City of Fayetteville Staff Review Form

2018-0470

Legistar File ID

9/18/2018

City Council Meeting Date - Agenda Item Only
N/A for Non-Agenda Item

Blake Pennington	8/27/2018	CITY ATTORNEY (021)
Submitted By	**Submitted Date**	**Division / Department**

Action Recommendation:

Mayor's signature on engagement letter with Thrash Law Firm, Williams & Anderson PLC, The Finnell Firm, and Bird Law Group so the City of Fayetteville may file a claim for unpaid HMR taxes in the case of Pine Bluff A&P Commission, et al v. Hotels.com, et al.

Budget Impact:

Account Number			Fund	
Project Number			Project Title	
Budgeted Item?	NA	Current Budget	$	-
		Funds Obligated	$	-
		Current Balance	$	-
Does item have a cost?	No	Item Cost		
Budget Adjustment Attached?	NA	Budget Adjustment		
		Remaining Budget	$	-

V20180321

Purchase Order Number:

Previous Ordinance or Resolution #

Change Order Number:

Approval Date:

Original Contract Number:

Comments:

OFFICE OF THE
CITY ATTORNEY

DEPARTMENTAL CORRESPONDENCE

Kit Williams
City Attorney

Blake Pennington
Assistant City Attorney

Rhonda Lynch
Paralegal

TO: **Mayor Jordan**
City Council

FROM: **Blake Pennington**, Assistant City Attorney

DATE: **August 27, 2018**

RE: **Outside Counsel Engagement Letter – Pine Bluff A&P Commission, et al v. Hotels.com, et al – Unpaid Hotel, Motel & Restaurant Taxes**

In 2009, a lawsuit was commenced on behalf of the Pine Bluff A&P Commission and Jefferson County over unpaid HMR taxes that were collected by online travel companies for several years but never remitted to the local tax authorities. The City of North Little Rock joined the lawsuit in 2011 and the suit was granted class-action status in 2013. A final judgment, a copy of which is attached, was entered against the travel companies earlier this spring.

Because it is a class action lawsuit, other similarly situated cities, counties, and A&P commissions will be able to file claims to recover unpaid taxes from the defendants in this case. The case is currently on appeal but, if the judgment is upheld, the attorneys appointed by the court to represent the class want to be in a position to quickly file claims on behalf of the class members.

The attorneys for the class include Thrash Law Firm and Williams & Anderson PLC of Little Rock, and The Finnell Firm and Bird Law Group which are Georgia law firms. § 31.45(E) of the City Code requires City Council approval to hire outside counsel.

This requires no up-front payment by the City but the attorneys representing the class will be entitled to fees and costs on the back end by awarding a portion of the total sum recovered from the defendants. This will reduce the amount paid to the class members but this is standard in class action cases. The final award of attorney fees and costs must be approved by the court.

Our office recommends hiring these firms to file a claim to recover any unpaid taxes to which we are entitled. If authorized, the City of Fayetteville will join the lawsuit alongside the Fayetteville A&P Commission, the Fort Smith A&P Commission and the City of Magnolia. Several local taxing authorities are expected to join the case. Once the claim filing period has passed, the Court will oversee a process in which the defendant travel companies will have to turn over their records showing what taxes were collected but never remitted to the class members. This is a potential significant benefit with low risk to the City.

THRASH LAW FIRM, P.A.
1101 Garland Street
Little Rock, AR 72201

Thomas P. Thrash
tomthrash@thrashlawfirmpa.com

Telephone: 501-374-1058
Facsimile: 501-374-2222

August 27, 2018

Mayor Lioneld Jordan
c/o Kit Williams
City of Fayetteville
113 W Mountain Street, Suite 302
Fayetteville, AR 72701

Re: ***Pine Bluff A&P Commission, et al v. Hotels.com, et al***

Intervention and Claim

Dear Mayor Jordan:

Please allow this letter to confirm your request that we represent the interest of the City of Fayetteville, as an Intervenor and a Claimant in the above referenced case. Your execution and approval of this *Letter of Agreement* will represent our authority to proceed with your intervention and claim in the above-described litigation.

You will not be responsible for any attorneys' fees or expenses. We will advance all expenses and deduct the expenses from any recovery in this case. Any award of legal fees and expenses will be determined and approved by the Court and will be paid from the overall recovery in this case. The attorneys representing the Plaintiffs and Intervenors in this case include: Thrash Law Firm, P.A., 1101 Garland Street, Little Rock, Arkansas 72201; Williams & Anderson PLC, 111 Center Street, Suite 2200, Little Rock, AR 72201; The Finnell Firm, PO Box 63, Rome, GA 30162-0063; and Bird Law Group, P.C., 2170 Defoor Hills Road NW, Atlanta, GA 30318.

If this accurately represents our agreement, please acknowledge your approval by your signature below.

Sincerely,

Thomas P. Thrash

APPROVED AND AGREED TO:

_____

Mayor Lioneld Jordan
City of Fayetteville

Cities, others urged to file tax claims

Court in Jefferson County finds 12 online travel firms liable for unremitted taxes

By Bill Bowden
Posted: May 20, 2018 at 1 a.m.

1

Online travel companies owe millions of dollars in Arkansas taxes that they collected over the past 23 years, said Thomas P. Thrash, a Little Rock attorney.

Jefferson County Circuit Judge Robert H. Wyatt Jr. ruled Monday that Hotels.com and 11 other online travel companies are liable for the back taxes, and he's giving potential plaintiffs four months to intervene in the lawsuit and make a claim for damages.

"It is like a bird nest on the ground," Thrash said. "The liability has been determined. The state, cities, counties and A&P commissions just need to file their claim and get paid."

The lawsuit was filed in 2009. The initial plaintiffs were the Pine Bluff Advertising and Promotion Commission and Jefferson County. North Little Rock was added as a plaintiff in 2011.

The case was granted class-action status in 2013, but taxing entities must file a motion to intervene in the lawsuit and make a claim for damages before they can collect any money.

Thrash said there are more than 40 advertising and promotion commissions in the state, and the lawsuit would likely affect all 75 counties.

"Any city with a Holiday Inn or other chain -- Comfort Inn, Motel 6, etc. -- would have online bookings," he said. "Most all counties would be included."

But Mike Maloney, executive director of the City Advertising and Promotion Commission in Eureka Springs, said calculating lost revenue over 23 years -- or a fraction thereof -- could be quite a chore.

"We have so many lodging properties -- 130, 135, I don't know what the exact number is," Maloney said. "To go back 23 years and pull whatever documentation out is going to be an issue. ... It would be a huge amount of money."

Claude Legris, president of the Arkansas Association of Convention and Visitors Bureaus, agreed.

"I venture it will be extremely difficult to do the look-back on it," said Legris, who is also executive director of the Fort Smith Advertising and Promotions Commission. "It could be quite a daunting task for the individual destinations."

Thrash said the cities, counties, and advertising and promotion commissions don't have to do that legwork.

"They do not have to do anything to determine their damages," he said. "They just have to claim they didn't receive taxes from the online travel companies. The court has ordered the online travel companies to provide the damage data within 30 days after [the taxing entities] make a claim."

RECOMMENDED COMMENTED

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Updated: Torn broken in Fort

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They just have to make a general claim, Thrash said.

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Wyatt had informed the parties of his decision in a Feb. 1 letter. His official order was filed Monday, giving potential plaintiffs four months to intervene and existing plaintiffs 30 days to petition for "supplemental relief of damages."

Thrash said he believes the damages can be calculated back to 1995.

To explain how the tax revenue was diverted, Thrash said Hotels.com might sell a hotel room through its website for $100 but it agreed to pay the hotel company $50 for that room. The consumer pays the appropriate Arkansas taxes on the $100 room, and half of the collected taxes go to the hotel company along with $50 for the room. The hotel company then remits the taxes on the $50 it received for the room.

But Hotels.com hasn't been paying the taxes on the $50 it made on that room, even though it collected taxes on that $50 from the consumer, Thrash said.

In essence, he said, the online booking companies have kept tax revenue that belongs to Arkansas, cities, counties, and advertising and promotion commissions.

"They're saying they don't really sell the room; they just facilitate the room," Thrash said.

According to Wyatt's opinion filed Monday, under Arkansas law, the travel companies' "fees" are also part of the tax base because they are "necessary to complete the sale."

"The [online travel companies'] admitted business practice of bundling their fees with the net rate price of the room and in the 'taxes and fees' line item is improper and conceals the true tax amount from the customer and the taxing authority," according to the court filing. "This practice alone renders the OTCs liable for the taxes on the total amount collected from the customer, as exemptions or deductions from the taxable amount are only given for items that are separately stated."

Paul Gehring, assistant revenue commissioner for the Arkansas Department of Finance and Administration, said they were still reviewing the court documents Tuesday. The state has yet to intervene in the case, initially taking the view that the online travel companies weren't "subject to gross receipts and tourism tax levied on the service of furnishing rooms to transient guests," according to an April 19, 2017, opinion letter from the department.

"We have not yet made any decision as to further steps that may be taken," Gehring said. "When there's a ruling in a court case, we take a very close look at what the ruling says before we make a decision going forward."

Jeffrey A. Rossman, a Chicago attorney representing Hotels.com, Hotwire and Expedia, didn't return a voice mail message Tuesday.

The Pine Bluff Advertising and Promotion Commission imposes a 3 percent tax on gross receipts from the rental of accommodations, according to the suit. Jefferson County and North Little Rock each impose a 1 percent tax.

Arkansas also has a 6.5 percent sales tax and a 2 percent hotel tax, according to the National Conference of State Legislatures.

NW News on 05/20/2018

IN THE CIRCUIT COURT OF
JEFFERSON COUNTY, ARKANSAS

PINE BLUFF ADVERTISING AND PROMOTION COMMISSION, JEFFERSON COUNTY, ARKANSAS, AND ALL OTHERS SIMILARLY SITUATED,	)	
Plaintiffs,	)	
v.	)	
HOTELS.COM, L.P.; HOTWIRE, INC.; TRIP NETWORK, INC. (d/b/a CHEAPTICKETS.COM); TRAVELPORT LIMITED; EXPEDIA, INC.; INTERNETWORK PUBLISHING CORP. (d/b/a LODGING.COM); LOWESTFARE.COM INCORPORATED; ORBITZ, LLC; PRICELINE.COM INCORPORATED; TRAVELOCITY.COM L.P.; TRAVELWEB LLC, AND SITE59.COM, LLC,	)	Case No. CV-2009-946-5
Defendants.	)	

MEMORANDUM OPINION IN SUPPORT OF ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

This Court, having considered all briefing and oral argument on the Parties' Cross-Motions for Summary Judgment, hereby DENIES Defendants' Motion for Summary Judgment, GRANTS Plaintiffs' Motion for Summary Judgment, and issues this memorandum opinion in support thereof.

I. Procedural Posture

Plaintiffs Pine Bluff Advertising and Promotion Commission and Jefferson County, on behalf of themselves and others similarly situated, filed this declaratory judgment action against the Online Travel Companies (or "OTCs") on September 25, 2009. The OTCs subsequently moved to dismiss Plaintiffs' action based on alleged want of subject matter jurisdiction, which this Court

denied on January 3, 2011. Thereafter, on April 22, 2011, Plaintiff City of North Little Rock filed a Complaint in Intervention on behalf of itself and other similarly situated Arkansas cities.

Plaintiffs moved for class certification on December 5, 2011. Following a hearing on November 19, 2012, this Court granted Plaintiffs' Motion for Class Certification on February 19, 2013. Upon the OTCs' appeal of that Order, the Supreme Court of Arkansas affirmed this Court's grant of class certification on October 10, 2013. *See Hotels.com, L.P. v. Pine Bluff Adver. & Promotion Comm'n*, 2013 Ark. 392 (2013).

In its Order granting class certification, this Court certified two classes. Class A is comprised of "[a]ll Advertising and Promotion Commissions, of Arkansas Cities, including the Pine Bluff Advertising and Promotion Commission that have or have had tax ordinances pursuant to Ark. Code Ann. § 26-75-602(a)(c)(1), since 1995." (Feb. 19, 2013 Order granting Class Certification at 20.) Class A includes the Pine Bluff Advertising and Promotion Commission and all other Arkansas city advertising and promotion commissions created pursuant to the Advertising and Promotion Commission Act, Ark. Code Ann. § 26-75-601, *et seq.*, that are to receive taxes upon "[t]he gross receipts or gross proceeds from renting, leasing, or otherwise furnishing hotel, motel, house, cabin, bed and breakfast, campground, condominium, or other similar rental accommodations for sleeping, meeting, or party room facilities for profit in such city ..." ("the A&P Tax") (Feb. 19, 2013 Order granting Class Certification at 20); Ark. Code Ann. § 26-75-602(c)(1).

Class B is comprised of "[a]ll counties and cities in the State of Arkansas that have or have had ordinances that provide for a tax on the gross receipts from the sale at retail within the county or city of all items which are subject to the Arkansas Gross Receipts Tax Act (Ark. Code Ann. § 26-52-301), since 1995." (Feb. 19, 2013 Order granting Class Certification at 20.) Class B includes Jefferson County, the City of North Little Rock, and all other Arkansas counties and cities that

have enacted ordinances pursuant to the Arkansas Gross Receipts Act of 1941, Ark. Code. Ann. § 26-52-101, *et seq.*, that impose taxes upon the "the gross proceeds or gross receipts derived from … [the] [s]ervice of furnishing rooms, suites, condominiums, townhouses, rental houses, or other accommodations by hotels, apartment hotels, lodging houses, tourist camps, tourist courts, property management companies, or any other provider of accommodations to transient guests …" ("the City and County Tax"). Ark. Code Ann. § 26-52-301(3)(A)(i).

II. Summary Judgment Standard

Summary judgment is "one of the tools in a trial court's efficiency arsenal." *Smith v. Rogers Group, Inc.*, 348 Ark. 241, 249 (2002). A motion for summary judgment should be granted when it is clear from the pleadings and depositions that there are no genuine issues of material fact to be tried. Ark. R. Civ. P. 56(c); *Smith*, 348 Ark. at 249. Here, all Parties agree that there are no issues of material fact, and thus this Court has made a legal determination based on the undisputed factual record before it, as set forth herein.

The questions before this Court are simple:

(1) Who are the taxpayers for the A&P Tax and the City and County Tax ("the Taxes")? All Parties to this dispute agree that the taxpayers are the OTCs' customers, and thus the answer to this question is not in contention, as further addressed below.

(2) What is the tax basis for which these taxpayers (i.e., OTC customers) are liable? Specifically, are the customers liable for the Taxes upon the gross receipts they pay in order to obtain the rights to accommodations (including the "fees" portion of the total charges and other bundled portions)? As detailed below, the answer to this question is "yes": Under the undisputed facts of this case, the Taxes are and must be based upon the gross receipts/total amounts paid by the taxpayers—without exclusion, deduction or exemption—as no exclusion, deduction, or exemption has been claimed nor applies. Further, no such exclusion, deduction, or exemption

could be upheld in light of the undisputed bundling that the OTCs use in their transactions with the customers.[1]

(3) Under the undisputed facts, including the operative contracts, and Arkansas law as applied to the facts and circumstances at issue in this case, are the OTCs legally bound and liable to collect and remit taxes upon the gross receipts that they charge to and receive from their customers in order for their customers to obtain the rights to accommodations in Arkansas (including the "fees" portion of the charges and all other bundled portions)? The answer to this question is "yes": Under the undisputed facts and law applicable to this case, the identity of the tax collector does not and cannot change the identity of the taxpayer, nor does it or can it change the tax basis for which that taxpayer is liable under Arkansas law.[2] Businesses are free to engage or continue in business and structure their business dealings and operations largely as they see fit within the confines of the law, but private contracts cannot be used to ignore, evade, or violate state law. Arkansas law is clear and unambiguous, establishing that: (a) customers purchasing the rights to Arkansas accommodations are liable as taxpayers; (b) customers must pay taxes on the gross receipts they pay in retail transactions to obtain those rights, including service fees either necessary to obtain the rights to accommodations or any charges that are bundled in the transactions; and (c) tax collectors who collect taxes (regardless of the identity or label they employ) must do so in full accordance with the law. Any person actually collecting taxes as a matter of fact and contract with other would-be tax collectors must comply with the duties

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[1] The OTCs explain and defend their business operations including the rationales for their bundling practices, but none of these explanations can alter the fact that Arkansas law requires separate statements of any supposedly non-taxable charges or else the Taxes are due upon both the taxable and supposedly non-taxable components. *See infra*, pgs. 30-32. There is no dispute that the OTCs bundle the fees that they claim are non-taxable right along with monies that they admit are taxable on the top line of their presentation of charges to the customers. The OTCs further admit to bundling taxes along with private service fees and the second line of their presentation of charges, thus making the Taxes themselves taxable under the mandate of the law. *See infra* Section X.

[2] So-called "breakage" transactions are also encompassed within the tax basis of the Taxes. *See infra* Section VIII.B.

Arkansas law places upon tax collectors, including but not limited to remitting any and all taxes collected.

III. General Approach to Interpreting and Applying Arkansas Tax Statutes and Ordinances

"The question of the correct application and interpretation of an Arkansas statute is a question of law." *Cent. Okla. Pipeline, Inc. v. Hawk Field Servs., LLC,* 2012 Ark. 157, *9 (2012). "The first rule in interpreting a statute is to construe it just as it reads by giving words their ordinary and usually accepted meaning. Statutes relating to the same subject should be read in a harmonious manner if possible. All statutes on the same subject are in *pari materia* and must be construed together and made to stand if capable of being reconciled.... In interpreting a statute and attempting to construe legislative intent, we look to the language of the statute, the subject matter, the object to be accomplished, the purpose to be served, the remedy provided, legislative history, and other appropriate matters that throw light on the matter." *Boothe v. Boothe*, 341 Ark. 381, 385 (2000).

"The basic rule of statutory construction is to give effect to the intent of the legislature." *Ford v. Keith*, 338 Ark. 487, 494 (1999) (citation omitted). "Where the language of a statute is plain and unambiguous, [the Courts] determine legislative intent from the ordinary meaning of the language used." *Id.* "The statute should be construed so that no word is left void, superfluous, or insignificant; and meaning and effect must be given to every word in the statute if possible." *Id. See also Yamaha Motor Corp. v. Richard's Honda Yamaha*, 344 Ark. 44, 52 (2001). Moreover, this Court must not give a statute a meaning that will nullify its operation if it is susceptible to another interpretation. At the same time, this Court will not enlarge, stretch, expand, or extend a statute to matters that do not fall within its express provisions.

Only if this Court determines the language of a statute is ambiguous will it proceed to the next step, which involves applying general principles of statutory construction to the language of the statute to construe any ambiguous language to accurately reflect the intent of the legislature. If

this Court determines that the language of the statute is not ambiguous, there is no room for further construction. It will apply the language of the statute using its ordinary and usually accepted meaning. A statute is ambiguous where it is open to two or more constructions, or where it is of such obscure or doubtful meaning that reasonable minds might disagree or be uncertain as to its meaning. *See Yamaha Motor Corp.*, 344 Ark. at 52. In this case, the Taxes are not ambiguous and can be applied from the plain statutory language and stated purpose.

IV. Arkansas' Local Taxation Scheme Relating to Accommodations

Before determining the scope of the Taxes, the Court first reviews the statutory scheme and the corresponding regulatory rules. It is clear from the plain language of the statute as well as relevant precedent that the Taxes are in fact sales taxes. *See* Ark. Code Ann. § 26-52-301; *Cook v. Sears-Roebuck & Co.*, 212 Ark. 308, 315 (1947) ("We have repeatedly held that the present Gross Receipts Tax Act is a sales tax act."). This point is particularly relevant because much of the OTCs' briefing misunderstands the nature of the Taxes at issue. These Taxes are not net income taxes imposed directly upon a certain category of business such as a motel, imposed for being in business as a motel. Instead, the Taxes are sales taxes that effectively tax the transactions themselves and the customers in those transactions for the full value of those transactions, without deduction for services or other integral amounts. *See Wiseman v. Phillips,* 191 Ark. 63, 73-74 (1935) (discussing that, under a retail sales tax, the merchant must collect and account for the tax as the tax collector, and the tax is required of the purchaser [the customer]).[3]

[3] Though both sides to this dispute cite numerous out-of-state cases, the Court decides this case by directly applying the plain language of the Arkansas Taxes to the voluminous but undisputed factual record before it. Having said that, the Court notes that many of the cases cited by the OTCs are either factually distinguishable because they were decided upon motions to dismiss, or they are legally distinguishable for a variety of reasons such as: (a) the taxes at issue were not "sales taxes"; (b) the taxes were not directly on the customers; (c) the taxes were not upon the "gross income" and "total amounts" without deduction; and/or (d) the taxes did not legally require itemization. In that regard, some of the out-of-state authority cited by Plaintiffs involving sales tax statutes and taxes upon the customers for "retail prices" are more persuasive and analogous to the law and factual record before this Court, such as the sales tax schemes at issue in the Wyoming Supreme Court and Montana Supreme Court decisions and the decision pertaining to Kentucky's sales tax—all of which resulted in findings of liability against the OTCs despite the advancement of many of the OTCs' same arguments here.

In enacting the Advertising and Promotion Commission Act, Ark. Code Ann. § 26-75-601, *et seq.*, the Legislature crafted a simple, straightforward law with the clear and express intent of taxing the full amount a customer pays in exchange for hotel accommodations, without deduction for the seller's markups, costs, services, or fees. The Advertising and Promotion Commission Act authorizes the City of Pine Bluff and others similarly situated (Class A members) to levy a tax on:

> The ***gross receipts or gross proceeds from renting, leasing, or otherwise furnishing hotel***, motel, house, cabin, bed and breakfast, campground, condominium, or other similar rental ***accommodations*** for sleeping, meeting, or party room facilities ***for profit*** in such city or town, but such accommodations shall not include the rental or lease of such accommodations for periods of thirty (30) days or more....

Ark. Code Ann. §§ 26-75-602(a) and (c)(1) (emphasis added). The Act further authorizes Class A members to create their own advertising and promotion commissions to collect (or to appoint an agent to collect) the A&P Tax from "the persons, firms, and corporations liable therefor." Ark. Code Ann. § 26-75-603(a). *See generally* Ark. Code Ann. §§ 26-75-603(b)-(c), -605. In creating the A&P Tax, the Legislature elected to model it upon the Arkansas Gross Receipts Act of 1941. Indeed, the A&P Tax specifically invokes the Gross Receipts Act's provisions regarding rules, regulations, assessment procedures, enforcement, and collection, and provides that these provisions are applicable to the Hotel Tax "so far as practicable." *See* Ark. Code Ann. § 26-75-603(b)(1) ("The rules, regulations, forms of notice, assessment procedures, and the enforcement and collection of the tax under the Arkansas Gross Receipts Act of 1941, § 26-52-101 et seq. and the Arkansas Tax Procedure Act, § 26-18-101 et seq., so far as practicable shall be applicable with respect to the enforcement and collection of the [A&P Tax]"). Moreover, the Legislature provided that liable taxpayers shall pay the A&P Tax to the advertising and promotion commission "in the same manner and at the same time as the tax levied by the Arkansas Gross Receipts Act of 1941, § 26-52-101 et seq." Ark. Code Ann. § 26-75-603(a).

Although the Advertising and Promotion Commission Act does not itself define the terms "lease" or "rent," the Arkansas Gross Receipts Act of 1941 (hereinafter "Gross Receipts Act") does. Ark. Code Ann. § 26-52-103(15) defines "lease" or "rental" as "any transfer of possession or control of tangible personal property for a fixed or indeterminate term for consideration."[4] Further, although neither the Advertising and Promotion Commission Act nor the Gross Receipts Act specifically define "furnish" or "furnishing," and these terms do not appear to be specifically defined elsewhere in the Arkansas Code, the plain, ordinary, and common usage of "furnish" means "to provide or supply." *See, e.g., Ballentine's Law Dictionary* (3d ed. 2010) (defining "Furnish" as "To supply, provide, equip, or fit out.") (accessible online through https://advance.lexis.com); *Merriam-Webster Online*, https://www.merriam-webster.com/dictionary/furnish (visited Aug. 4, 2017) (defining "furnish" as *inter alia* to "supply, give"); *Cambridge Dictionary Online*, http://dictionary.cambridge.org/us/dictionary/english/furnish (visited Aug. 4, 2017) (defining "furnish" as *inter alia* to "to supply or provide something needed").

Under the plain, statutory language of the Advertising and Promotion Commission Act, the breadth of the tax basis is clear. The definitions set forth within the Gross Receipts Act provide:

> "Gross receipts", "gross proceeds", or "sales price" means the ***total amount of consideration, including cash, credit, property, and services,*** for which tangible personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, ***without any deduction for*** the following:

[4] The statutory definitions of "lease" and "rental" accord with the prevailing dictionary definitions of those terms. *See, e.g., Black's Law Dictionary* (10th ed. 2014) (defining "lease" as "[a] contract by which a rightful possessor of real property conveys the right to use and occupy the property in exchange for consideration, usu. rent," and defining "rental" as "the amount received as rent") (accessible online through https://1.next.westlaw.com); *Ballentine's Law Dictionary* (3d ed. 2010) (defining "lease" as "[a] contract for the possession and profits of lands and tenements on the one side, and a recompense of rent or other income on the other" and defining "rental" as "[a] charge made by way of rent") (accessible online through https://advance.lexis.com); *Merriam-Webster Online*, https://www.merriam-webster.com/dictionary/lease (visited Aug. 4, 2017) (defining "lease" as "a contract by which one conveys real estate, equipment, or facilities for a specified term and for a specified rent"); *Merriam-Webster Online*, https://www.merriam-webster.com/dictionary/rental (visited Aug. 4, 2017) (defining "rental" as "something that is rented").

> (i) ***The seller's cost of the property sold***;
> (ii) The cost of materials used, labor or service cost, interest, any loss, any cost of transportation to the seller, any tax imposed on the seller, and any other expense of the seller;
> (iii) ***Any charge by the seller for any service necessary to complete the sale***...

Ark. Code Ann. § 26-52-103(13)(A) (emphasis added).[5]

Together, the City of North Little Rock, Jefferson County, and all other similarly situated cities and counties (the Class B Members) have adopted the Gross Receipts Tax or the City and County Tax. Just like the A&P Tax, the Gross Receipts Act is a simple, straightforward law with the clear and express intent of taxing the full amount derived from all sales to any person from the service of furnishing hotel rooms to transient guests, again without deduction for the seller's markups, costs, services, or fees. *See* Ark. Code Ann. § 26-52-301(3)(A)(1). Ark. Code Ann. § 26-75-502(a) authorizes the City of North Little Rock and other cities similarly situated to levy a tax "on gross proceeds or gross receipts derived from sales, as such sales and gross proceeds or gross receipts are defined in the Arkansas Gross Receipts Act of 1941, § 26-52-101 et seq...." Similarly, the Arkansas Code authorizes Jefferson County and other counties similarly situated to levy a tax upon the gross receipts from the sale of all items that are subject to the Gross Receipts Act. *See* Ark. Code Ann. § 26-74-309(d)(2)(A) ("[C]ountywide tax shall be levied ... on the gross receipts from the sale at retail within the county of all items and services that are subject to the Arkansas Gross Receipts Act...."); Ark. Code Ann. § 26-74-404(d)(2)(A) ("[T]here shall be levied

[5] This statutory definition of "gross receipts" set forth within the Gross Receipts Act accords with the prevailing dictionary definitions of "gross receipts" and "gross proceeds." *See Black's Law Dictionary* (10th ed. 2014) (defining "Gross receipts" as "The total amount of money or other consideration received by a business taxpayer for goods sold or services performed in a taxable year, before deductions.") (accessible online through https://1.next.westlaw.com); *Ballentine's Law Dictionary* (3d ed. 2010) (defining "Gross receipts" as "The entire earnings of a business without deduction; the total as opposed to the net. For the purpose of a sales tax: -- the proceeds of sales of personal property without deduction on account of cost of the property or any other expense whatsoever," and defining "Gross proceeds" as "The entire proceeds. The proceeds of a sale or of a collection without deduction for cost, commissions, or any other expenses whatsoever.") (accessible online through https://advance.lexis.com); *Merriam-Webster Online*, https://www.merriam-webster.com/legal/gross%20receipts (visited Aug. 4, 2017) ("Legal Definition of Gross Receipts: the total amount of value in money or other consideration received by a taxpayer in a given period for goods sold or services performed").

... [a] tax on the gross receipts from the sale of all items that are subject to the Arkansas Gross Receipts Act...."). *See also* Ark. Code Ann. §§ 14-20-112(a)(1)(A)(i), (b)(1) (authorizing a county tax "upon the gross receipts from furnishing of hotel or motel accommodations" in counties that contain a qualifying municipality.... [T]he tax so levied shall be paid by the persons, firms, and corporations liable therefor and shall be collected by the levying county in the same manner and at the same time as the gross receipts tax levied by the Arkansas Gross Receipts Act....").

In enacting the Gross Receipts Tax, the Legislature chose to impose a broad tax

> upon the ***gross proceeds or gross receipts to any person [from the] [s]ervice of furnishing rooms***, suites, condominiums, townhouses, rental houses, or other accommodations ***by*** hotels, apartment hotels, lodging houses, tourist camps, tourist courts, property management companies, or ***any other provider of accommodations to transient guests***.

Ark. Code Ann. § 26-52-301(3)(A)(1) (emphasis added). Per the Gross Receipts Act, the term "sale" includes the "[e]xchange, barter, lease, or rental of tangible personal property." Ark. Code Ann. § 26-52-103(19)(B)(i). As previously discussed, in crafting the Gross Receipts Tax, the Legislature chose to define the terms "gross receipts" and "gross proceeds" broadly and encompasses the "total amount of consideration ... including ... services ... without any deduction for ... [a]ny charge by the seller for any service necessary to complete the sale." Ark. Code Ann. § 26-52-103(13)(A).

Further supporting this Court's construction and analysis of the statutory scheme, the Arkansas Tax Rules provide that "gross receipts or gross proceeds is synonymous with 'sales price' and means the total amount of consideration, including cash, credit, property, and services, for which tangible personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise." GR-3. The Arkansas Tax Rules also state that "any charge by the seller for any service necessary to complete the sale, other than a delivery charge or an installation charge" is included within the tax basis. GR-3. *Accord Travelocity.com, LP v. Wyo.*

Dep't of Revenue, 2014 WY 43, *P53 (2014) ("[G]uests cannot obtain a hotel room through an OTC using the merchant model without paying the price they set, and therefore all charges for services are 'charges by the seller for any services necessary to complete the sale,' which are not deductible from the taxable 'sales price.'"); *District of Columbia v. Expedia*, 2012 D.C. Super. LEXIS 14, *25 (September 24, 2012 order); *Travelscape, LLC v. S.C. Dep't of Revenue,* 391 S.C. 89, 33 (2011).

Neither the A&P Tax nor the City and County Tax discuss taxes on "net" receipts or proceeds. Yet, the OTCs have asked this Court to convert the "gross" taxes at issue into "net" or "wholesale" rate taxes, which it cannot and will not do. Further, there is no express or implied exemption that applies to the OTCs' customers, who are the taxpayers. *See infra* Section X.

V. The Taxpayers Who Are Taxed

One of the first steps in applying or interpreting any taxation scheme is to determine the identity of the taxpayer. Both sides acknowledged the fundamental nature of this "who" question in their briefing and at oral argument. As Plaintiffs' counsel pointed out during oral argument, and as the OTCs admitted in their briefing, the taxpayers here are the OTCs' customers. Thus, these Taxes are properly viewed from the perspective of the taxpayers or OTCs' customers. Notably, not a single taxpaying customer has intervened, objected, or challenged the fact that he/she owes taxes when paying the OTCs for the right to accommodations in Arkansas. Additionally, not a single taxpaying customer has intervened, objected, or argued in favor of a tax exclusion or deduction from the fees they pay to OTCs to secure the rights to Arkansas accommodations.

VI. The Tax Basis of the Taxes

The tax basis for these Taxes is broad. The law clearly provides that the gross receipts or gross proceeds from the sale of the service of furnishing rooms or the rental, leasing, or otherwise furnishing of rooms are taxed. The term "gross" is all encompassing and means without any

deduction under both its plain meaning and Ark. Code Ann. § 26-52-103(13)(A), which provides in pertinent part:

> 'Gross receipts', 'gross proceeds', or 'sales price' means the total amount of consideration, including cash credit, property, and services, for which tangible personal property or services are sold, leased or rented, valued in money, whether received in money or otherwise, without any deduction for the following: ... (iii) Any charge by the seller for any service necessary to complete the sale, other than a delivery charge or an installation charge.

The history of the application of the Taxes over time is also important in determining whether and how they apply to the transactions at issue in this case. As Plaintiffs' counsel articulated at oral argument, there is no dispute that the Taxes apply to customers of brick-and-mortar hotels and travel agencies. Like the OTCs, brick-and-mortar hotels and travel agencies both spend money on marketing, website development, customer service, and other services that make it possible for them to advertise and provide their services to customers via the internet. As the OTCs set forth in their briefing, they too "invest significant financial resources to accumulate and display the content on their websites," which are the same categories of services.

The OTCs' arguments hinge upon the supposedly unique nature of their business model and the effectiveness of their so-called "facilitation" services. But these arguments are largely rhetorical and gloss over or distract from the larger legal points at issue. Arkansas law sets forth an even playing field in the realm of the Taxes (as well as the other privilege and excises taxes). It is not and was not the stated goal of the Legislature to reward supposedly more innovative or "better" businesses with tax amnesty and relatively punish supposedly "worse" or less technological businesses with full Taxes. Instead, Arkansas must have a taxation scheme that is clear, fair, and transparent—which it does. The Legislature stated its purpose to raise revenues from customers to support important governmental functions and, in so doing, to avoid disparate and unequal treatment. The OTCs' interpretation of the law is stilted and would directly contravene the Legislature's stated purpose, as well as the many other provisions of the law. All customers

purchasing the rights to accommodations from "all providers" shall pay Taxes on the gross receipts and total amounts they pay—including "services," "without any deduction," and including "all amounts necessary to complete the sale" and any other bundled amounts (even if not otherwise taxable). To require tax on the gross rate for brick-and-mortar providers of accommodations but some lower amount when the advertising or promotion of such transaction is done by an outside source, as the OTCs argue, would be nonsensical and thwart the Legislature's intent to achieve equal tax application.

The OTCs' arguments do not and cannot reconcile the historic and ongoing application to taxpaying customers who use hotels and travel agencies to book Arkansas hotel rooms and who directly pay those tax collectors the full sales amount, including Taxes on the full amount, without any deduction for the services the brick-and-mortar hotel or travel agency has provided (including advertising, marketing, payment processing, and customer service). As further explained later in the Court's memorandum, there is no logical or legal reason for these Taxes to apply any differently to the customers of OTCs versus customers of brick-and-mortar hotels and travel agencies who choose to "facilitate" their own room reservations. For example, when a customer books a hotel room through Starwood.com (a brick-and-mortar location) or American Express Travel (a travel agency), it is undisputed that taxes are owed on the entire amount of the transaction. The OTCs would have this Court find that when the same booking is done instead through Hotels.com or Expedia.com, the entire amount of the transaction is no longer subject to taxation.

It is not the place or the expertise of taxing authorities nor this Court to determine that Hotels.com is a more innovative business than Starwood or American Express Travel. Undoubtedly, American Express Travel could easily make many of the same claims being made here by the OTCs: "American Express Travel invest[s] significant financial resources to

accumulate and display the content on [its] website." And, American Express Travel could go further and discuss how it uses innovative technology and cutting edge security, maintains customer information, allows for shopping and comparisons across brands of hotels, allows package bookings, displays content, and performs a host of other functions, just like the OTCs claim. But, where is the deduction under the law for their customers paying for all of those services as part of their bookings? As recognized by the Wyoming Supreme Court, travel agent bookings are fully taxed, and no deductions are provided for their services. *See infra* Section VIII. In this case, Plaintiffs have made that same point, and there is no dispute by the OTCs that travel agent services should not be deducted as a matter of fact or practice. In fact, the OTCs themselves conduct some transactions as agency bookings (when customers click "pay later"), and in those bookings full taxes are paid without deduction for the OTCs' services. But, if a customer clicks "pay now," that decision results in the booking becoming a "merchant" booking from which the OTCs will not remit any taxes upon the money they keep from the transaction. The significance of the "pay now" or "pay later" decision was discussed by Plaintiffs' counsel at oral argument:

> And what's interesting is if you go to their website and you go through the booking path ... that we submitted as evidence in this case, a guest can search for comparative shopping ... which hotel they want, compare rates, look at all those things and then get all the way to the end of the process, look at every picture, read every review, do all the things they call facilitation that [they] think is nontaxable; but at the end, if they click the button that says pay later, pay at the hotel, then what happens ... is it is turned into an agency transaction.... The hotel is involved with them on one style of the transaction, and it's fully taxable. But if that guest in the last click decided, no I want to pay now ... All of a sudden, that becomes a merchant model booking, because they're handling the money ... they take their $20 off the top, on the front. They pass on the $80; and then all of a sudden, only $80 is the subjective tax remittance.

(*See* Motion for Summary Judgment Hearing, January 31, 2018, Tr. at 116-117.) As counsel continued and pointed out, there is no provision in Arkansas law that provides if the hotel collects all the money and then pays a commission out to a third party afterward (agency model) that the

total amount collected is taxable, but if some of the fee is taken out beforehand (OTC merchant model transaction) then only the lesser amount remitted to the hotel is taxable. The identity or label of the entity that collects the money from the customer does not change the tax basis. Here, the tax is on the customer and on the gross amount the customer pays for the reservation, without deduction.

The OTCs argue that the Taxes must be strictly construed against the taxing authority. This would only be correct if the Court determined the Taxes were ambiguous, which they are not. As there is no ambiguity to strictly construe against the taxing authority, this Court will apply and enforce the Taxes based on the plain statutory language.

The Plaintiffs also argue for strict construction, but not regarding an ambiguity. Instead, Plaintiffs assert that the OTCs seek what amounts to an exemption from the Taxes, which should be strictly construed against the OTCs. Under Arkansas law, a taxpayer must "establish facts to support a claim for a tax exemption, tax deduction, or tax credit [by] clear and convincing evidence." Ark. Code Ann. § 28-18-313. "Furthermore, there is a presumption in favor of the taxing power of the state, and all tax-exemption provisions must be strictly construed against the exemption. Taxation is the rule, and exemption is the exception." *Holbrook v. Healthport*, 2014 Ark. 146, *10-11. It is clear that each of the transactions at issue in this case is taxable because, in exchange for monetary consideration, the OTCs provide their customers with the right to occupy a hotel room. The Court believes the OTCs are, in addition to other arguments, seeking an exemption from taxation for their "fees." Whether or not the OTCs are seeking an exemption, it is clear that they have not met their burden for any such exemption or deduction to apply.

VII. Arkansas Department of Finance and Administration ("DF&A") Letter and *Leathers v. Active Realty*

The OTCs argue that, to find in their favor, the Court need only consider the DF&A Opinion Letter dated April 19, 2017, or in the alternative, the Arkansas Supreme Court decision in *Leathers v. Active Realty*, 317 Ark. 214 (1994). The Court does not find either to be dispositive or persuasive in this case.

First, the April 19, 2017 Opinion Letter issued by the DF&A is clearly incorrect because it is based on incomplete facts and inapplicable law. The record developed in this case is far superior to the "scenario" upon which the DF&A based its Opinion Letter. Indeed, even when asked at oral argument, the OTCs' counsel could not tell the Court who requested this Opinion Letter, nor could they provide the Court with the factual inquiry underlying the Opinion Letter. Further, during oral argument, the OTCs' counsel assured the Court the request for the Opinion Letter did not come from any of the Defendant OTCs. Taking into account all of these factors, the Court cannot rely on an Opinion Letter that is the result of an anonymous inquiry and does not substantively appreciate or address the realities of the OTCs' business practices, as clearly reflected in the voluminous record before this Court. Further, the Court need not base its ruling on a hypothetical factual scenario when, instead, it can base its decision on the voluminous, fully developed factual record properly before the Court. Furthermore, the Opinion Letter bases its conclusion on a case that has subsequently been abrogated by statutory changes which the Letter fully failed to address. Finally, the Letter failed to address the specific definition of "gross receipts" in Ark. Code Ann. § 26-52-103(19)(A).[6] As such, the Court finds that the Opinion Letter is clearly wrong and, as such, would be an improper basis for this Court's analysis.

[6] Though the Opinion Letter cites to block quotes from the updated statute, the remainder of the letter fails to analyze or even mention the 1995 amendment, ignoring not only the changes to the plain language but also the purpose of these changes.

Second, *Leathers v. Active Realty* is not persuasive or dispositive because the Arkansas Supreme Court decided that case in 1994 under a previous version of the Arkansas Gross Receipts Tax that is not at issue in this case. Plaintiffs' claims only involve the Taxes after the 1995 amendment. In *Leathers*, the Court determined that the 1994 version of the Gross Receipts Tax did not impose tax liability on a business that managed rental houses and townhouses, as the tax only applied to those businesses that were specifically listed in the statute, *i.e.*, hotels, apartment homes, lodging houses, and tourist camps or courts. *Leathers*, 317 Ark. at 216. However, in 1995, at its earliest opportunity following the *Leathers* decision, the legislature amended the Gross Receipts Tax to ensure that the tax applied to all entities that furnish accommodations of any type to transient guests by adding the phrase, "or any other provider of accommodations to transient guests." Ark. Code Ann. § 26-52-301(3)(A). Accordingly, the current statutory language at issue in this case is much broader than that in *Leathers*, thus rendering that case inapplicable to the current controversy.

Indeed, the Court need not guess what the intent of the legislature was in amending the statute in 1995 as the emergency clause of the bill expressly lays out the Legislature's intent:

> It is hereby found and determined by the General Assembly that recent court decisions resulted in disparate treatment by requiring hotels, motels and lodging houses furnishing lodging to transient guests to collect sales tax on such lodging while property management companies which provide similar services are not taxed; that this act is necessary to specify that these provisions of law apply to all entities which furnish accommodations of any type to transient guests and is designed to correct the current unequal treatment. Therefore, an emergency is declared to exist and this act being necessary for the preservation of the public peace, health and safety shall be in full force and effect from and after July 1, 1995.

1995 Ark. HB 1199, § 6. The Legislature clearly desired to prevent disparate treatment between entities furnishing hotel rooms and lodging to transient guests. To find that the reasoning in *Leathers*, namely that the enumerated entities in the statute, as amended, do not encompass the OTCs, would be in direct contradiction to the plain language of the amended statute and also

contrary to the express intent of the Legislature in the wake of *Leathers*. In fact, per the expansive legislative amendment, the OTCs plainly fall within the entities enumerated in the statute as amended as they are plainly "provider[s] of accommodations to [ ] transient guest[s]."

Furthermore, even if the Legislature had not amended the statute with an express purpose, *Leathers* would not be dispositive. It is clear that the factual record in *Leathers* did not include the type of contractual relationship described in the voluminous record in this case—whereby the OTCs contract to collect all monies from the customers (including any and all taxes); use mathematical formulas that, in many instances, apply the tax rate to the full retail charges;[7] and solely maintain the relationship with the customer all the way up until the customer arrives at the hotel. Thus, the Court finds that, even without the 1995 amendment, the *Leathers* case is clearly distinguishable from the facts of this case before it.

VIII. Undisputed Material Facts

While at times the Parties differ in the characterizations or labels they use, the parties agree that the material facts of this case are not in dispute. The Plaintiffs are Arkansas counties and cities that have tax ordinances that impose taxes upon transactions for lodging or accommodations in their jurisdictions, as set forth above. The Plaintiffs consist of individual named Plaintiffs Pine Bluff Advertising and Promotion Commission, Jefferson County, Arkansas and Plaintiff-in-Intervention City of North Little Rock, Arkansas and Class Members ("Members") that fall into the two aforementioned classes ("Classes") that have been certified by this Court and affirmed as such by the Arkansas Supreme Court.

Customers are those interested in purchasing Arkansas accommodations for themselves or for others. The customers obtain the rights to accommodations by purchasing such rights in a

[7] In all cases, the OTCs bundle taxes along with other amounts and create a bundled "taxes and fees" line. Nearly always, this bundled amount approximately equals, if not exceeds, the taxes on the retail price or the total gross receipts.

number of ways: (1) from accommodations businesses located within Arkansas (such as from a local hotel property); (2) from national and international accommodations companies that are not residents of and do not have principal places of business within the state (such as Starwood or www.starwood.com); (3) through in-state and out-of-state travel agents (online or offline); and (4) through for-profit companies that are often self-described or identified by others as Online Travel Companies or OTCs. OTCs maintain travel websites through which the public may book hotel rooms, airline reservations, rental cars, packages, and other travel-related products and services. This case involves only the Taxes on Arkansas accommodations reserved and paid for by customers via the OTCs and/or their websites.[8]

Though characterizations and labels may vary between the Parties, it is undisputed that the OTCs made the decision years ago to engage in business with Arkansas accommodations businesses and with Arkansas travelers (meaning those interested in purchasing the rights to Arkansas accommodations regardless of their point of origination/location). The OTCs advertise, market, and promote travel destinations nationally, including within Arkansas, and the OTCs have handled and continue to handle transactions pertaining to the purchase of short-term accommodations within Arkansas.[9] To purchase a reservation through an OTC, the Arkansas customers must accept the OTC's terms and conditions, as well as the OTC and hotel's cancellation policies and other rules and restrictions applicable to the reservation. The OTCs do not allow customers to pick and choose which provisions to accept or reject—it is an all-or-nothing agreement between the OTCs and the customers. Similarly, with respect to the charges displayed on their websites, there is no mechanism by which a customer can accept and pay for nightly room

[8] Most transactions are accomplished via the internet, though phone calls may be used as a means of booking, confirmation, or payment in some cases.

[9] The exact start dates for hotel booking transactions vary by company, but many of the OTCs began handling bookings more than 15 years ago, according to the record in this case.

charges without also incurring service fees, facilitation fees, and taxes. It is also undisputed that the charges the OTCs present on their websites are "bundled" and do not provide separate itemization for any of the following: (1) the net or wholesale rate; (2) the markup or facilitation fee; (3) the "service fee" or fee that appears on the tax line; and (4) the Tax(es). Items 1 and 2 are bundled together, as are items 3 and 4. In fact, even if a customer calls and requests a breakdown of the charges, the OTCs will not provide it.[10]

To accomplish or conduct their business operations, the OTCs negotiate and enter into contracts with Arkansas accommodations businesses such as local hotels and motels, but these contracts cannot subvert Arkansas law. With the contracts in place, the OTCs possess numerous rights that can vary slightly from year-to-year or contracts-to-contract but which generally, if not uniformly, include the following: (1) the right to access accommodations "inventory"[11] (sometimes through central reservations services or CRSs and/or through third party databases of such inventory); (2) the right to advertise, market, and display such available inventory on their websites, (3) the right to use the trademarks and trade names of accommodations companies (such as Hilton) to advertise, market, and promote such inventory; (4) the right to charge customers on a prepaid basis for all charges for the accommodations, including all applicable taxes; (5) the right to collect from customers (on a prepaid basis) all charges for the accommodations, including all applicable taxes; (6) the right to perform credit card processing and customer service and handle cancellations and refunds consistent with their own policies as well as any applicable policies that

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[10] The OTCs claim that they discuss or explain their charges to customers with language presented on their websites, but this is not an itemization of the dollars and cents for the individual components. The general information provided by the OTCs does not enable any customer to determine how much they are paying in OTC fees, nor does it enable any customer to know the amount they are paying in Taxes. The idea that Arkansas taxpayers are required to pay Taxes to this State and to the local governments within the State but are not entitled to even know what they are paying in Taxes is antithetical to common sense, fundamental principles of tax transparency, and the specific legal and regulatory requirements set forth within the taxation scheme at issue here.

[11] The Court will use the term "inventory" herein. The OTCs' contracts, statements to the U.S. Security and Exchange Commission, and other materials within the record use terms such as "inventory," "allocation," and "allotment" somewhat similarly or interchangeably.

the accommodation businesses may have; and (7) the right to and the role of serving as the one and only merchant of record to appear on the customers' credit card statements for each booking.

In short, the OTCs obtain significant rights over Arkansas accommodations through their contracts. Undisputedly, the OTCs individually and collectively have carried out a substantial number of business transactions relating to bookings of Arkansas accommodations. Notably, the contracts give sole tax collection authority and responsibility to the OTCs such that hotels and other accommodations businesses are not allowed to collect any taxes on the prepaid amounts from the customers, nor are the accommodations businesses allowed to divulge or explain the breakdown of the OTCs' bundled charges—even if a customer requests a breakdown of the charges, as discussed above.

In terms of pricing, while accommodations businesses retain the right to set the wholesale or net rates they will accept or receive some time after the OTC charges and collects from its customers, the OTCs obtain the right to set the final retail price/total gross receipts amount presented and charged to the customers. While the number of rooms or accommodations may vary due to occupancy or the accommodations business's decision as to how much inventory to make available, once the inventory is made available and booked on an OTC website, the OTCs and, in turn, their customers, have binding contractual rights that cannot be simply or arbitrarily taken away. Specifically, barring rare circumstances, the accommodations booked on an OTC website are guaranteed. Even in those rare circumstances where a hotel is oversold, for instance, the accommodations business are generally required to treat the OTCs' customers at least as favorably as—and often more favorably than—their direct customers.[12]

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[12] As addressed in greater detail herein, though the OTCs deny having any control over the rooms they book and deny that their customers even have a right to a room as a result of the transactions on their websites, the evidence demonstrates that this is a litigation "portrayal" or "characterization." The undisputed facts actually demonstrate that the OTCs and their customers have contractual rights that cannot simply or arbitrarily be set aside. As Plaintiffs' counsel pointed out during oral argument, customers do not go to the OTCs' websites, select rooms, pay all charges on their credit cards, then travel to Arkansas, go to the hotel, and merely "hope" that they might possibly have a room

Relevant to this case, both directly and as context, there are five "models" by which hotel rooms are rented, as are outlined in other national decisions, including as contained in the detailed Order from the Wyoming Supreme Court:

> First, the hotel may simply rent the room itself, and the entire transaction is taxed at a maximum of 10% under current rates. Second, a travel agent may book the room for a traveler. In that kind of transaction, called the "agency model," the hotel charges the traveler for the room and pays tax on the entire room rental, but remits a commission to the travel agent. The amount of the agent's commission is therefore taxed, because it is paid from the total room rate. The modified merchant model, the third variant, is similar to the agency model. In it, the customer pays the OTC to occupy a room with a credit card, and the OTC also collects tax on the full amount of the rental. The OTC then remits all of the funds received to the hotel, which pays the OTC a commission, and the hotel pays tax on the entire amount paid by the customer to the OTC.
>
> The controversy in this case involves the merchant model, which comprises the majority of the OTCs' business. In it, the OTC collects the net rate the hotel has agreed upon, the amount of tax estimated on the net rate, and what the OTCs call a "service" or "facilitation" fee. The putative service fee is a markup from the net rate the hotel has agreed to plus the tax on that base rate. The parties sharply disagree as to what this difference should be called because it may affect the outcome, and in an effort to use neutral terminology, we will refer to it as "the markup." If the guest utilizes the reservation, the hotel bills the OTC, and the OTC pays it the net rate plus the estimated tax. The OTC retains but does not pay Wyoming sales tax on the markup. The hotel pays the state or local taxing authority (in this case Wyoming) the tax due on its net rate.
>
> Under the merchant model, the hotel is not informed of the total amount paid to the OTC by the customer for a reservation. The customer is not informed of the net rate the hotel has agreed upon or the amount of tax collected upon it. Without conducting an audit, state and local taxing authorities, including the Wyoming Department of Revenue, cannot determine the basis for the tax collected on each transaction. Only the OTC knows how much its markup is. ...

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waiting for them. Instead, the customers have as a matter of fact and contract: (1) a prepaid booking with a confirmation number, (2) a binding contract with the OTC (which in turn has one with the corresponding hotel), and (3) a contractual guarantee that a room will be available as a matter of fact and contract. If the guarantees and contracts were not in place, obviously many customers would obtain their bookings in other more assured ways. As Plaintiffs' counsel explained, the OTCs' customers are not buying "lottery tickets"; they are booking the right to a room and fully expect to have a room waiting when they show up. The OTCs' characterizations to the contrary fly in the face of common sense, the representations made on their own websites, and the terms of their contracts. Litigation labels, of course, cannot and do not alter the undisputed factual and contractual record.

> The parties agree that although the hotel is obligated by its contract with the OTC to provide a room of a certain type and quality, the hotel assigns the room and charges for any services not included in the rate, including meals, health club access, etc. The OTC has no voice in the room assignment. The parties also agree that the customer can only obtain a refund from the OTC under the merchant model — the hotel cannot grant a refund.
>
> The "opaque" model is also used by certain of the OTCs. This is a variant of the merchant model. In it, the customer does not learn the identity of the hotel until the reservation is made and payment is received. Reservations cannot generally be cancelled and it is nearly impossible to obtain a refund. The OTC remits the net rate and the estimated tax on that amount before the date of the traveler's stay. The OTC has the exclusive right to make exceptions to the no-refund policy. The OTCs retain the markup and do not pay sales tax on it, so the tax issues are the same as with the merchant model, and they will not be discussed separately.
>
> As will be addressed in further detail, the taxing authorities generally argue that tax should be paid to them based on the gross amount the customer pays for a room, while the OTCs contend that the markup is not taxable by the state or local government entity in which the hotels are located because it is a service fee.

See Wyo. Dep't of Revenue, 2014 WY 43 at P9-P15.

It is undisputed that when accommodations businesses in Arkansas handle or "facilitate" their own bookings, they must pay the Taxes not just on the room itself but on services relating to the room rental, including but not limited to advertising, marketing, credit card processing, and customer service. The accommodations businesses generally do not seek nor do they obtain exclusions, deductions, or exemptions for those categories of charges. Similarly, when accommodations businesses work with travel agents, taxes are collected and remitted on the total charges paid by the customer, not the lower net amount retained by an accommodation business after paying the travel agent's commission. *See Wyo. Dep't of Revenue,* 2014 WY 43 at P9. Thus, it is undisputed that in travel agent bookings the law does not permit customers (or anyone else on their behalf) to secure exclusions, deductions, or exemptions for any advertising, marketing, credit card processing, and/or customer services related to the room booking, and instead, Taxes are paid on the total retail price/gross receipts paid by the customer. The fact that in "merchant model"

bookings through the OTCs, the customer pays all money first to the OTC (who passes much of it on to the hotel) versus in "agency" bookings whereby a customer may pay all of the money first to the hotel (who then gives a portion to the agent as a fee or commission) is of no import under the law. That is, the manner or order in which the payments of the gross receipts by the customer are collected from the customer does not alter the tax basis.

The undisputed material facts in this case are based on the voluminous record before this Court, including the OTCs' contracts with Arkansas accommodations businesses, the OTCs' sworn statements to the U.S. Securities and Exchange Commission ("SEC"), and the written and oral discovery produced in this case, including the OTCs' mathematical formulas through which they calculate their "taxes and fees" line item.

A. OTCs' Merchant Business Model[13]

The OTCs sell, rent, lease, or otherwise furnish hotel rooms to customers for profit via a business model termed the "merchant" model. The OTCs' merchant business model is a prepaid model by which the OTCs profit by selling, renting, leasing, or otherwise furnishing hotel rooms to customers at retail prices higher than the wholesale (or net rate) prices for which the OTCs acquire the room inventory from brick-and-mortar hotels. The OTCs' merchant model business practices are nationwide practices that do not vary from jurisdiction to jurisdiction, nor do they, according to the OTCs, differ between the Defendant companies for the purposes of these Motions. Indeed, the OTCs admit that as the merchants of record they, not the hotels, collect the total amount charged for the hotel room from the customer at the time of booking, including taxes. The details of the OTCs' merchant model and the nature of the OTCs' relationship with brick-and-mortar hotels are described in their contracts, SEC statements, and the mathematical formulas that they use to calculate the amounts displayed and charged to customers.

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[13] *See generally* Plaintiffs' Motion for Summary Judgment at 6-12.

1. The OTCs' Contracts[14]

The OTCs take the position that, under their merchant business model, they are merely "intermediaries" who "facilitate" the retail sales of hotel rooms.[15] However, the power of contracts cannot be ignored. Here, two parties reached a meeting of the minds and contracted to define their relationship, which is much more than that of a "facilitator" or even a "broker."[16] These contracts are central to the Court's analysis of the OTCs' merchant business model and the taxability of OTC customers under Arkansas law.

Under their contracts with hotels, the OTCs acquire inventory, room availability, allocation and/or allotments and then furnish that inventory of rooms to customers pursuant to their own contracts with their customers. For example, in a contract between Expedia and Hilton, dated August 22, 2000, the services provided by the OTCs were defined as:

> The services. Web Service Provider is building a proprietary online service which will be accessible via Web Service Provider's website that will enable customers to make Hotel Reservations [which is defined in the contract as- an available room sold or offered for sale at a specified price by an entity]...Customers who use the service for Hotel Reservations will specify Criteria and Web Service Provider, based on its inventory of Available Rooms, will determine whether it can meet such customer's specifications.

Plainly, the "services" the OTCs contract with hotels to provide include the "selling, renting, leasing or otherwise furnishing rooms."

Further, the OTCs' contracts with hotels exhibit the OTCs' complete control of the financial aspects of merchant model transactions. As the merchant of record, the OTC establishes the retail price it charges a customer for a hotel room by being in control of the "fees" and "taxes"

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[14] *See generally* Plaintiffs' Motion for Summary Judgment at 6-12.

[15] Although this Court's decision is not based on this provision, it merits mention that from April 2011 until February 2015, the Gross Receipts Act included a provision that specifically targeted "facilitators." *See* Ark. Code Ann. § 26-52-110(a)(3). This provision is consistent with Plaintiffs' position and this Court's interpretation of the law and was never addressed by the Defendants.

[16] Of course, whether termed as a principal in the transactions or as a broker, the OTCs are liable in either event as undisputed tax collectors that collect and remit taxes in accordance with the law.

it adds to the net rate price for the hotel room. The OTC then charges the customer's credit card for the retail price of the room, which includes the net rate price and a facilitation fee, plus a bundled, non-itemized amount for "taxes and fees." Once the customer pays for a room through an OTC website, the reservation is complete; the customer receives from the OTC a reservation confirmation and, along with it, the right to occupy a hotel room. However, the OTC's involvement does not end there. From the time of credit card payment until the customer physically arrives to check into the hotel, the OTC governs all aspects of the transaction, including reservation modifications or cancellations, refunds, and customer service. In some cases, the customer never shows up at the hotel to claim a room reservation and, thus, the customer's only involvement is with the OTC.

The OTCs argue that, despite the contractual language, all a customer receives from them is a possibility or "expectation" that the hotel "may" provide them with a room when they arrive. The Court finds this position unpersuasive and illogical. If that characterization were true, no customer would ever book through an OTC. Following the money in this case, it is clear that the payment goes from the customer's credit card to the OTC's bank account. Based on the undisputed facts in this case, the only reasonable conclusion regarding who in a merchant transaction provides the service of selling, renting, leasing, or furnishing the room is the OTC. It would be simply nonsensical to conclude that the entity that collects the payment from the customer and provides the reservation confirmation, modifications, cancellations, and customer service does not "rent, lease, or otherwise furnish" the room.

Stepping further into the role traditionally handled by brick-and-mortar hotels themselves, the OTCs contractually assume the business activity of marketing hotel rooms on their websites using the hotel's logos and trademarks. For example, a contract dated March 14, 2011, between Hotels.com and Sohom, LLC, a local hotel in North Little Rock, provides:

> 11. Merchandising. The companies and the affiliates have the right, for the purposes of identifying, promoting, merchandising, and/or obtaining reservations for the Property, to use the name, logos, trademarks, images, and other content from Property's website, providing by Property or otherwise obtained by the Companies with Property's knowledge and/or consent.

In another contract between Expedia and Hilton dated August 22, 2000, Hilton grants the OTCs "a limited, revocable, non-exclusive, non-transferable license for the term of this Agreement to use the Hilton Properties solely for the purpose of developing and maintaining the Web Site." These examples establish that the OTCs are not merely middlemen in these transactions. Instead, the OTCs clearly contract to step into the shoes of the hotel and become the only party who has any contact with the customer from the time of booking until the customer checks into the hotel. During this time, the OTCs are the only entities that collect gross receipts from the customer and provide them with reservations. These functions are precisely what the Legislature intended to encompass in devising the Taxes, and it would result in disparate treatment to find otherwise.

2. The OTCs' Formulas

The factual record before this Court indicates that the OTCs do, in fact, collect taxes from the customer based directly upon the retail price/total gross receipts the customer pays the OTC or generally designed to equal or exceed those amounts.

Indeed, a direct booking through a hotel—from which the taxing authority receives taxes on more than the "wholesale or net" rate—will typically have a total charge that is equal to or within pennies of the total charge on an identical OTC booking. Yet, the OTC always remits significantly less taxes to the hotel than what the OTC collected, and the OTC retains all charges paid in excess of the net rate and taxes on the net rate. In fact, Expedia, the largest OTC group, has mathematical formulas that demonstrate a direct application of the statutorily imposed tax rate to

the margin or mark-up, even though no taxes are ever remitted on that amount.[17] It is clear this practice is longstanding and not isolated. An internal email from Expedia confirms this practice as early as 2002.[18] Further, the corporate representative for Travelocity, another Defendant group in this case, testified that the variable percentage rate used to calculate the company's service fee or facilitation fee usually worked out to be similar or the same as the tax rate for the jurisdiction where the transaction took place. The OTCs admit that they bundle the "taxes and fees" line in their charges in an attempt to mimic the tax amount that brick-and-mortar hotels charge, for the purpose of concealing the wholesale or net rate of the room from the customer. The OTCs did not identify, nor is this Court aware of, any other companies in the hotel industry or otherwise that use governmental tax rates and formulas for calculating and collecting private profits or revenue. This practice clearly constitutes conversion of public tax proceeds into private profit.

3. The OTCs' Statements to the SEC

In addition to the OTCs' business practices as demonstrated through their contracts with hotels and their own websites, the OTCs' statements to the SEC further establish their practice of selling hotel rooms to customers for profit at marked-up retail rates. As Plaintiffs' counsel explained at oral argument, the OTCs' SEC statements—which each Defendant has confirmed are truthful and accurate—describe their business model:

> We sell travel services through five different distribution channels. The primary distribution channel is through our own websites.... Under the merchant model we receive inventory (hotel rooms, airline seats, car rentals ...) from suppliers at negotiated rates. We determine the retail price paid by the customer and we then process the transactions as the merchant of record for the transaction. Acting as a merchant enables us to achieve a higher level of gross profit per transaction.... Integrating merchant inventory with the ESP technology platform has enabled us to create product offerings....

[17] Those formulas were presented to this Court but are being maintained under seal.
[18] As with the formulas, certain internal correspondence was presented to this Court, but it also under seal.

This statement, and others like it, lends further support to this Court's understanding of the OTCs' business model and their liability for the Taxes based on their business practices.

B. Breakage

The OTCs' improper conversion of public tax proceeds is even more blatant in "breakage" situations where customers prepay an OTC the full retail price for a room plus an amount for taxes but, either because of hotel error or because the customer was a no-show, the hotel fails to invoice the OTC for the transaction. Under the OTCs' contracts with hotels, after a certain amount of time has passed without an invoice, the OTCs have no obligation to remit any amount collected. In these "breakage" transactions, the OTCs collect tax line charges from the customer and keep the *entire* amount as profit, remitting nothing—only because the hotels fail to invoice the OTCs. Arkansas law plainly and directly prohibits the OTCs from retaining tax monies that rightfully belong to the taxing entities.

IX. The OTCs' Transactions are Taxable

Based on the foregoing, this Court finds that the OTCs rent, lease, or otherwise furnish hotel rooms in the State of Arkansas and in the jurisdictions of the Class A and B members. The OTCs are therefore liable for the Taxes on all such transactions.

This Court is not alone in its conclusion that the OTCs rent, lease, or otherwise furnish hotel rooms through their transactions. The Supreme Court of Colorado and the Superior Court of the District of Columbia are in accord. *See City and County of Denver v. Expedia.com*, 2017 CO 32, ¶ 24 (2017) ("Although the [OTCs] maintain that even in merchant-model transactions they do not sell, or furnish for consideration, a right to occupy or use the hotel rooms in question, no matter what terminology they may choose to use in describing their transactions, as a function matter that is precisely what they do."); *District of Columbia v. Expedia, Inc.*, No. 2011 CA 002117 B, 2012 S.C. Super. LEXIS 14 at 14-16 (D.C. Super. Sept. 24, 2012) ("Regardless of the particular names

that Defendants choose to attach to their transactions with transients, the Court finds that Defendants' services fall within the services taxable under the gross sales tax law.")

X. The OTCs' "Fees" are Taxable

The next determination before this Court is whether the OTCs' fees are part of the tax base. The OTCs charge "facilitation fees" and "service fees" that they retain as compensation from each hotel room booking made via their websites.[19] As provided above, under Ark. Code Ann. § 26-52-103(13)(A), the Legislature specifically defined "gross receipts" and "gross proceeds" to encompass *all* consideration received, including "any charge by the seller for any service necessary to complete the sale, other than a delivery charge or an installation charge." It is without question that a customer must pay an OTC's facilitation and service fees to complete an online OTC booking. A customer cannot make a room reservation through an OTC without paying the OTC's "fees." Thus, these "fees" stand in contrast to optional charges such as in-room movie rentals that are assessed to a customer only if and when the customer rents a movie. Put another way, under Arkansas law, the OTCs' "fees" are legally part of the tax base because they are "necessary to complete the sale."

Further, the OTCs' admitted business practice of bundling their fees with the net rate price of the room and in the "taxes and fees" line item is improper and conceals the true tax amount from the customer and the taxing authority. This practice alone renders the OTCs liable for the Taxes on the total amount collected from the customer, as exemptions or deductions from the taxable amount are only given for items that are separately stated. *See* Ark. GR-3. Further, tax transparency is imperative, and clearly the OTCs' practice of bundling charges conceals from the government, the customers, and the courts the tax amounts (or "tax recovery charges") collected

[19] As set forth above, there is no legal distinction between the services hotels, travel agencies, and OTCs provide to consumers such that the OTCs' services should be exempt from taxation and the others' not.

and ultimately retained by the OTCs. This violates Arkansas law. Notably, the OTCs have not provided any explanation as to how their "bundling" practices do not subject them to liability for the Taxes on the total amount charged to the customer.

Lastly, the OTCs argue that the "net rate" agreed to between the OTC and the hotel constitutes the taxable amount. This simply does not harmonize with the evidentiary record before this Court. First, the OTCs argue that they bargain for the net rate in their contracts with hotels, and thus the net rate should be the "sales price" of the transaction. However, as the OTCs themselves have pointed out, their contracts with hotels do not amount to a "sale" of a hotel room. The true sale—the transaction for the right to occupy a hotel room—occurs between the customer and the OTC. Thus, the total amount paid in the transaction between the customer and the OTC is the proper tax base. Second, even if one viewed the tax base as being strictly what the *hotel* receives, the tax base would still equal the total amount charged to the customer because the hotel not only receives the net rate from the OTC but also the valuable services that the hotel would normally provide that the OTC contractually assumed. No matter how the transaction is analyzed, the tax base is the total value of the transaction, *i.e.*, the gross receipts.

XI. Supplemental Relief

Declaratory judgment actions are governed by Ark. Code Ann. §§ 16-111-101, *et seq.* Under the Uniform Declaratory Judgments Act, this Court is permitted to award damages as supplementary relief pursuant to Ark. Code Ann. § 16-111-108, which reads:

> Further relief based on a declaratory judgment or decree may be granted whenever necessary or proper. The application therefore shall be by petition to a court having jurisdiction to grant the relief. If the application be deemed sufficient, the court shall, on reasonable notice, require any adverse party whose rights have been adjudicated by the declaratory judgment or decree, to show cause why further relief should not be granted forthwith.

Further relief, which is authorized whenever necessary or proper, may include an award of damages. *Hanjy v. Arvest Bank*, 94 F. Supp. 3d 1012, 1031 (E.D. Ark. 2015).

This action is one for declaratory judgment. The Court has made its determination and declares that the OTCs are liable for the Taxes in the class member jurisdictions on the total amounts they collect from their customers. Having made this determination, it is proper for the Court to consider necessary and proper supplemental relief prior to entry of a final order and judgment. To that end, the Court has established guidelines in its Order filed herewith to allow named and putative class members to seek such supplemental relief.

IT IS SO ORDERED.

HONORABLE ROBERT H. WYATT, JR.
JEFFERSON COUNTY CIRCUIT JUDGE

5-14-18

DATE

IN THE CIRCUIT COURT OF
JEFFERSON COUNTY, ARKANSAS

PINE BLUFF ADVERTISING AND PROMOTION COMMISSION, JEFFERSON COUNTY, ARKANSAS, AND ALL OTHERS SIMILARLY SITUATED,	)	
Plaintiffs,	)	
v.	)	
HOTELS.COM, L.P.; HOTWIRE, INC.; TRIP NETWORK, INC. (d/b/a CHEAPTICKETS.COM); TRAVELPORT LIMITED; EXPEDIA, INC.; INTERNETWORK PUBLISHING CORP. (d/b/a LODGING.COM); LOWESTFARE.COM INCORPORATED; ORBITZ, LLC; PRICELINE.COM INCORPORATED; TRAVELOCITY.COM L.P.; TRAVELWEB LLC, AND SITE59.COM, LLC,	)	Case No. CV-2009-946-5
Defendants.	)	

ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

This Court, having considered all briefing and oral argument on the Parties' Cross-Motions for Summary Judgment, and for the reasons further explained in the Court's Memorandum in Support of Order on Cross-Motions for Summary Judgment hereby DENIES Defendants' Motion for Summary Judgment and GRANTS Plaintiffs' Motion for Summary Judgment. The Court finds and orders as follows:

(1) The OTCs are liable for the taxes established in Ark. Code Ann. § 26-75-602(c)(1) and Ark. Code Ann. § 26-52-301(3)(A)(i) on the full gross receipts they receive from customers, consistent with this order. This finding applies to their past transactions, current transactions, and any other transaction conducted under the merchant business model.

(2) The named class members have 30 days from the date of this Order to petition for additional relief permissible under the law relating to past taxes owed, supplemental relief or otherwise, including but not limited to amending the Complaint.

(3) If the Court rules that supplemental relief shall be granted, the OTCs will have 30 days to provide all transaction data for the named class members who filed a petition for supplemental relief, including data from which breakage amounts can be calculated, for the time period and transactions at issue so that a calculation of the amounts due, including penalties and interest can be completed.

(4) Notice shall be given to all class members of this finding of liability and their right to intervene for the purpose of determining damages. The unnamed class members shall have 120 days from the date of this Order within which to intervene as individual plaintiffs, in order to pursue supplemental relief pursuant to the Court's declaration of their rights and to do so efficiently and in a consolidated manner to avoid duplicative discovery and unnecessary utilization of court resources.

(5) If the Court rules that supplemental relief shall be granted to the interveners, the OTCs will have 30 days to provide all transaction data for the individual intervening class members, including data from which breakage amounts can be calculated, for the time period and transactions at issue so that a calculation of the amounts due, including penalties and interest can be completed.

(6) Once the damages have been calculated, the parties are ordered to proceed with mediation with Mr. James W. "Jim" Tilley of Watts, Donovan and Tilley, 200 River Market Avenue, Suite 200, Little Rock, Arkansas 72201 (501) 372-1406 within 45 days in order to reach a determination on the final amounts owed. The fees for the mediation shall be split equally between the parties.

(7) This Preliminary Order is not final and will be held open consistent with and to allow for further development of these proceedings consistent with the steps outlined above. This Court accordingly retains jurisdiction to determine any and all further and supplemental relief appropriate.

IT IS SO ORDERED.

HONORABLE ROBERT H. WYATT, JR.
JEFFERSON COUNTY CIRCUIT JUDGE

5-14-18
DATE