must quote and charge customers.” *Id.* at 135, fn. 3.

<sup>3</sup> The rate parity amount is the room rate that is set pursuant to a rate parity agreement between a hotel and an OTC.

<sup>4</sup> The wholesale room rate is the amount that a hotel offers to sell a room to an OTC.

<sup>5</sup> Some examples of OTCs include Expedia, Inc., Hotels.com, L.P., Hotwire, Inc., Orbitz, LLC, Trip Network, Inc. (d/b/a Cheaptickets.com), Internetnetwork Publishing Corp. (d/b/a Lodging.com), Priceline.com Incorporated, Travelweb LLC, Travelocity.com, L.P., and Site59com, LLC.

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paid TOT and TMD assessments on the rate parity amount and not the wholesale rate for merchant model transactions.

To confirm your compliance with the Opinion, please send us all contracts and documents between your hotel(s) and all OTCs with whom you have had agreements from 2000 to the present. Please contact our office via email at [sdtot@sandiego.gov](mailto:sdtot@sandiego.gov) or (619) 615-1530 to set up a secure method to provide your files electronically.

Sincerely,



Gail R. Granewich  
City Treasurer

Enclosure: Attachment A – The Merchant Model

## ATTACHMENT A – The Merchant Model

In explaining the operation of the merchant model, the California Supreme Court stated:

*The price the hotel charges the OTC for the room is the “wholesale” price; rate parity provisions in most master contracts between OTCs and hotels bar the OTC from selling a room for a rent lower than what the hotel quotes its customers directly. The OTC offers the rooms to the public at retail prices. Its charge to the customer includes a “tax recovery charge,” which represents the OTC’s estimate of what the hotel will owe in transient occupancy tax based on the wholesale price of the room as charged by the hotel to the OTC.... The hotel then bills the OTC for the wholesale price of the room plus transient occupancy tax the hotel will have to pay based on the room’s wholesale price. The OTC remits the charged amount to the hotel, which in turn remits the tax to San Diego; the OTC retains its markup and service fees.<sup>1</sup>*

### Incorrect Application of the Merchant Model

As an example of a merchant-model transaction incorrectly applied, assume a hotel charges the OTC a “wholesale” price of \$80 for a room and the OTC then charges the customer at the “rate parity amount” of \$100, plus a “tax recovery charge” equal to 10.5% (the City TOT rate) on the \$80 wholesale price, or \$8.40. Thus, the OTC bills the customer \$100 for the room plus \$8.40 in taxes for a total price of \$108.40. The OTC remits the \$80 wholesale price plus the \$8.40 in taxes to the hotel. In turn, the hotel remits \$8.40 in taxes to the City.

### Correct Application of the Merchant Model

Using the example above, the Supreme Court’s ruling means the hotel must remit TOT on the \$100 rate parity amount, or \$10.50 (\$100 multiplied by 10.5%), and not just the \$8.40 amount on the \$80 wholesale rate. This difference of \$2.10 (\$10.50 minus \$8.40) is the additional amount owed to the City under the correct application of the merchant model using this example. Furthermore, the TMD assessment<sup>2</sup> consisting of an additional 2 percent of the rent would also need to be reported and remitted to the City based on the same methodology.

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<sup>1</sup> *In re Transient Occupancy Tax Cases*, 2 Cal. 5<sup>th</sup> 131, 135 (2016)  
([www.sandiego.gov/sites/default/files/tr\\_in\\_re\\_transient\\_occupancy\\_tax\\_cases.pdf](http://www.sandiego.gov/sites/default/files/tr_in_re_transient_occupancy_tax_cases.pdf))

<sup>2</sup> At the time of the original lawsuit against the OTCs, the TMD had not yet been created so TMD assessments were not included in the action. Like the TOT, the TMD assessment is based on a percentage of the Rent as defined in San Diego Municipal Code section 35.0102.



Office of the City Treasurer  
 Transient Occupancy Tax (TOT)/  
 Tourism Marketing District (TMD) Return

**For Period End Dates 9/1/16 or later**

<b>For Office Use Only</b>	
Postmark Date _____	
Amount Paid _____	

Payments can also be remitted online at <https://webapps.sandiego.gov/TOTPay/>

General Information	
Certificate Number * _____	Return For Month Ended * <sup>1</sup> _____ <div style="text-align: right; margin-top: -10px;">Month _____ Year _____</div>
Property Name _____	
Property Address* Street # _____ Street _____ Unit _____	
City _____ State _____ Zip Code _____	
TOT Calculation	
1. Taxable/Assessable Rent* _____	
2. Additional OTC Rent* _____	
3. Total Taxable/Assessable Rent (Line 1 plus Line 2) _____	
4. Gross TOT Due* (10.5% of Line 3, or TOT collected, whichever is greater) _____	
5. Less: Credit (not common) _____	
6. TOT Due (Line 4 minus Line 5) _____	
7. TOT Late Penalty (1% 1st day plus 1/3 of 1% each additional day, not to exceed 25%) _____	
<b>8. Total TOT and Late Penalty Due (Line 6 plus Line 7)</b> _____	
TMD Calculation (Applicable to lodging businesses with 70 or more rooms/units)	
9. Gross TMD Due (2.00% of Line 3) _____	
10. Less: Credit (not common) _____	
11. TMD Due (Line 9 minus Line 10) _____	
12. TMD Late Penalty (1% 1st day plus 1/3 of 1% each additional day, not to exceed 25%) _____	
<b>13. Total TMD and Late Penalty Due (Line 11 plus Line 12)</b> _____	
<b>14. Grand Total TOT and TMD Due (Line 8 plus Line 13)</b> _____	

I declare under penalty of perjury that I am authorized to make this statement and that to the best of my knowledge and belief, it is a true, correct, and complete statement.

Authorized Signature\* \_\_\_\_\_ Date \_\_\_\_\_

E-mail Address \_\_\_\_\_ Phone \_\_\_\_\_

\* Required Fields  
<sup>1</sup> Per San Diego Municipal Code §35.0114, monthly remittance is considered timely when postmarked on or before the last day of the following month.

## TOT/TMD Return Instructions



### Additional Return Information

**1. Taxable/Assessable Rent** is the total consideration charged to a Transient as shown on the guest receipt for the occupancy of a room, or portion thereof, net of any Exemptions. For rooms sold through an online travel company (OTC), revenue received based on the Wholesale Room Rate must be included in Taxable/Assessable Rent. The Wholesale Room Rate is the amount that an Operator charges an OTC for the Operator's room.

**2. Additional OTC Rent** is the difference between the Wholesale Room Rate and the Rate Parity Amount for transactions in the reporting period. The Wholesale Room Rate is the amount that an Operator charges an OTC for the Operator's room. The Rate Parity Amount is the minimum rate that an OTC must charge to sell an Operator's room which is set pursuant to an agreement between an Operator and an OTC (also known as a Rate Parity Agreement). Additional information can be found at: <https://www.sandiego.gov/treasurer/taxesfees/tot/rateparityfaq>

**3. Total Taxable/Assessable Rent** (Line 1 plus Line 2)

**4. Gross TOT Due** is the greater of 10.5% of Total Taxable/Assessable Rent, line 3, or TOT collected.

**5. Credits** are not common, but may include a credit due as the result of a compliance audit or an overpayment remitted by the Operator. Credits may be used to offset all or a portion of TOT due; however, a credit shall not exceed TOT due. Operators claiming credits resulting from an audit must attach the credit letter to the monthly return, noting any differences between the amount claimed and the credit amount stated in the letter.

**6. TOT Due** (Line 4 minus Line 5)

**7. TOT Late Penalty** is due for late TOT payments. Penalties are computed at the rate of 1% for the 1st day plus 1/3 of 1% each additional day, not to exceed 25%, of the amount of the tax due. The penalty schedule can be found at: <http://www.sandiego.gov/treasurer/pdf/pentab.pdf>

**8. Total TOT and Late Penalty Due** (Line 6 plus Line 7)

**Note - Lines 9 through 13 are applicable to lodging businesses with 70 or more rooms/units.**

**9. Gross TMD Due** is equal to 2.00% of Line 3.

**10. Credits** are not common, but may include an overpayment remitted by an Operator for a prior period or can be due as a result of a compliance audit or an adjustment for exempt contract rent. Credits cannot exceed TMD due. Operators claiming credits resulting from an audit must attach the credit letter to the monthly return, noting any differences between the amount claimed and the credit amount stated in the letter.

**11. TMD Due** (Line 9 minus Line 10)

**12. TMD Late Penalty** is due for late TMD payments. Penalties are computed at the rate of 1% for the 1st day plus 1/3 of 1% each additional day, not to exceed 25%, of the amount of the assessment due. The penalty schedule can be found at: <http://www.sandiego.gov/treasurer/pdf/pentab.pdf>

**13. Total TMD and Late Penalty Due** (Line 11 plus Line 12)

**14. Grand Total TOT And TMD Due** (Line 8 plus Line 13)



### How to Submit this Return

The signed return and payment may be sent to the Office of the City Treasurer as follows:

1. Make check or money order payable to City Treasurer
2. Payment and Return can be mailed to:  
**Office of the City Treasurer**  
**Attn: TOT/TMD Desk**  
**PO Box 122289**  
**San Diego, CA 92112-2289**



### Questions or Additional Assistance

- Visit our TOT/TMD Website at: <http://www.sandiego.gov/treasurer/taxesfees/tot/index.shtml>
- Contact TOT/TMD Administration:  
Email at [SDTOT@sandiego.gov](mailto:SDTOT@sandiego.gov)  
Office (619) 615-1530