WHITE PAPER – TOT Disclosure Issues and Legal Implications

29 December 2007 ***Original (1st) Draft*** **Local Issue Briefing Paper (LIBP) pages = 26**
28 January 2008 ***Updated***
30 January 2008 ***Revised-Updated***
01 February 2008 ***Expanded***
17 February 2008 ***Recently Received Info Added / Policy Direction Reflected***
04 March 2008 ***Revised Focus draft to Highlight Disclosure Concerns***

California Association of Realtors® – Legislative Staff
California Association of Realtors® – Legal Staff
California Association of Realtors® – Executive Staff

Transient Occupancy Tax (TOT)-
Collection Practices in Placer County

DRAFT VII ------- Not For Distribution

"Deep Background & Disclosure Concerns Edition"

The following IBP is for internal use/study only.

This draft LIBP is not intended to be considered or used as a legal brief, is not drafted by an attorney-at-law, does not represent a formal legal opinion on the case or its merits, and in no way can be implied, inferred, construed, or cited as a legal position or advice. Its sole purpose is to inform committee discussions and spur additional research and debate.

This draft is subject to revision as information, opinion, or policy direction warrants.

Issue:

Placer County is pursuing an aggressive programmatic approach to the collection of perceived past TOT underpayment. Concurrently, they are attempting to establish a particular but broad interpretation as to what constitutes TOT taxable events. Property managers are reporting receiving antagonistic audit notices from the county; notices intended to collect TOT funds presumed to be due via the broad inclusive definitional decision rendered by county staff. The window for response to the demand letter is very short (7 days). The short-term revenue implications for the county are clear, but is their case compelling/legitimate? Research into the topic also exposed significant concerns related to potential disclosure requirements at-sale. The implications for buyers, seller, their professional representatives, and escrow/title processing are many and far-reaching.

CAR Relevant Requests for Commentary:

1. Request that CAR legal Division & Standard Forms to look into the matter of a "Tax Clearance Certificate" as provided for in state law (ref. Assembly Bill 1916 of 2004, Revenue & Taxation Code, Section 7280 - 7283.51) and opine as to the disclosure ramifications as well as potential expanded liability exposure and how to best mitigate it.

2. Consider pursuit of state-level legislation to amend the Revenue & Tax Code in ways that will protect private property from undue title burden, reduce any liability exposure for real estate professionals, and constrain the number or type of taxable events. Noting that a legislative remedy, i.e., sponsoring the introduction of a bill that would clarify (restrict) the application of TOT taxation by local jurisdictions to reflect 'room rate' actually paid, carving out the many auxiliary charges that are currently asserted by the county to be TOT taxable (e.g., cleaning fees, management fees, reservation and processing fees…), would face stiff opposition by various interest groups in Sacramento.

State-Level Summary - Legislative Matters:

The California Lodging Industry Association sponsored legislation in 2004 that amended the State enabling act regarding local TOT. The bill, Assembly Bill 1916, was something of a two-edged sword for our industry, adding some clarity to the application parameters of TOT, but also muddying the waters related to title transfer and whether TOT matters run with the proprietor (operator) or with the property. AB 1916 was signed into law by the Governor in September of '04, thus taking effect on 01 Jan. 2005. Three amendments to the TOT statute were achieved. On the 'plus' side, the bill streamlined the "government exemptions" provisions, requiring a standardized form for reporting rentals exempt from local TOT taxation, and articulating what would be deemed acceptable documentation to demonstrate that the exemption was legitimate. It should be noted at this point that the State enabling statute does not require that a local taxing authority provide exemptions for any subdivision of government, but rather allows each local TOT ordinance to include or exclude one or more levels/units of government, on official business, to be exempted from TOT collections. Some cities and/or counties have broad exemption policies, to include local government, California state government, other U.S. states' government workers, and foreign government representatives from around the globe. Placer County has elected to include in its Code only one exemption, "…any officer or employee of a foreign government who is exempt by reason of express provision of federal law or international treaty." (ref. Sec. 4.16.040 of County Code). Given the strict construction of this exemption, it is so narrow that only a subset of foreign government representatives would even be eligible (due to formal national or international agreements that would supercede county code anyway). Thus, for all practical purposes, there are no exemptions that would be germane to one's day-to-day operations.

Another AB 1916 amendment on the plus side of the ledger was the addition of a statute of limitations for back tax collections. State R & T Code now includes Section 7283.5, which establishes a four-year window of opportunity for local government to commence formal actions to capture due but unpaid TOT taxes. Of course, this limitation does not apply if the local government can prove that fraud was involved (thus becoming a criminal proceeding, not a civil matter). This is of value to the short-term rental owner and/or property manager, for as long as one makes a good faith effort to collect and report TOT tax activity, the liability exposure for past years activities and possible underpayment seems to be well bracketed by this four-year window for the county (or city) to initiate a claim. On the negative side of the ledger in regard to this

same provision, the statute also carves out “failure to file TOT tax returns” from the four-year timeline. As such, a second homeowner who has rented his/her unit at some point in the past, unaware of the County Code regarding TOT collections, remains exposed beyond the four-year back tax collection limitation.

The third, and perhaps most concerning amendment to the state statute, involves “tax clearances” as articulated in R & T Code Sec. 7283.5. This provision allows, but does not require, a prospective purchaser of a property that was/is subject to the local TOT code to request a TOT Tax Clearance Certificate from the taxing entity (city or county). The government then has ninety days to either issue the certificate that the property is clear of any back TOT tax liability, or request within that same ninety-day window that records be made available for review/audit. The audit process itself runs within that ninety-day window. At the conclusion of the allotted timeline the governmental entity must either: issue the clearance certificate; issue a certificate declaring the outstanding amount of TOT tax due and the time period reflected in this claim; or withhold the certificate by claiming that the records are insufficient to allow for an audit. On the “up side”, if the prospective purchaser requests such a certificate then the county is obliged to act, with the information provided (or failure to comply on the county’s part) being treated as reliable for the purposes of the new property owners’ tax liability. This provision answers an important potential liability question for the buyer. On the “down side”, if the purchaser does not request such a tax certificate, and monies were indeed due to the city or county as a byproduct of short-term rental activities by the previous owner, then the new owner appears to be liable for the uncollected back TOT taxes. From our industry’s prospective, this creates a significant potential liability for single-family residences and multi-unit properties that might have been offered as short-term rentals as an incidental aspect of owning a second home. In resort areas such as ours, this becomes a real issue. It would seem that the law was written with the full-time proprietor (e.g., hotel or motel owner/operator) in mind, yet it is structured in such a way as to capture the individual second homeowner as well. Questions regarding seller’s disclosure obligations are made all the more complex in a resort second-home dominated community. Somewhere between 60-75% of homes in the region have been identified by U.S. Census surveying as being secondary dwelling units. The liability implications regarding sales of homes in resort communities with such TOT provisions in-place becomes significant and concerning.

Apprehension related to TOT applicability and liability exposure arises when the state statute casts such a wide net. Again, a primary concern revolves around the nature of the use, with hotel-type commercial uses being the apparent focus of much of this legislation, which may be reasonable and appropriate, but in using broader more open-ended application language it has the net effect of including and thus burdening the less-sophisticated incidental operator, namely the second-home owner. While the law makes it plain (black and white), if you rent a property for 30 consecutive days or less, for which any sort of remuneration is expected, and in whose jurisdiction a TOT Ordinance is in-force, then occupancy taxes are due. The reality is that two very different forms of short-term rental activity are being treated identically, the commercially dedicated use of a property as a hotel, verses the individual private

homeowner who might rent the unit sporadically to offset some of the costs associated with second homeownership. One type of use is principally a commercial revenue-generating endeavor, while the other form of use is principally as a vacation home (residence) for the owner. This commercial venture vs. residential use distinction (primary purpose to rent for short-term vs. primary purpose is for short-term owner occupancy, with outside rental activity being incidental to its primary usage) is not made in the code, but has a unique and disadvantageous impact on resort regions such as ours.

Also deeply concerning is the fact that these 2004 revisions to State law appear to establish that TOT liability can run with (attach to) the property, as opposed to being a solely proprietor/operator held liability. TOT is something of a business activity tax, yet is being applied as something of a global special use tax on real property. The implication of this state-of-affairs makes it unclear as to whether various taxpayers 'right to vote' initiatives would apply (Prop. 13, 62, and 218). Once again, what intuitively "makes sense" in reference to a hotel-type commercial property seems out-of-place and unduly burdensome in regard to the second home incidental rental activity of a previous owner. When considering the state regulatory restrictions on encumbering real property, it would seem that R & T Code Sec. 7283.5 contravenes the intent of the State Constitution. In the text of "A Planner's Guide to Financing Public Improvements" it is stated that, "(t)he transient occupancy tax [TOT] is a popular type of excise tax available to both cities and counties." This becomes a significant point when one considers the nature and intent of excise taxes as a class. Again citing from the Planner's Guide, it explains that,

> "Although the California Constitution does not expressly prohibit multiple taxation, the provisions of Section 1 of Article XIII of the California Constitution, requiring that all property shall be taxed in proportion to its value, have been construed in a number of [court] decisions to prohibit the multiple taxation of property…" (Opinion #19078 of the California Legislative Counsel). Continuing, "In the words of the U.S. Supreme Court, an excise tax is 'a tax imposed upon a single power over property incidental to ownership' (Bromley v. McCaughn (1929) 280 U.S. 124). It is not a property tax. Instead, it is a tax levied on one of the incidents of land ownership; **not on the land itself nor on land ownership per se.**" (emphasis added)
>
> "…At the same time, since it is being imposed on a single activity or privilege of ownership, an excise tax must be collected from the person involved in that activity or privilege (not necessarily the property owner). …Another interpretation suggests that Proposition 218 may actually prohibit certain excise taxes. The reasoning is as follows: Proposition 218 provides that those taxes, assessments, fees or charges which may be assessed 'upon any parcel of property or upon any person as an incident of property ownership' are limited to ad valorem property taxes, special taxes, assessments, and fees or charges (Section 3, Article XIII D, California Constitution)."

As can be ascertained from reviewing the material cited immediately above, the law in these taxation matters is not as clear-cut as one might have hoped or believed. This is demonstrated by the fact that Prop. 62 was an attempt to close some of the "loopholes" in Prop. 13, and more recently Prop. 218 was intended, at least in part, to better define the limitations imposed by Prop. 62's passage. Reasonable people can read the statutes and come to very different conclusions. Thus, it is oftentimes left to the courts (or additional initiatives) to set or correct the record as to how a given law is to be interpreted and applied.

Discussion - General:

California's tax structure has been broadly divided into two classes or types, "special" and "general". TOT taxes can in point of fact be either a general tax or a special tax, depending upon how it was approved by the electorate (simply majority or super-majority), and based on the allowable uses of the funds collected (general fund for multiple uses or dedicated/earmarked for specific/limited uses). General taxes require a simple majority affirmative vote to achieve passage (50% + 1), and are to be placed before the voters during a regularly scheduled general election. Special taxes are imposed for specific purposes, with revenue collected being restricted to use in the furtherance of these enunciated purposes (whether held in the Gen Fund or a separate account), and require a so-called "super-majority" of affirmative votes to achieve passage (2/3rds of those casting ballots).

Transient Occupancy Taxes (TOT), commonly referred to as a "bed tax", "room tax" or "hotel tax", have become an increasingly popular way for local government to backfill its General Fund in the wake of Prop. 13, Prop. 62, the ERAF Shift, and Prop. 218. Part of its appeal to both local government and the electorate is that TOT taxation is viewed as a tax "that someone else pays", namely tourists. Of course, this overly simplistic characterization is not to suggest that our elected officials or the voters have disregarded or discounted the impact any such tax scheme has upon the region's economy and its competitiveness in the marketplace. One recurrent theme in the local dialogue regarding TOT has been the threshold or tolerance level the consumer has for the imposition of such taxes. The "decision space" for TOT rates to act as an effective revenue generator while retaining the destination's attractive position in a highly competitive market is a universally acknowledged issue of importance. Recognition of this delicate balance has been articulated by local elected officials, hotel operators, the broader business community, and the public at-large. Given the extremely fluid/dynamic economic environment in which we find ourselves today, the issue of TOT rates and their application must continuously be reviewed. This ongoing dialogue is critical to ensure that our region does not 'lose' needed revenue by pushing the rate too low, nor lose its customer base and do damage to our tourism/recreation-based economy via driving the rate too high. Striking this balance is a hotly contested matter; one without clear-cut answers. Around the state, TOT rates range from eight percent (8%) to fifteen percent (15%). According to the California Lodging Association, the state average is a 10% TOT rate, which brings in more than $1 billion dollars a year in revenue to cities and counties throughout the state. Across the nation, the TOT-type tax rates vary more widely. As of 2004, the reported national average TOT-type tax

was 12.4%, as levied on short-term lodging occupants. Additionally, the formula used for TOT collections, i.e., which transactions are TOT taxable events and which are not, also differs significantly from place to place. The one constant in all of this is that, wherever TOT taxes are imposed, they become an important (relied upon) source of revenue for local governmental operations.

Discussion - Regional:

Placer has a countywide 8% TOT tax rate, with an additional 2% overlay in the High Sierra. This form of taxation does require voter approval. As such, the voters of Eastern Placer County have "self-imposed" a 10% transient occupancy tax rate. Placer County structured its TOT to be a "general tax"; thus, requiring only a simple majority to achieve passage. This also allows the monies received to be entered into the county's unrestricted General Fund. The Tahoe region 2% addition was presented to the voters as a "general tax". There was a great deal of discussion and debate prior to the formulation of the local measure as to whether it would be superior to utilize special tax provisions or a general tax approach. The major benefit of going with a special tax designation would have been to guarantee that the revenue generated by the 2% overlay would "stay home", and that these monies would only be used for those purposes designated in the proposal/measure. The main liabilities associated with going down the special tax road were the super-majority vote required to pass the measure, along with the relative inflexibility of use of funds collected. The general tax approach was selected due in large part to the more manageable simple majority affirmative vote requirement to achieve passage. While there was some "risk" of allowing this 2% tax to be placed in the county General Fund for discretionary use by the supervisors, informal agreements as well as formal contracts for services in the Tahoe region reduced the likelihood of this revenue being 'lost' to the General Fund. Polling and surveys were conducted to determine both the potential for passage at various rate points and to discern if the 2/3rds threshold could be obtained. The super-majority vote required for imposition of a special tax was too close to the margin, and as such a general tax was proposed.

Coincidental Legal Actions:

In 2004 the City of Los Angeles filed a lawsuit against some 15 (updated, now 16) Internet-based travel companies, contending that companies such as Priceline, Expedia, Hotwire, Orbitz, Travelocity, and Hotels.com were collecting TOT from its customers at the "retail" rate/price for a room, but only remitting the "wholesale" price TOT charge to the county based on what the company paid for the block of rooms secured at a deeply discounted rate. The City of San Diego filed a similar case in the San Diego California Superior Court (ref. City of L.A. Case No. BC 326693, City of San Diego Case No. GIC 8611117 – Judicial Council Coordinated Proceedings No. 4472). At some point during these filings the City of L.A. asked the court to consider their suit as a "class-action" case.

It is alleged that these on-line operators were charging the customer the TOT applicable to the room rate paid by the consumer, then remitting only the amount paid by the on-line company for its initial buy, and pocketing the difference. Unfair competition in these

companies' business practices is also alleged (Cal. B&P Code, Section 17200, et seq.). While the outcome of these claims are still in question, it appears that one argument being formed is that the on-line proprietor paid the appropriate/applicable rate, and any difference between TOT collections from wholesale to retail rates are reflected in their cost of doing business. Another possible course of argument that might be forwarded would be to suggest that the on-line company is simply the middle-man in the transaction, and that any deficiency in the tax rate collected should be directed to the actual consumer who is liable for the tax, and/or the actual property at which they stay. Further, representatives for the Defendants have argued that a class-action lawsuit would not be appropriate, given the variability between and among local TOT ordinances (e.g., what activities are included or excluded, the procedures used for collection, the process for administrative adjudication applied to those out of compliance, the amount of tax imposed, general vs. special tax designations depending upon the particulars of a given jurisdiction's approach…).

Interestingly, it was during this same time period, 2004, that the Placer County Executive Office initially recommended that an internal audit be conducted on TOT collections. Also of interest is the fact that in June of 2007 The League of California Cities (state level lobbying organization for a number of cities across the state) released an update on this litigation, which included a call to action, saying, "(i)f the court declines to grant class action status, individual cities may need to act very quickly to preserve their rights to recover all past unpaid taxes, and to avoid the 4-year statute of limitations in Revenue and Taxation Code section 7283.51. Therefore, we recommend that you bring this matter to the attention of your city attorney and your TOT auditor as soon as possible." Coincidentally, the County of Placer amended its TOT Ordinance in June of the same year. It is unknown if the California counties legislative/lobbying organization (California State Association of Counties) was keeping its members informed as to this city matter; nor is it known, irrespective of state-level outreach, if Placer County was aware of these proceedings. Nevertheless, given the significance of TOT resources to county as well as city General Fund balances, it seems reasonable that to assume that county officials would be interested in court proceedings that attempt to perfect a claim that additional TOT revenue is due.

The situation playing out in Southern California is different in many ways from what has been occurring in our High Sierra communities. Fortunately, in our situation there are no known allegations of operator/proprietor retention of TOT revenue in whole or in part. Yet, in some respects similarities can be teased out of the circumstances that evolved from 2004 to the present. The overarching question is if local government has been "underpaid" for past TOT collections. Associated with this question is the issue of how the local jurisdiction so affected can better establish its position regarding taxes due, past and present. Of course, embedded within both issues/questions relates to just what is a TOT taxable event. Clearly, the particulars of the So. Cal. cases and our High Sierra experience are dissimilar; however, some of the global policy and legal issues in play might well be applicable to how things are done locally.

Local Issue Summary:

The TOT collections policies and procedures revisions were driven (locally) by an internal audit, requested by the county's Executive Office, purportedly to assess the level of compliance with the county's Uniform Transient Occupancy Tax. According to a Memo to the Board of Supervisors from Rich Colwell (Chief Assistant County Executive Officer), dated May 8, 2007, as a result of the aforementioned audit, "...the Auditor-Controller made recommendations to update certain areas of the Ordinance that were not clearly defined." Three sections of the county's Code associated with TOT (Article 4.16) were considered for revision (*italics reflects 2007 amendments*):

(1) Section 4.16.020 "Definitions" was amended to read, " 'Rent' means the consideration charged, whether or not received, for the occupancy of space in a hotel valued in money, whether to be received in money, goods, labor or otherwise, including all receipts, cash, credits, property and services of any kind or nature without any deduction therefrom whatsoever. *Rent does not include any additional items included in a special package rate, such as ski passes, or other recreational or other activity or additional service, as long as the operator separately states the rent and tax from other amounts on all receipts and books of record. If additional benefits or services are not stated separately as indicated above, the entire amount shall be presumed to be rent.*"

(2) Section 4.16.070 "Reports and Remittances" was amended to read, "C. For the purposes of this section, 'on or before' shall be interpreted as (1) hand delivery; or (2) postal delivery of a properly stamped and addressed envelope containing the return and full amount of the tax to the United States Postal Service. Delivery to the Postal Service must be verified by the cancellation by the Postal Service showing a postmark date no later than midnight on the day the tax is due. *If the due date of the tax falls on a Sunday the tax due date shall be the next business day (excluding federal holidays.)* Private postal meter strips and dates shall not be considered evidence of delivery to the United States Postal Service."

(3) Section 4.16.100 "Determination of tax by tax administrator upon failure of operator to collect and report tax -- Notice and Hearing" was amended to read, "B. For purposes of determining the liability of any operator failing or refusing to file a return, there shall be a rebuttable presumption that the liability is the same as in the *maximum liability* quarter for the previous *fiscal* year."

The major point of contention involves the definition of "rent" for the purposes of tax collections. One might concur with the internal auditor's initial finding that this section of the code was unclear. Perhaps, better stated, the section of the code defining rent was far too vague to be adequately understood or properly applied. The overly broad definition in the Code was worthy of amendment to introduce greater clarity. The 2007 amendments to the definition of rent added a degree of clarity and precision to the scope of taxable events within the context of rental charges. Taken at face value, many a property management professional viewed the amended language as simply adding clarity and codifying the long-standing accepted standard practice in the county regarding TOT collections, better articulating areas of allowable exclusion from taxation. This stance was reinforced by the fact that past audits by the county in which items

such as cleaning fees were called out as non-taxable for TOT purposes had passed muster (deemed to be a clean audit – without error or back TOT taxes due). Members who were aware of the mid-year '07 TOT ordinance revisions, and had read the code in its present form, came away with an understanding (interpretation) that items such as 'cleaning fees' were indeed "exempt-able" under the definition of "rent" as revised. A well-informed, long-standing member, and politically involved professional property manager contacted the Board to ensure that we had the current version of the County Code, for he felt that this language expressly allowed for such line-item exemptions to TOT taxation. In specific, the amended code section was referenced in which, "…Rent **does not include** any **additional items** included in a special package rate, such as ski passes, or other recreational or other activity **or additional services**, **as long as** the **operator separately states** the rent and tax from other amounts on all receipts and books, of record. If additional benefits or services are not stated separately as indicated above, the entire amount shall be presumed to be rent." (emphasis added) It was/is his considered opinion that the strength of the language in the ordinance itself, which expressly allows "additional services" to be carved out of the TOT taxation scheme, if itemized, to be inclusive and permissive. This member was then directed by the advocate to refer to the correspondence from the county, dated December 26, 2007, in which the county staff announces its "determination" that items such as 'cleaning fees' are not to be excluded from TOT taxation. After reviewing the December letter, he questioned how a staff generated correspondence could so radically alter the ordinance without being subject to formal public scrutiny (hearings). His question is a valid one.

The aforementioned letter of determination regarding 'rent' went out from Placer County on December 26, 2007, directed "To All Transient Occupancy Tax Certificate Holders". This TOT update letter goes to the heart of the county's attempt to expand (or perfect its claim to) the number or type of TOT taxable events. It says, in pertinent part, that,

> "…it has been **determined** that **any** 'room-related **fees and services necessary to occupy space**' **is subject to TOT tax**. Per the Ordinance, the definition of rent 'means the consideration charged, whether or not received, for the occupancy of the space in a hotel valued in money, whether to be received in money, goods, labor or otherwise, including all receipts, cash, credits, property and services of any kind or nature without any deduction there from whatsoever.' **Other receipts and services subject to TOT tax would include, but is not limited to, resort fees, reservation fees, gratuity fees, energy surcharge fees, maid fees, and cleaning fees**." (emphasis added)

To be clear, this interpretation of the Code was *not* articulated by the Board of Supervisors in their proceedings, nor referenced in any ballot measure that went to election as being accurate, complete, or applicable to TOT collections activities. The Internal Audits Division of the Placer County Auditor-Controller's Office is identified as the party generating this determination. One might forward an argument that this approach to revenue enhancement is over-inclusive as a matter of policy, overreaching in its application, and at odds with the language and intent of both our local TOT Ordinance (Sec. 4.16) and the State's enabling act (Revenue & Taxation Code, Section

7280 - 7283.51). In any event, the letter of notification establishes that, "effective January 1, 2008, if you are not already doing so, you must collect and remit tax on all room-related fees and services." An unanswered question directly pertains to this Jan. 01, 2008, "effective date"; specifically, does this provision relieve the operator of prior claims by the county of TOT underpayment? It might appear to afford such latitude. One could argue that if it does not, by generating yet another "effective date" the tax becomes something of a moving target, and thus an unknown liability. Yet, reports are being received that the county is engaging in audit practices that make use of the newly articulated and recently disseminated notice of determination; applying this definition to the past collections practices of operators, and assessing back taxes and penalties based upon this "refined" definition of 'rent'.

The initial positive perception of the amended ordinance was turned upside down as property managers began receiving audit notices. Interactions with county staff left many property management professionals confused and frustrated with the apparent sea change in TOT collections policies as generated/interpreted by staff. The attempt to clarify the code language was distorted by staff with its in-house interpretations of the verbiage. The December 2007 "Notice of Determination" letter from the county to all TOT Certificate Holders did little to reduce the ambiguity. If anything, this "determination" further clouded the issue. The pronouncement of what is or is not deemed to be "rent" for the purposes of TOT collections appears on its face to be at odds with the Ordinance language as amended. This staff level input placed the code section in question in a dubious position of being contradictory in nature, or duplicative at best, thus creating circular reasoning that only serves to further muddy the already conflicting opinions. Not only were property managers being told that charges such as cleaning fees were to be considered a TOT taxable event, but it has been reported by those affected that such an interpretation has been applied recently in audit situations when past collections practices were scrutinized by the county. Reportedly, some of these audits utilizing the newly established determination have been conducted; resulting in the county asserting that prior years books exposed an 'underpayment' of TOT taxes due via the presumptive "inappropriate" exclusion of fees such as cleaning from the tax calculations. The back-tax assessments reported to-date have ranged anywhere from $800 to well over $12,000. This oppressive business climate has forced some operators to reconsider the viability of continuing to practice within the County of Placer. Untold damage has been done, and continues to be perpetrated upon the professional property management segment of the real estate industry. The ripple effect of these adversarial tactics will be felt by the county in innumerable ways in the years ahead.

The evolution of the concept:

An initial query of TOT accounting practices and procedures appears to have been launched by Placer County's Executive Office in 2004. This 2004 investigation coincidentally conforms to the date that a major court case in regard to TOT underpayment was being pursued by two Southern California cities (see Coincidental Legal Actions section heading within this IBP). On or about October 5, 2007, an initial letter of inquiry went out to some 2,300 property owners in and around Tahoe City,

asking if their property had been used for rental purposes. Apparently, Placer has been investigating how to initiate a TOT notification process/procedure for some time, targeting individuals who engage in short-term rentals of their property but were unaware of the TOT Ordinance.

The Revenue Services Division of the county was charged with the task of identifying properties within the boundaries of District 5 (Supervisor Kranz's District) that did not claim a 'homeowner's exemption'. Once identified, Placer mailed letters to these 2,300 homeowners in and around Tahoe City, inquiring about rental activity. This initial mailing has been characterized as a "pilot" program, to evaluate responses against the operational impacts (possible revenue sources) from the initial mailing effort. If a respondent identifies their property as having been rented for short-term vacation rentals (i.e., 30 days or less per occupancy), then a 10% charge/tax should have been affixed to the rental rate. Of course, prior to operating as a hotelier, one should have obtained a TOT Certificate for the property. Purportedly, this audit of TOT subject properties is to "ensure fairness and competitiveness among local businesses and vacation properties that are required to collect Transient Occupancy Taxes." Yet, by their own admission, "(p)ast audits have shown that most properties conscientiously collect and report the taxes." So, what compelling reason is there for the county to expend these resources to do multiple mass-mailings and ramp up what has been called by some "an aggressive collection practice"? Many questions were posed regarding the mailing. These inquiries were submitted to the county Administrative Services Division; their responses are captured below. Issues remain associated with equal treatment, due process, cause, and perhaps even entrapment may come into play. All remaining properties are slated to receive this letter inquiring about rental activity during a second and third phase of mailings.

This IBP, much like the matter under consideration, is dynamic in nature. This fluid situation continues to provide answers to issues, but then raises new questions where information was previously fleshed-out. The Director of Administrative Services for Placer County, Mr. Clark Moots, responded directly to a number of questions posed in reference to the letters distributed in October of 2007. These questions dealt with the matters discussed internally, e.g., the reasoning and methodology employed by the county in sending out the TOT letters of inquiry.

Issues associated with the ordinance amendment procedures:

The three sections of the TOT Ordinance that were proposed to be amended went through 'first reading' before the Supervisors on May 8, 2007, with second/final reading and adoption on May 22nd of 2007. The Ordinance, as amended, then became effective 30 days after the date of adoption. As such, these amendments to "clarify" the TOT ordinance only became operational in mid-year of 2007. It is concerning that there was little-to-no outreach on the part of county staff to inform us of these changes, much less to engage us in the process; of even greater concern is the possibility, as reported by members, that the county has made attempts to impose the "maximum liability" presumption for "underreporting" in previous years. One might question if such a position is sustainable, given that the county only offered up clarifying language some

six-months ago. Add to this the fact that the county felt compelled to send out a letter on December 26, 2007, which was intended to further "clarify" the meaning and intent of the TOT Ordinance as revised. Taken together, the county' auditor's admission via Colwell's Memo to the Board that the Code was unclear to-date (May 2007), the actions taken to amend the Code to better define the matter that became effective in June of '07, and then the end-of-the-year correspondence to all TOT Cert holders that once again attempted to "clarify" the meaning and intent of the Code provisions under consideration, all lead to the inevitable conclusion that the attempt to clarify the code has failed to do so. To retroactively apply this new found (or newly articulated) clarity in the code to past practices seems ill-informed at best, or a disingenuous revenue supplementation plan that should have been put before the voters as a new or amended/expanded tax prior to implementation at worst.

The Clerk for the Board of Supervisors has provided clarification regarding dates and details of the TOT Ordinance revisions of 2007. As has been mentioned, there was no proactive outreach on the part of the County Executive's Office, nor were we informed of the internal TOT *audit* conducted by the county Auditor-Controller's Office at the behest of the County Executive's Office. The utilization of "stealth" tactics, intended or unintended, resulted in the issue never showing up on our political "radar". A couple of underlying issues may exacerbate the emerging negative impression of just how this matter was handled by county staff. First, both "hearings" were conducted in Auburn, although the opportunity was available to include at least one of the two hearings during the Board's July 23 and 24 meetings in Tahoe. The term "hearing" is placed in quotes because as a matter of individual discussion and debate the issue was not heard at all (see underlying issue number two). Second, and perhaps more damning, the introduction of the proposed revisions to the TOT Ordinance was not even slated for discussion, much less debate, for it was buried within the extensive "consent agenda". On the date the ordinance revisions were introduced (08 May 2007), the consent agenda included some sixty-five (65) items on which the Board took action via a single sweeping vote. The item itself was listed as '23.(a)' under that day's consent calendar. While the second reading of an ordinance will often be listed under "consent", especially if it has been fully aired-out during the first reading, its inclusion as a non-controversial item anticipating no dissention or debate at its first reading is concerning. At the very least, this was an error in judgment. Had the issue been addressed as an individual topic for presentation and discussion, a number of the concerning aspects of the proposal might have been voiced. The second reading and adoption of the TOT amendments were placed on the 22 May 2007 "consent agenda" (item 14.a), a thirty-nine point consent calendar, again approved by a single sweeping vote.

A dialogue has been initiated with our County Supervisor on the matter. The Honorable Bruce Kranz, Placer County Supervisor (Dist. 5), understands the issue and how it impacts our industry. He is attempting to address the back-tax collection confusion; it is our hope that he can secure concurrence with at least two other supervisors that individuals and their property management firms should not be held liable for previous years "underpayment" based upon the recently "clarified" TOT Ordinance. We have not received a definitive response from Supervisor Kranz or the County as to how those

who manage the short-term rental of second homes will be treated. Until information to the contrary is received, the most up-to-date information is contained within the text of the correspondence that was sent by the County to "All TOT Certificate Holders", dated Dec., 26, 2007.

Local Elections Information:

The County Elections Division has been responsive to requests submitted regarding TOT measures, their wording, and their respective outcomes. In point of fact, this subdivision of our county government has been the most accommodating and expeditious in obtaining and communicating valuable information on the history of TOT in Placer. There are records of three relatively recent TOT Measures going before the voters in Placer County. All three measures were area-specific (i.e., not county-wide).

Tahoe TOT Additional Tax 'take one'- In March of 1996 Measure "B" was placed on the ballot exclusively in the Eastern/High Sierra area. It sought to raise the Tahoe area TOT from the county-wide collection rate of 8% by 2%, for a total TOT tax of 10% in the "North Lake Tahoe Transient Occupancy Tax Area". This was the first of two High Sierra TOT ballot measures to-date. It was approved by the voters with 1,640 "yes" votes (60.3%) to 1,078 "no" votes (39.7%). Its term/tenure of collection was set at six years, at which point it would "sunset" (cease) unless the voters took up the issue again by ballot.

Interestingly, the original 2% tax increase in TOT collections for North Tahoe was initially placed into law solely by a Supervisors' vote on June 27, 1995. Concern over a contemporary State Supreme Court ruling that nullified a TOT tax increase as invalid until and unless it was subject to a vote of the people led the Placer Board to reconsider the soundness of their Supervisor-imposed tax increase. As a direct result, Measure "B" was sent to ballot by a Board of Supervisors resolution, dated December 5, 1995. At its core, the measure established the following:

> "For the privilege of occupancy in any hotel each transient is subject to and shall pay a tax in the amount of eight percent (8%) of the rent charged by the operator. Effective October 1, 1996 and sunsetting September 30, 2002, with a review by the Board of Supervisors in three years, for the privilege of occupancy in any hotel located in that portion of Placer County legally described..." The 2% addition was to be imposed.

Foothills Attempt to 'Match' the High Sierra Increase- In November of that same year (1996), a Western Slope TOT increase from the base 8% to 10% was put to the voters. Measure "L" failed to achieve passage in the foothills, with 11,361 "yes" votes (35.4%) to 20,755 "no" votes (64.6%) recorded. It was also mentioned in passing that a couple of cities within the county have brought forward TOT measures. The outcome of these proposals has not been determined; but, given the fact that the incorporated segments of Placer County are only to be found in the foothills, the results of these proposals has little bearing upon the High Sierra issue under consideration.

Tahoe TOT Additional Tax 'take two'- In March of 2002 the second area-specific North Tahoe TOT tax increase went to a vote. Measure "C" similarly proposed to augment the 8% county-wide base with an additional 2%, replicating the previous measure's 10% tax rate. However, this second round of TOT voting in the High Sierra was scheduled to remain active for ten years (as opposed to Measure B's six year term), to then "sunset" in 2012; thus requiring another voter-approved measure to be secured to extend the 2% override past 2012. The vote for 2002's Measure C tallied 1,662 "yes" votes (63.05%) to 974 "no" votes (36.95%).

The follow-up tax proposal (Measure C) to succeed initial six-year 2% tax override was presented to the voters in 2002 as a "re-authorization" of the North Tahoe TOT rate increase. However, this proposition differed in some significant ways from its predecessor. First, it was slated to have a ten-year lifespan, four years more than its forerunner. Second, there were no progress reviews required of the Board of Supervisors (Measure B had mandated a review in year three). The Impartial Analysis of the measure, authored by the County Counsel's Office, is suggestive at points that this "General Tax" might be 'earmarked' for treatment more in keeping with a "Special Tax". For example, in the ballot statement the County Counsel states: "The additional revenues approved by the ballot measure in 1996 have been directed by the Placer County Board of Supervisors for programs that promote tourism and the economic welfare of the North Lake Tahoe area including marketing, visitor services, infrastructure development and public improvements." This statement seems to lean towards an inference that the monies collected will be retained for local usage (which would make the measure a special tax, requiring a 'super-majority' affirmative vote to achieve passage). To County Counsel's credit, they make an immediate course correction in the statement that followed this 'past use' comment. It reads, "(h)owever, the Transient Occupancy Tax and this proposed increase is a general tax and may be deposited into the County's General Fund and used for any purpose at the discretion of the Board of Supervisors." The importance of this distinction cannot be overemphasized in that it dramatically affects the vote threshold to achieve passage. By ending with a reiteration of the general tax nature of Measure C and the discretionary use of its proceeds, it reestablishes that this is indeed a general tax vote, thus demanding only a simple majority (50% + 1 vote) to enact.

While the ballot statement by County Counsel was factual, fair, and balanced, the same cannot be said for the "Argument In Favor of Measure C" published in the election information booklet. One would not expect the "pro" C position to soberly weigh the merits and liabilities of such a proposal. Nevertheless, the authors of the argument in favor are expected to represent the matter in a factually accurate way. In fact, the author(s) must sign/attest that "(t)he undersigned proponent(s) of the primary argument in favor of ballot proposition MEASURE C at the Primary election for the Placer County TTOT District to be held on March 5, 2002 hereby state(s) that such argument is true and correct to the best of his/her/their knowledge and belief." You be the judge as to whether the "pro" ballot argument met this standard. Representative examples include, "Please vote YES for Measure C to continue this special tourism tax. A yes vote will ensure that tourism dollars collected in North Tahoe REMAIN in North Tahoe." The

Argument in Favor goes on to state that this 2% addition is, "...the only portion of tourism taxes collected by the county that completely remains in our area."

County-wide 8% TOT base rate establishment- Curiously, the initial county-wide 8% TOT tax has proven difficult to pin down in regard to its passage, by whom, when, and under what circumstances/conditions. As reported by the Elections Division, they have very strong records going back as far as 1976, but have been unable to locate the initial county-wide 8% ordinance. They have identified an ordinance adopted in 1995 that addresses the entire county's TOT collections (Ord. No. 4665-B), but it is clear that a TOT provision existed prior to that date. In fact, the '95 Ordinance cited immediately above makes reference to 1985 TOT provisions/ordinances that were being amended by this 1995 update of the Code. According to the current County Counsel's Office, the original TOT is believed to be contained within the county charter. She is researching the date of its adoption at present, but it may prove to have been established in the distant past. The question of whether this initial TOT matter was put to a vote of any kind remains a great unknown. Equally important, after the passage of Proposition 218 (in 1996), which amended the State Constitution closing purported "loopholes" in the excise tax laws, thus superseding previous provisions of law, was the county-wide TOT tax then put up for a vote? The importance of this question cannot be overstated, in that for the county-wide TOT tax rate of 8% to be valid, even if initially imposed / established prior to the voting requirements, was required to be put before the people within a defined period of time Post-Prop 218. If the original TOT proposition is embedded within the County Charter, and the charter was put to a vote of the people, would that be sufficient to sustain an argument that the 8% tax was legally created/valid? This matter remains unresolved and research continues.

County Charter

With it having been mentioned that the County Charter might be the ultimate source (or hiding place) for the county-wide TOT provision, research into the content of the latest posted/published iteration of the charter (some 83 pages in length) revealed the following.

Sec. 602 Fiscal Provisions.
"General law shall govern the assessment of property, the levy and collection of taxes, the adoption of the county budget, and the appropriation, accounting and transfer of funds unless otherwise provided for in this Charter or by ordinance."

Sec. 603 General Law.
Unless the context of this Charter otherwise requires, the terms "general law" or "general laws" as used herein mean the Constitution and statutes of the State of California.

1.04.020 Definitions and rules of construction.
"Tenant" or "occupant" applied to a building or land, means and includes any person holding a written or oral lease of or who occupies, the whole or a part of such building or land, either alone or with others.

1.24.010 General penalty—Continuing violations.
As to offenses committed prior to the effective date of this subsection, the provisions of said ordinance shall be applicable to continuing violations thereof which occur from and after the effective date of said ordinance.

Other than the sections noted immediately above, which only tangentially relate to the issue at-hand, no Article, Section, or subsection could be found that specifically speaks to the establishment of a Transient Occupancy Tax (TOT). Thus, unless the county suggests that the imposition of the county-wide 8% TOT is implied within the enumerated powers as generally laid out (which would be a weak position for the county to take), then it appears that the Charter is not the document of origin for the county-wide TOT tax. The search continues.

Conclusions:

On balance, the revenue-generating mechanism that is the Transient Occupancy Tax has merit, in that it provides another tool in the local government toolbox to spread the tax burden. This objective is made all the more compelling in resort areas, where the visitor/tourist has a dramatic impact upon not only the local economy but also the demand for locally provided services (e.g., mass transit, adequate parking, police protection, public parks and other recreational opportunities, safe streets and sidewalks, bike trails…). Properly applied, these tax revenues can benefit all concerned: the visitor, the resident, local business interests, and government. The statewide initiatives to rein in government taxation, initially targeting the state level via Prop. 13, and most recently targeting the local level by the passage of Prop. 218, have also added checks and balances to the imposition of such taxes. Nevertheless, abuse can occur. These abuses can only occur in the event that a unit of government steps over the line and it goes unchallenged. At what point does an innovative practice become an illegal undertaking? When does interpretation of existing ordinance/code language become overreaching and considered a misapplication of intent? How far can a unit of government go in its efforts to expand the use or application of an existing tax before triggering a requisite vote of the people to confirm or deny the revenue expansion activity? These and many other questions related to this topic are not easily answered. Some matters can only be definitively addressed by the courts, others are more amenable to local political petitioning, and still others need only be pointed out to government officials to be rectified. Nevertheless, a good faith effort to find that line of demarcation between allowed and prohibited conduct is a worthy pursuit. A desire to ensure fairness in application, establish a reasonable approach to misunderstandings or disagreements, and create a climate of open, honest, and earnest dialogue to resolve these matters to the benefit of all must be in the foreground of any attempt to facilitate change. There may well be aspects of Placer County's TOT practices that could and should be called into question; but again reiterating, in the quest for corrective action it might be advised to avoid "tunnel vision" on winning the point at the expense of a greater long-term good.

Local Committee Discussions:

TSBOR Local Government Relations Committee Initial Commentary - The LGR Committee met on 29 January 2008. On the day's agenda was a discussion of the Placer County TOT situation, referencing Draft I of the local IBP. The consensus position of the group was to "table" the issue in regards to possible action recommendations to afford the TSBOR Property Management Committee the opportunity to review the matter and comment upon possible options to pursue to resolve the issue. Nonetheless, the LGR Committee engaged in an extensive dialogue on the issue at-hand. For purposes of this update, the committee wanted to add a cautionary note related to the unintended consequences of pursuing certain courses of action. Specifically, if an objective is to get residential properties (vacation rentals of second homes) split out from all other forms of short-term rental activity such as hotel/motel uses for separate treatment (e.g., not collecting TOT on cleaning fees), this could lead to a range of negative outcomes. A relevant example can be found in the desire to reduce or eliminate all short-term rentals of residential properties, as proposed by the Tahoe Regional Planning Agency in 2003. TSBOR fought long and hard to preserve this right to rent. After extensive debate the matter was, for the most part, discarded by TRPA; but, it carried through as a concept that was eventually refined and implemented by the City of South Lake Tahoe. El Dorado County's vacation rental ordinances were also shaped by the TRPA discussions. This neighboring county imposed draconian regulations and procedures, against our organization's loud protests. In fact, it has been reported by agents in-the-field that they simply do not deal in property management / vacation rentals in El Dorado County anymore specifically because of the burdensome mandates in place. In June of 2006 this vacation rental restriction/prohibition idea began to take shape once again in the Tahoe Basin. Again, TSBOR was forced to engage those who were pressing this agenda. Arguments have been made that if short-term vacation rentals were to be removed from the tourists rental options it would open up that segment of the second home market to affordable long-term rentals or perhaps even sales to primary residents. Such action would be anticipated to reduce property values overall, and narrow the potential client/buyer pool due to the inability to offset some of the costs associated with second home ownership via occasional short-term rental. The notion of zoning conformance has also been broached as a method to disallow short-term vacation rental activities in residentially zoned areas. TSBOR has also responded effectively to-date to these challenges. However, if differential treatment were to be pushed too vigorously by our organization it could produce "blow-back" in the form of renewed interest in limiting or prohibiting this form of rental altogether. For those readers who are interested in this topic and its history at Lake Tahoe, an equally extensive issue brief was crafted by the Board's advocate on this topic as well (dated Sept 2003).

TSBOR Property Management Committee Commentary- The TSBOR Property Management Committee met on 30 January 2008 to discuss their concerns regarding Placer County's approach to TOT assessment and collection. Members of this committee had also requested that the Board's legal counsel be present if possible during their discussion of the topic. Mr. Steve Lieberman, the Board's long-term counsel, was unavailable; however, Ms. Jana Gill, Esq., affiliated with his office,

participated in his stead. After much discussion, the committee made a multi-pronged motion to recommend to the TSBOR Board of Directors that they, "obtain formal clarification directly from the Placer County Board of Supervisors regarding ongoing ambiguity surrounding the TOT Ordinance's charge structure (4.16.020, .070, & .100), the language employed, and its intent. Linking to the language of the Code, as revised on May 22, 2007, and then further "interpreted" by the county Auditor-Controllers Office, (a) seeking to nullify the determination rendered by that office as reflected in their correspondence to "All TOT Certificate Holders", dated December 26, 2007. To then (b) reaffirm or establish that items which are not "marked up" as a source of profit, representing a "pass-through" type of charge/expense, be excluded from any TOT tax liability. This pass-through expense could be (c) demonstrated by establishing that than independent contractor agreement exists for activities such as pre-or-post occupancy cleaning, and that payment to the contractor for such services rendered is reflective of the full amount charged and received for said agreement (i.e., without profit to the TOT Certificate Holder); documentation could include, but would not be limited to, a signed contractual agreement, Tax Form 1099 distributions, or accounting ledgers/books. (d) If the operator (i.e., TOT Cert. Holder) meets the conditions set forth in sections "b" and "c", then the option should be made available in practice and reflected on reporting forms as a line item expense exempt from TOT imposition."

Concurrently, (e) the Board of Supervisors should issue an immediate "stay" order to all departments, divisions, and individuals involved in the collection of TOT monies, which would hold in abeyance (forbearance) any actions, claims, or taxes accrued under the implementation of the disputed "Notice of Determination" issued by the Auditor-Controller's Office. This injunction upon implementation would remain in effect until such time as the Board of Supervisors takes specific action to rescind it; to be considered only during a regularly scheduled Board meeting, during 'open session', placed on the agenda as a "time certain" action item. In the event that the Board elects to retain all or some portion(s) of the determination of Article 4.16.020 as reflected in the correspondence from the county dated December 26, 2007, (f) retroactive TOT tax collections actions for that portion of taxable events reflective of the activities in dispute shall be forgone/forgiven by Placer County. No operator shall be held liable for past/back taxes due based upon the recent interpretation of the ordinance.

Additionally, (g) in acknowledgement of the lack of clarity in the TOT Ordinance language, a "grandfathering clause" shall be added to Article 4.16 of the County Code which excludes all short-term rental contracts entered into prior to 01 January 2008 from compliance with the Notice of Determination disseminated by the County, dated December 26, 2007; this contractual "safe harbor" shall apply to all agreements entered into before 01 January 2008, irrespective of the actual or anticipated date of occupancy.

Finally, the Property Management Committee respectfully requests that the Tahoe Sierra Board of Realtors® (h) retain legal counsel for the express purpose of providing advice and direction to members on this TOT matter."

Given the active (in-force) nature of the issue, the committee asked that staff approach the Board President, Cathy Harry, to request that she consider calling for (convening) a special meeting of the Directorship as soon as possible to review the matter and the committee recommendations for action. The Property Management Committee also requested that the advocate look into the possibility of obtaining a reversal of the County's newly adopted TOT Certificate issuance strategy, in which every single home that is utilized as a short-term vacation-type rental must obtain an individual Certificate for the property in question, regardless of the property being professionally managed. At issue is the reporting and auditing nightmare that would ensue for the professional property manager who, under contractual arrangement, offers 25, 50, or even more homes up for occasional short term rental. It seems more reasonable and manageable to allow the property management company to obtain/secure one TOT Certificate reflective of all properties under their control.

TSBOR Board of Directors Actions - Policy direction was requested by staff, and was received on 06 February 2008, by unanimous affirmative vote of the Tahoe Sierra Board of Realtors® Board of Directors. The Board's professional advocate is tasked with the pursuit of a multi-pronged approach to secure a reasonable and functional solution to the problems associated with the overreaching determination promulgated by county staff. These efforts are to include: Obtaining a letter of understanding from the county that there will be no retroactive application of the local ordinance/code amendments and subsequent notice of determination for the purposes of auditing past practices. Corresponding with the county supervisors to share concerns associated with the county's TOT Ordinance from a historical prospective, as presently written, and in regard to its future application. In drafting this letter we are seeking clarification on some issues, and amendments in other areas; with specific focus upon reining in the staff definition of what is to be included as a TOT taxable event (i.e., exclude cleaning fees, supplemental services…). Our objective is to return to the standard of practice that was widely understood and accepted in years past; codified in such a way so as to avoid misapplication or overextension of the tax's intent in the future. The shift in policy regarding who is to hold a TOT Certificate (i.e., individual Certificates for each property under the contractual management of a firm) will also be addressed within the context of past practices and the unnecessarily burdensome change in the county's approach to Certificate issuance. If a reasonable solution cannot be achieved by political means, then less attractive alternatives will be considered to achieve redress of the industry's legitimate grievances, such as (but not limited to) consideration of: a legal challenge to the ordinance and its application; pursuit of a referendum to rescind all or a portion of the TOT tax, by popular vote (i.e., reduce or repeal by initiative); and/or establishing partnerships with affiliated interests, such as the Howard Jarvis Taxpayers Association, the Pacific Legal Foundation, the Reason Institute for Public Policy, et al. to bring additional expertise and pressure to bear on the issue. A state level legislative remedy might also be considered in the form of a bill that would serve to bracket how second-home vacation rental units are treated under the State enabling Statute (Revenue & Taxation Code, Section 7280 - 7283.51). Concurrently, given the complicating issues put into play by Assembly Bill 1916, signed into law in 2004, CAR's legal team will be approached to look into the Tax Clearance Certificate matter; to opine on the disclosure

implications at-sale, as well as to comment upon any potential expanded liability exposure and how best to mitigate this potential expanded and far-reaching risk scenario.

Issue Breakdown Based Upon Member to Advocate Q & A To-Date:

A number of questions have been articulated by our members, as have a number of salient points and real-world examples. In as many instances as possible, the question, comment, or concern has been recorded by your advocate. Research into these matters has yielded the following issue-response sections:

(1) Some have asked if they must show/provide their accounting ledgers (books) to Placer County upon demand for the purpose of a TOT collections audit.

Response: Initial research into the matter seems to indicate that "yes", the county has a right (some might argue, an obligation) to inspect one's books on occasion to ensure that appropriate taxes have been collected and remitted. A notice of audit is something of a subpoena for records. As recently as October of 2007, court decisions have been handed down that affirm a local government's right to enforce subpoenas for records deemed necessary to audit compliance with that jurisdiction's transient occupancy tax ordinance. (ref. Santa Cruz County Superior Court, No. CV154423; Cal. Court of Appeal, Dist 6, rejected hotel owners appeal on Sept. 18, 2007, of the trial court's decision to uphold the enforceability of the local gov. audit materials requirements).

(1a) Directly relating to the first question, other members have asked if the county must first have a reason, that is, a suspicion of wrongdoing (a.k.a 'probable cause') before requesting to review your records.

Response: The Court of Appeal in the aforementioned Santa Cruz case also addressed this issue of Fourth Amendment protections. In short, "no", the local government requesting to review these records is not subject to strict illegal search and seizure provisions associated with probable cause. The Court opined that legislative or administrative subpoenas, such as the TOT tax records request, need only be: (A) authorized by local ordinance or similar action, (b) serve a legitimate purpose, and (c) request materials pertinent to the matter at hand.

(2) Inquiries have been received as to whether or not it is legitimate for the county to pursue collections actions for alleged unpaid back taxes based upon the current county code of ordinances.

Response: While it seems allowable for the county to attempt to capture taxes due based upon the extant code, in this instance the TOT code as it presently exists has only been in place since July of 2007. If one goes back further, then the question of what standard the county will apply to ascertain if collections were appropriate becomes less clear. By the county's own admission, the TOT code was "not clearly defined" in some areas, thus providing the motivation for the mid-year '07 amendments. It could be inferred that even the July 2007 revisions to the TOT ordinance were less-than-clear, in that the county felt compelled to draft a letter of notification at year's end (Dec. 26, 2007) in which the definition of what was to be included in "rent" was further explained/detailed. If such a determination was warranted (as noted in the correspondence cited immediately above), then it goes to the question of whether the

current iteration of the code could reasonably be applied at all prior to the "determination" publication.

(3) Members who were aware of the mid-year '07 TOT ordinance revisions, and had read the code it its present form, came away with an understanding (interpretation) that items such as 'cleaning fees' were indeed "exempt-able" under the definition of "rent" as revised.

Response: The issue outlined above presents a compelling set of facts to forward an argument that the December 2007 "determination" was inappropriately generated. Further, the history and timeline of ordinance adoption, amendment, and then a formal notice of determination, all appear to go to the fact that the local TOT ordinance is overly vague, not well understood or easily applied by the professional property manager (much less the citizen second-home owner), and should, at a minimum, motivate the county to nullify the internally generated determination. If, in turn, the staff or members of the Board of Supervisors wish to have the staff determination reflected in the code, then place the language in an ordinance amendment to further revise the TOT code, which would then be an 'open' transparent process, subject to public review, discussion, and debate before the Board of Supervisors. A cursory review of court decisions in regard to invalidating a TOT ordinance due to vagueness have shown that the courts have found in favor of the local jurisdiction in some instances, while supporting those who contested such ordinance language in others. Perhaps most interesting (pertinent) to the present situation is the case of Britt v. City of Pomona (1990) 223 Cal.App.3d 265, 269. A succinct overview of the Britt case can be found in an opinion delivered by the Fourth District Court of Appeals in considering a set of claims made against the City of San Bernardino – it states,

> "In Britt, the court held that a transient occupancy tax imposed by the City of Pomona violated due process requirements because its terms were too vague to be understood and applied by persons of common intelligence. (Britt v. City of Pomona, supra, 223 Cal.App.3d 265, 278-280.) The court considered two versions of the tax and found them both vague. The 1987 version, although it appeared 'to be directed at transients, in actuality includes persons living in 'hotels' who, like the plaintiffs, are not in fact transients. Second, the law appears to require the tax to be paid by all persons living in the 'hotels,' even those living there under a fee interest in the hotel . . . .' (Id., at pp. 278-279.) The court also noted that the 1987 version included the word 'dwelling' in its definitions of 'hotel' and 'occupancy,' even though the word 'dwelling' generally is a building used for long-term residents. The court also found that the definitions of 'transient' and 'hotel' were circular."

(4) Some have questioned the legality of the tactic used to expand the revenue collected via this tax, namely the distribution of a notice of determination letter.

Response: As is noted on the top of page one of this briefing paper, this IBP is not to be considered or used as a legal brief. However, as a subject of inquiry, the matter itself is inexorably tied to past and present court proceedings, legislative actions, and political maneuvering. Therefore, while the law and court decisions are referenced throughout this draft issue brief, it is in the service of a political affairs analysis of the

situation. With that frame of reference in mind, an attempt will be made to offer up possible arguments in reference to the limits of administrative latitude in such tax affairs. Proposition 218, a California Constitutional Amendment, provides guidance as to taxpayers rights and the parameters for various forms of fees, charges, and taxes. Prop. 218 amended our State Constitution. Of specific interest to the current issue, Article XIII C was added to the California Constitution, which reads, in pertinent part, *"SEC. 2. Local Government Tax Limitation…*

> *(b)* ***No local government may impose, extend, or increase any general tax*** *unless and* ***until that tax is submitted to the electorate and approved by a majority vote****. A general tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved. The election required by this subdivision shall be consolidated with a regularly scheduled general election for members of the governing body of the local government, except in cases of emergency declared by a unanimous vote of the governing body."* (**emphasis added)**

Whether the recent TOT "determination" by county staff would meet the test or intent of reflecting an "increase" in the general tax is a matter of some debate. If it does reach that threshold, then a vote of the people would be required to impose the expanded TOT tax scheme. Locally, the action does not alter the "maximum rate" of collection as approved by the voters, but does indicate that the revenue collected will increase over and above the presumed maximum amount due at the 10% rate as the number/type of taxable event are expanded. Some direction is afforded regarding the intent of Prop. 218's applicability to the present case; it states in Section 5 of this Constitutional Amendment, entitled "Liberal Construction", that, "The provisions of this act shall be liberally construed to effectuate its purposes of limiting local government revenue and enhancing taxpayer consent." Some have read this section to mean, 'when in doubt, vote.' The safest course for the county to follow when the tax in question has been established under less-than-optimal (ambiguous) means would be to either remove it or put it before the people for a vote of affirmation (or reaffirmation).

(5) A question was forwarded by a member as to how contractual arrangements, agreed to prior to this "letter of determination" being received, were to be treated in regard to TOT collections. Apparently, it is not uncommon for property managers to enter into contracts with vacation renters' months in advance of their intended dates of occupancy. These contractual agreements oftentimes spell out in some detail the costs to be borne by the occupant; other times, the agreement focuses on the 'bottom line' amount due for rent plus security deposit. In either event, the rental rate has been agreed upon in good faith by both parties. The follow-up question, articulated by yet another property manager, is whether the occupant is to be hit with an additional TOT charge based upon the most recent county notice, or if the contract should be "grandfathered" under the prior/existing practices at the time the agreement was entered into. Alternatively, the question is whether the owner or property manager will be expected to "eat" the difference in TOT collection rates for those contracts.

Response: It does not appear that this issue or situation has even been considered by the taxing authority. "Grandfathering", for lack of a better term, seems like a reasonable

request to make; especially when one can demonstrate that a valid contract had been entered into prior to the most recent definition of what constitutes “rent” for the purposes of TOT taxation. It is unknown if the local jurisdiction would entertain such a proposal, but it could be forwarded. It is reasonable to assume that the jurisdiction, if interested at all, would be looking for some sort of bracketing on the grandfather clause, be it three, six, nine, or twelve months grace period for contracts signed before January 01, 2008. One side point to consider though, if a grandfathering clause is pursued, does that infer that the organization would be conceding the point of the appropriateness of the scope of the definition of what it to be considered a TOT taxable event? Can these two issues be successfully bifurcated, so as to advance the one (grandfathering) without compromising the other (that the determination as expressed by staff in its letter of 26 Dec. is overly inclusive and errant in its interpretation of the ord)? As to the owner or operator “eating” the tax differential, there are some indications that such a practice would not be in keeping with the letter of the law (ref. Placer Ord. Section 4.16.050).

(6) The question, in a broader sense, of whether the local TOT ordinance might have any points of conflict with its enabling statute at the state level has been considered. Aside from Prop. 218 issues, the question is really one of how the Revenue & Taxation Code meshes with the County’s ordinance.

Response: A side-by-side comparison of the county Code, Article 4, Section 16 et seq., against the State’s Revenue and Taxation Code, Section 7280 et seq., brings up a few points of possible disagreement. First, the county’s definitions of “Hotel” and “Tourist Home or House” (4.16.020) does not appear to adequately call out an exclusion (required, not optional) from TOT taxation in the case of time-share projects and associated uses (ref. R&T Code 7280.(b)-(c)). This concern is reinforced when looking into the county’s “Instructions For Completing The TOT Registration Certificate Application”, last revised on 12/13/07. The codes assigned by the county for various types to taxable units includes “Timeshare” (Code 06), and “Condotel” defined as “Multiple owners on one property operated with resort amenities” (Code 10). It would seem that state code carves out these forms of use from inclusion in a local TOT ordinance, yet Placer County’s ordinance does not appear to differentiate these uses from other forms of short-term occupancy.

Second, the county’s definition of “rent”, which includes all kinds of goods, labor, or services without any deduction whatsoever, appears to conflict with the State R&T Code, Sec. 7282.3, subsections (a) through (c), which states, “Notwithstanding any other provision of law, no city, county, or city and county may levy a tax under Section 7280 on any amount subject to tax under the Sales and Use Tax Law (Part 1 (commencing with Section 6001)) with respect to the sale of food products.” It goes on to say, “For purposes of this section, "food products" means food and beverage products of every kind, regardless of how or where served, and shall specifically include, but not be limited to, alcoholic beverages and carbonated beverages of every kind.” By default, it seems as if the county’s approach is over-inclusive and inappropriately captures tax for items not taxable under Section 7280 of state law.

Other issues are more nebulous, such as whether the county's inclusion of dormitories, mobile homes, or rooming houses as TOT taxable conflicts with the state's affordable housing objectives. Or whether the county's requirement that to relieve the operator of the obligation of remitting TOT for an unused 'reservation' is predicated on compliance with Sec. 4.16.130 "Refunds", subsection "D", (n)o transient shall be entitled to a refund from any operator of any transient occupancy tax paid to the operator on the grounds that such transient did not take occupancy of the room unless he or she files a written request with such operator stating his or her full name, address, telephone number, date of request, date tax paid to operator, room number for which such tax was paid, and that he or she did not occupy such room." Given the burdensome nature of this scheme, one might view it as a tax by default, not a tax based upon use.

(7) Questions have been raised concerning just how much latitude the county is afforded in affixing fees, fines, and penalties associated with non-payment or underpayment.

Response: Unfortunately, the state enabling statute, specifically R&T Code Section 7283, gives the county great latitude in setting up its structure of collections for delinquent accounts. The more difficult question is, at what point does the local entity's collection practices become usury. In considering this question, two facts are troubling- one, that the response time allotted by the county in regard to audit claims is a short seven-day window; and two, that the aggregate penalties that could accrue for delinquencies can be as high as 56.5% of the total tax due, plus the original delinquent amount (ref. Sec. 4.16.090, subsections A through E). Add to this the 'blank check' type of provision contained in Sec. 4.16.100, subsection C, which reads, "In the event records are not produced upon request, or such records are not reasonably auditable, tax, interest and penalties will be levied upon the average room rate and occupancies for similar properties within the same area during the audit period. Further, and without limitation, any operator and/or owner who does not produce records following written notice as set forth herein shall pay, in addition to any tax, interest, or penalties due, the sum of one hundred dollars ($100.00) per day for each day the records are not produced." In contrast, the operator is only afforded a short timeframe to submit a waiver-appeal request, seven working days from the date of penalty assessment notification (ref. 4.16.110, A.1.). Also in contrast to the "without limit" county fine of $100.oo per day for each day that records are not produced upon request, the operator's waiver request appears to be limited to an amount not to exceed $5,000.oo.

(8) Some frustrated Certificate holders have considered simply continuing to do business as they have for years (i.e., not charging TOT taxes to cleaning fees) and remitting the 10% assessed and collected for the actual rental rate. It has even been said in passing that perhaps it would be best to let Placer County press the issue (via non-payment) then tie the matter up in court while all the "shady" dealings can be addressed under the spotlight of a court proceeding.

Response: While that "fighting spirit" is admirable, especially when it relates to taxation, such a decision to consciously forgo collecting taxes on items that the county has expressly said are taxable events might be unwise. The disagreement over what is or is not a taxable event is worthy of further exploration/pursuit, but as a practical

matter, electing not to assess and collect TOT taxes could well result is significant fines being attached to your business (see item seven above). Furthermore, with the confounding variable of AB 1916 (became law on Jan. 01, 2005), such "underpayment" might not only accrue against the person/operator, but might end up as an encumbrance upon the property/title itself. Whether accurate or errant in its determination, until such time as the matter has been resolved, it might prove to be a more prudent course to collect the full amount as asserted as being taxable by the county, and remit that full amount in a timely fashion. If one feels compelled to "be heard" on this perceived injustice, then adding a notation with the payment to the county that it is "made under protest" should serve your purposes and preserve your rights. As with most disputes in which defiant action (or inaction) could pose a threat of civil or even criminal prosecution, it would be advisable to confer with your individual or your firm's/company's legal counsel before exposing yourself and your business interest to such risk.

(9) Some folks have deflected their outrage over the county's unilateral determination that expanded the number/type of TOT taxable events by questioning the inaction on the part of the Resort Association (North Lake Tahoe Resort Association – NLTRA). A few folks have even suggested "pulling" their NLTRA membership in protest. Others have opined that as is the case with most political matters, things are not always as they seem, and the 'backstory' provides insight as to why it would not be proper to "punish" the Resort Association for heavy-handed tactics adopted at the county level.

Response: Initial research into the matter of perceived inaction by Resort Association reaffirmed to your advocate's satisfaction that this group is, as it has been, our ally, not our adversary. Within the context of an e-mail broadcast to the General Membership on the changing landscape of the TOT Ordinance, the misperception of NLTRA being somehow in league with the county was hopefully dispelled. It read, pertinent part, "One item that has become an unnecessary and undeserved point-of-contention is the perceived role that the North Lake Tahoe Resort Association (NLTRA) has played in this TOT debacle. To be clear, the Resort Association is NOT is league with Placer County in this matter. I have spoken with NLTRA President & CEO Steve Teshara. Steve confirms that the NLTRA has no involvement with TOT collections or collection policies. They are a recipient of TOT funding from Placer County for reinvestment at North Lake Tahoe for marketing, transportation and infrastructure projects. They agree with TSBOR that the County's approach to the "new TOT collection policies" have been heavy-handed and unilateral. The NLTRA was "warned off" having any opinion regarding the County's approach. The "mandates" that have trouble us all have emanated from the Placer County Executive Office. County staff has pressed the issue, and it is here that our fight must be focused (ref. Memo to the Supervisors from Rich Colwell, Chief Assistant C.E.O., dated May 8, 2007). Yes, they are dependant upon the TOT collections to accomplish a large segment of their mission; a mission that includes much more than tourism marketing, notably infrastructure improvements and transit solutions to name but two. These essential functions performed by our Resort Association should not be damaged due to improper target acquisition. NLTRA seeks the same sense of fairness, balance, and predictability in the tax base as does TSBOR and the public generally. A diverse population from within the business community and

beyond has called in question the recent unilateral mandates regarding TOT matters. To be effective we must retain our focus. Those who seek to divide the business community divert the focus from the primary problem and its solution; don't be pulled off-point."

(10) More sweeping inquiries have been noted, in which state-level issues or even federal/Constitutional questions have been broached. Specifically, at the state level the recurrent question involves disclosure uncertainties that arise from the "Tax Clearance Certificate" optional request. On a U.S. Constitutional level, questions concerning Freedom of Speech might be in play when considering the "muzzle" that county code section 4.16.050 preemptively places upon advertising language.

Response: While these matters are intriguing and pertinent to the overall integrity of the ordinance under review, it would literally take volumes to adequately address such legislative and Constitutional issues. As such, the former question is perhaps better put to C.A.R., and the latter to Constitutional scholars.

~END OF ISSUE BRIEF~

DRAFT 7 – Not for External Distribution

For additional information, documentation, or illustrations…
Please contact John R. Falk, Legislative Advocate
Governmental & Public Relations Consultant
(530) 546-4598
jrfintel@charter.net

Reader's notes:

_____

_____

_____

_____

_____

_____

_____

_____

_____

_____

_____

_____

_____

###