

# CITY COUNCIL REPORT



Meeting Date: July 5, 2016  
General Plan Element: *Provide for the orderly administration of the affairs of the City*  
General Plan Goal: *Fiscal Management*

## ACTION

Request: **Adopt Resolution No. 10521** authorizing the City Attorney to direct the appeal of any adverse judgement or action to the Arizona Court of Appeals (and up to and including the ability to seek review before the Arizona Supreme Court) in the case currently pending as Case No. TX 2014-000470 in the Superior Court of the State of Arizona, Arizona Tax Court, related to the City's portion of statewide, unpaid privilege taxes.

### Background

The City of Scottsdale imposes a privilege tax (currently 1.65%) on the business activity of hotels. The City imposes an additional privilege tax on the activity of transient lodging (currently 5%). This additional tax is often referred to as the "bed tax". The City of Scottsdale, as well as other cities and towns, has also adopted language in its tax code that allows the broker for a taxable activity to be liable for the taxes of their principal.

For several years, the City of Scottsdale and the other "non-program" cities (large cities whose tax collection is not administered by the Arizona Department of Revenue) have been involved with conducting a joint multijurisdictional privilege tax audit of the online travel company (OTC) industry. This industry provides the ability for people to search for and book hotel rooms by accessing OTC websites. The OTC industry charges the user a fee or charge over and above the rate charged for occupancy of the room. It is the contention of the cities that taxes are owed on the difference between what the OTC collects from the customer and what the hotel ultimately collects (and would remit taxes on). The audit resulted in a finding that the OTCs were operating as brokers and assessed unpaid tax for this activity. The OTC challenged the assessment and the matter was appealed.

The City of Tempe was the lead city in the multijurisdictional audit and the cities joined together to retain outside counsel. After a competitive process the firm of Schneider Wallace Cottrell Konecky became the lawyers representing all of the cities participating in the joint audit and moving forward to affirm and collect the audit's assessments.

The question of whether or not the original multi-jurisdictional audit assessment should be upheld was submitted to the Superior Court of the State of Arizona, Arizona Tax Court. Motions for Summary Judgement were filed with that Court and a Judgement was recently entered. In short, the Court ruled that the OTC's business activities in booking hotels and other rentals are taxable. However, the Court further ruled that because this application of

the tax code was new, the tax owed could only be collected prospectively and no tax would be owed during the previous audit period.

The City's staff strongly disagrees that its position is new. The City had taken the position that the OTC's activities were taxable and a tax was owed well before the audit in question. In fact the City litigated another case on the same subject in Superior Court of the State of Arizona, Arizona Tax Court, in 2006 where the City's tax was upheld.

Because this ruling seems to be clearly mistaken, outside counsel recommends that the City appeal this portion of the Court's Judgment. The City Attorney's Office concurs.

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## **ANALYSIS & ASSESSMENT**

### **Recent Staff Action**

Staff from the City Attorney's Office and Treasurer's Office have discussed the Judgment and the potential appeal with other cities involved in the litigation and outside counsel.

### **Policy Implications**

To uniformly impose and collect the tax on all OTC.

### **Significant Issues to be Addressed**

None other than those discussed above.

### **Community Involvement**

No community involvement is necessary regarding this matter in litigation.

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## **RESOURCE IMPACTS**

### **Available funding**

The City is not required to pay outside counsel, who has agreed to provide legal services on a contingency basis of 27% (of any funds collected). Further, the awardee is not requiring City to reimburse it for any costs. Should the City not prevail, no monies will be owed. Based on estimates provided by the joint audit, Scottsdale is owed approximately \$2.4 million dollars in unpaid taxes for the audit period.

### **Staffing, Workload Impact**

The City Attorney's Office will work with outside counsel on the appeal.

### **Future Budget Implications**

If the City prevails, it will be able to collect the tax at issue, which is approximately \$2.4 million dollars. The City may become liable for the Defendants' costs and attorney's fees, but given that the City has primarily prevailed in Tax Court, that risk has been reduced.

### **Cost Recovery Options**

None.

**OPTIONS & STAFF RECOMMENDATION**

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**Recommended Approach**

**Adopt Resolution No. 10521** authorizing the City Attorney to direct the appeal of any adverse judgement or action taken in the case currently pending as Case No. TX 2014-000470 in the Superior Court of the State of Arizona, Arizona Tax Court.

**Proposed Next Steps**

Direct outside counsel to prepare the appeal.

**RESPONSIBLE DEPARTMENT(S)**

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City Attorney's Office

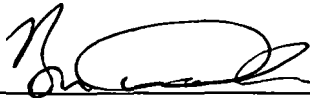
**STAFF CONTACTS (S)**

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Bruce Washburn, City Attorney, [bwashburn@scottsdaleaz.gov](mailto:bwashburn@scottsdaleaz.gov)

**APPROVED BY**

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Bruce Washburn, City Attorney  
(480) 312-2405  
[bwashburn@scottsdaleaz.gov](mailto:bwashburn@scottsdaleaz.gov)

6/24/16  
Date

**ATTACHMENTS**

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1. Resolution No. 10521
2. Judgment

RESOLUTION NO. 10521

A RESOLUTION OF THE COUNCIL OF THE CITY OF SCOTTSDALE, MARICOPA COUNTY, ARIZONA, AUTHORIZING THE APPEAL OF THE MARICOPA COUNTY SUPERIOR COURT'S JUDGMENT AND RULING IN CASE NO. TX 2014-000470, CURRENTLY PENDING IN MARICOPA COUNTY SUPERIOR COURT IN THE STATE OF ARIZONA, ARIZONA TAX COURT.

WHEREAS, the City, along with many other cities, collectively brought a tax case currently pending as Case No. TX 2014-000470 in the Superior Court of the State of Arizona, Arizona Tax Court, related to collecting the City's portion of statewide, unpaid privilege taxes following a multi-jurisdictional audit and the audit's resulting tax assessments; and

WHEREAS, the Maricopa County Superior Court has entered a judgment and ruling confirming the validity of the tax, but which is in part, adverse to the City;

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Scottsdale, Maricopa County, Arizona, as follows:

Section 1. That the City Council hereby authorizes the City Attorney to direct the appeal to the Arizona Court of Appeals of any judgment or other action taken by the Arizona Tax Court in Case No. TX 2014-000470 and to seek review before the Arizona Supreme Court of any adverse ruling received upon such appeal.

PASSED AND ADOPTED by the Council of the City of Scottsdale, Maricopa County Arizona this 5th day of July, 2016.

CITY OF SCOTTSDALE, an Arizona  
municipal corporation

ATTEST:

\_\_\_\_\_  
Carolyn Jagger, City Clerk

\_\_\_\_\_  
W.J. "Jim" Lane, Mayor

APPROVED AS TO FORM:

  
\_\_\_\_\_  
Bruce Washburn, City Attorney

**Granted with Modifications**

\*\*\*See eSignature page\*\*\*

Michael K Jeanes, Clerk of Court

\*\*\* Electronically Filed \*\*\*

H. Bell, Deputy

6/6/2016 8:00:00 AM

Filing ID 7465038

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 27 Trip Network, Inc. (d/b/a CheapTickets.com), and  
 28 Internetnetwork Publishing Corp. (d/b/a Lodging.com)

**IN THE SUPERIOR COURT OF THE STATE OF ARIZONA**

**IN THE ARIZONA TAX COURT**

20 City of Phoenix, et al.,  
 21  
 22 Plaintiffs,  
 23  
 24 v.  
 25  
 26 Orbitz Worldwide, Inc., et al.,  
 27  
 28 Defendants.

Case No. TX2014-000470

**JUDGMENT**

(Assigned to the  
Hon. Christopher Whitten)

26 By its Minute Entry dated April 11, 2016 and filed by the Clerk on April 20, 2016  
 27 (the "Minute Entry"), this Court disposed of all matters in this appeal. Accordingly,  
 28 pursuant to Rule 54(c), Arizona Rules of Civil Procedure, the Court finds that no further

Snell & Wilmer

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matters remain pending and enters final judgment on such terms and consistent with the findings and conclusions in the Minute Entry.

DATED this \_\_\_\_ day of \_\_\_\_\_, 2016.

\_\_\_\_\_  
The Honorable Christopher Whitten  
Judge of the Superior Court, Maricopa County

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# eSignature Page 1 of 1

Filing ID: 7465038 Case Number: TX2014-000470  
Original Filing ID: 7383786

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**Granted with Modifications**



**ENDORSEMENT PAGE**

**CASE NUMBER: TX2014-000470**

**SIGNATURE DATE: 6/2/2016**

**E-FILING ID #: 7465038**

**FILED DATE: 6/6/2016 8:00:00 AM**

**MICAH RAY ALEXANDER**

**ROBERT SCHWIMMER**