

## NEW YORK ADOPTS A VAT

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### INTRODUCTION

Virtual intermediaries (enterprises like Priceline.com,<sup>1</sup> Expedia.com,<sup>2</sup> Orbitz.com,<sup>3</sup> and Travelocity.com<sup>4</sup>) are having a significant impact on state and local revenues. These enterprises (room remarketers) acquire lodging at steep discounts and then resell the accommodations to the public. When rooms are resold the discount the public receives is more modest. The difference is the intermediary's profit. Thus, a room listing for \$100 per night might be sold to an intermediary for \$50 and then resold to an online customer for \$70.<sup>5</sup> The tax question is – should the tax base be \$100, \$70 or \$50?

How this question is answered has a direct impact on the virtual intermediary's profit (because hotel taxes impact the final price). As a result, intermediaries are inclined to arrange transactions to keep the tax base as low as possible (preferring a tax on \$50). Tax authorities feel that a true measure of consumption is \$70 (if not \$100).

To deal with revenue loss in this area state and local jurisdictions have three major options at their disposal: (1) litigate current law and then tinker with statutory or

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<sup>1</sup> Priceline.com was founded by Jesse Fink (venture capitalist) and Jay Walker (digital entrepreneur) headquartered in Norwalk Connecticut. The origins of the company are closely tied to Walker's research company Walker Digital. Priceline.com was formed in July 1997, commenced operations on April 6, 1998 and had its first \$1 million day on April 28, 1999 when it sold over 5,000 airline tickets. See: <http://www.expedia.com/>.

<sup>2</sup> Expedia.com, headquartered in Bellevue, Washington, was founded within Microsoft Corporation in 1995 and was launched on the Internet in October 1996. It offers one-stop travel and reservation services, making over \$17 billion in travel reservations annually. It operates sites in the US, Canada, the United Kingdom, Germany, France, Italy, Spain, the Netherlands, Norway, Sweden, Denmark, Australia, Japan and China. See: <http://www.expediainc.com/phoenix.zhtml?c=190013&p=home>.

<sup>3</sup> Orbitz.com, headquartered in Chicago, Illinois, has been in operation since 2001. It was founded by Continental Airlines, Delta Air Line, Northwest Airlines, and United Airlines (American Airlines joined later). It is a publicly traded company with an initial public offering in July 2007. See: <http://corp.orbitz.com/>.

<sup>4</sup> Travelocity, headquartered in Southlake, Texas, was created in 1996 as a wholly owned subsidiary of Sabre Holdings Company which was itself a wholly owned subsidiary of American Airlines. It was a publicly traded company until March 2007 when it was taken private. In 1999 it gained market share when it became associated with the AOL travel portal, but by 2002 it was suffering from competition with Priceline.com and Expedia.com. See: <http://www.travelocitybusiness.com/>.

<sup>5</sup> Jay Walker, the founder and vice chairman of Priceline.com explains the business model of virtual intermediaries as a "demand collection system."

In the traditional model of commerce, a seller advertises a unit of supply in the marketplace at a specified price, and a buyer takes it or leaves it. Priceline turns that model around. We allow a buyer to advertise a unit of demand to a group of sellers. The seller can then decide whether to fill that demand or not. In effect, we provide a mechanism for collecting and forwarding units of demand to interested sellers – a demand collection system.

N. Carr, *Forethought – Redesigning Business: A Conversation with Jay Walker*, HARVARD BUSINESS REVIEW 19 (Nov.-Dec. 1999).

regulatory provisions if the outcome is not favorable,<sup>6</sup> (2) abandon *ad valorem* taxation and adopt a flat fee per room scheme,<sup>7</sup> or (3) adopt a European-style value added tax (VAT).<sup>8</sup> Somewhat surprisingly, New York has taken the third approach.

This paper considers the New York VAT in hotel accommodations in three sections. The first defines a European-style credit-invoice VAT and applies it to the New York Hotel Room Occupancy Tax, the second considers the critical term – the *operator* – and examines how this term in the context of a hotel tax modeled on the retail sales tax creates problems when virtual intermediaries get involved facilitating accommodation

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<sup>6</sup> This appears to be the approach of many states. The Indiana Office of the Attorney General for example is defending the state's Department of Revenue in six cases brought by various online travel companies in state court. See: Karen Setze, *FTA Panelist: Online Travel Companies Faring Worse than Advertised in Court*, (June 15, 2011) TAX ANALYSTS Doc. No. 2011-12956 or 2011 DSTT 115-2 (referencing the presentation of Indiana Deputy Attorney General Jessica Reagan who explained that when virtual intermediaries were winning cases it was largely based on "... the specific language of the local ordinance or statute, which courts in some cases described as appearing to be a 'tax loophole.'")

Walter Hellerstein suggests how state and local governments might "tinker" with hotel tax statutes to meet the virtual intermediary challenge. He suggests borrowing from the tax treatment of drop shippers. Instead of goods being drop shipped into a jurisdiction by a third party, what is happening with virtual intermediaries under the hotel tax is the "drop shipment" of a service.

In my treatise, in offering a "normative" approach to the issue addressed in this memorandum, [citations omitted] I suggested a "practical approach" [citation omitted] to taxing the travel intermediaries' margin that neither the MTC nor the industry proposal has embraced, namely, requiring the hotel operator to add a presumed markup to the travel intermediary's price, and collect tax on the marked-up price, subject to the hotel's establishment of an actual markup that is different. This would remove the travel intermediary from the tax collection process altogether and was addressed to the concern that there might otherwise be constitutional problems with asserting tax collection nexus over out-of-state travel intermediaries.

Walter Hellerstein, *Letter to the National Conference on State Legislators: Taxation of Travel Intermediary Services*, 2 (July 16, 2009) available at: <http://www.netchoice.org/library/travel-intermediary-tax-proposals.pdf>.

<sup>7</sup> This is the Quebec approach. Lodging taxes are imposed on the customer. [Quebec Sales Tax, R.S.Q., c. T-0.1, §541.24]. Localities can elect either (a) a flat \$2 per room/ per day tax, or (b) a tax based on 3% of the purchase price – but only if the supply is made by the operator. In cases where a 3% ad valorem tax is elected – and if an intermediary makes the supply not an operator – the tax is \$3 per room/ per day. Intermediaries are defined as "... the recipient of a supply of an accommodation unit who receives the supply only to again make a supply of the accommodation unit for consideration." [Quebec Sales Tax, R.S.Q., c. T-0.1, §541.23]. An intermediary cannot be a customer. The customer is defined as "... the recipient of a supply of an accommodation unit, but does not include an intermediary" [Quebec Sales Tax, R.S.Q., c. T-0.1, §541.23]. The key to Quebec's approach to Lodging Taxes is that in the localities where the tax is ad valorem based, it is *only an ad valorem based tax when a customer purchases directly from an operator*. [Quebec Sales Tax, R.S.Q., c. T-0.1, §541.24]. Whenever an intermediary purchases rooms from an operator for resale the tax is at a flat rate per room/ per day. The operator selling to the intermediary collects it in advance. [Quebec Sales Tax, R.S.Q., c. T-0.1, §541.25]. New York already does something similar in New York City where a \$1.50 fee per unit/day fee is imposed. New York City and the State of New York also impose an *ad valorem* sales tax on every unit located within New York City. See TSB-M-05(2)S.

<sup>8</sup> Richard T. Ainsworth, *Virtual Intermediaries in the Lodging Industry: Consumption Tax Problems in the U.S. and Japan*, 57 TAX NOTES INTERNATIONAL 865 (March 8, 2010) (indicating that the virtual intermediary problem is unique to both the US retail sales tax, and the Japanese consumption tax, and that it is not a problem at all under other types of consumption taxes – notably the European VAT generally, and the Canadian GST particularly when it considers cross-border drop shipments of goods or services).

rentals, and the third considers the new term *room remarketer* as it is used in the New York Hotel Room Occupancy Tax.

A short concluding section discusses why in re-designing this tax as a VAT New York has made an insightful tax policy decision. New York will most likely *increase revenue without increasing rates or expanding the tax base* with this decision. Gains will come from increased efficiency, more stable revenue deposits from fractionated payments, and lower enforcement costs from the self-enforcing nature of the VAT.

#### NEW YORK'S VAT

On August 13, 2010 the New York State Department of Taxation and Finance, Office of Tax Policy Analysis, Taxpayer Guidance Division released *Amendments Affecting the Application of Sales Tax to Rent Received for Hotel Occupancy by Room Remarketers*.<sup>9</sup> The legislative revision it considers (Chapter 57 of the Laws of 2010) was effective September 1, 2010. The changes brought in by this Chapter effectively converted New York's Hotel Room Occupancy Tax from a single-stage retail sales tax to multi-stage European-style VAT.

*Definition.* Like the retail sales tax, a value added tax is an *ad valorem* tax. However, instead of collecting the full tax on value at the point of final consumption, a VAT collects the tax in slices all along the supply chain measured by the value added at each stage. As Schenk and Oldman indicate:

A value added tax (VAT) is a generic name associated with a multistage tax that is levied on the value added by each business firm at every of production of goods and services.<sup>10</sup>

In the normal case, when a final consumer secures a room directly from a hotel, a retail sales tax is easy to apply. The consumer pays tax to the operator of the hotel based on the value paid for the accommodations. A retail sales tax “fits” this fact pattern very well.

However, when an intermediary is interposed between the final consumer and the hotel what was formerly a single-stage transaction now becomes multi-staged. A short commercial supply chain is created, and value is added at each stage. Stated another way, the hotel (like a manufacturer) produces inventory each day (vacant rooms). Unfilled rooms are perishable commodities. As the time for occupancy comes closer a certain number of these rooms will be sold (at a discount) to a middleman (a room remarketer) that will add important value (securing rent for the room on short notice). The best middlemen possess what is known as “demand collection systems” to help them find willing renters on short notice.<sup>11</sup> A value added tax “fits” this kind of supply chain fact pattern very well.

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<sup>9</sup> TSB-M-10(10)S (August 13, 2010) available at: [http://www.tax.ny.gov/pdf/memos/sales/m10\\_10s.pdf](http://www.tax.ny.gov/pdf/memos/sales/m10_10s.pdf).

<sup>10</sup> Alan Schenk & Oliver Oldman, VALUE ADDED TAX – A COMPARATIVE APPROACH 30 (2007).

<sup>11</sup> Jay Walker, *supra* note 5.

*Operator.* The same problem that New York faced with its Hotel Room Occupancy Tax is replicated in many hotel taxes throughout the US. These taxes are modeled on a retail sales tax, and they pivot on the requirement that the *operator*<sup>12</sup> (like a retail merchant) must collect the tax from an *occupant* (assumed to be a final consumer). Prior to the passage of Chapter 57 of the Laws of 2010 New York defined an *operator* as simply: “Any person operating a hotel.”<sup>13</sup>

New York only had to look to North Carolina to see what would happen if it tried to require a virtual intermediary (a room reseller) to collect the Hotel Room Occupancy Tax on the value they were adding to the final sale of accommodations. Pitt County, North Carolina brought such a suit on behalf of itself and others alleging violation of its Occupancy Tax. The case was removed to federal court and quickly dismissed.<sup>14</sup>

The District Court determined that there was no injury in fact. Pitt County had no standing to sue. On appeal the Fourth Circuit agreed, but on different grounds. This time the court said there was a failure to state a claim on which relief can be granted.<sup>15</sup>

The key to both decisions is the term *operator*. The essential argument raised in the lower court was: *if* a business is a retailer (a hotel *operator*) under the North Carolina sales tax, *and if* that business rents accommodations within Pitt County, *then* Pitt County should be able to require that business to collect the Pitt County Occupancy Tax. But, online travel companies are not “retailers,” because they do not *operate* hotels in Pitt County. Thus, Pitt County cannot compel them to collect tax on their room re-sales.

The Appeal Court took a different route but reached the same result. Online businesses with no physical presence in North Carolina are not subject to the sales tax, because they are not “retailers” within the meaning of the sales tax. The retailer in the hotel industry is defined as the *operator*.<sup>16</sup> Thus, the Fourth Circuit decided simply:

... an online travel company is not a retailer because it is not a business of a type that is similar to a hotel, motel, or tourist home or camp. As a result, an online travel company is not subject to the Pitt County occupancy tax.<sup>17</sup>

Rather than fight this battle,<sup>18</sup> New York has decided to change the definition of an *operator* in Chapter 57 of the Laws of 2010. The expanded definition now includes room remarketers.<sup>19</sup> It states that an *operator* is:

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<sup>12</sup> New York Tax Law §1105(e).

<sup>13</sup> New York Tax Law §1101(c)(4).

<sup>14</sup> *Pitt County, N.C. v. Hotels.com*, 2007 U.S. Dist. LEXIS 85910 (E.D.N.C., Aug. 12, 2007).

<sup>15</sup> *Pitt County, N.C. v. Hotels.com*, 553 F.3<sup>rd</sup> 308 (4<sup>th</sup> Cir., 2009).

<sup>16</sup> N.C. GEN. STAT. § 105-164.4(a)(3).

<sup>17</sup> *Pitt County*, 553 F.3<sup>rd</sup> 308, 314.

<sup>18</sup> In fact, the State of New York had an inkling of how difficult litigation would be on this issue, because Nassau County had unsuccessfully tried to bring a class action suit against many of the virtual intermediaries. *County of Nassau, NY v. Hotels.com et. al.* 594 F. Supp. 2d 251 (E.D.N.Y., 2007) (case dismissed because the county did not exhaust administrative remedies); *County of Nassau, NY v. Hotels.com et. al.* 577 F.3d 89 (2<sup>nd</sup> Cir., 2009) (vacated and remanded for failure to meet requirements for

Any person operating a hotel. Such term shall include a room remarketer and such room remarketer shall be deemed to operate a hotel, or portion thereof, with respect to which such person has the rights of a room remarketer.<sup>20</sup>

This solves the problem. Both the owner of the hotel and the virtual intermediary (room remarketers) are *operators*. Both the virtual intermediary and the guest are *occupants*.<sup>21</sup> Thus, for example, if a room that normally lists for \$100 is sold to a virtual intermediary for \$50, and then resold to a guest for \$70 the tax will be collected twice. The virtual intermediary (as an *occupant*) will pay the hotel owner (as an *operator*) a tax on \$50. In addition, the guest (as an *occupant*) will pay the virtual intermediary (as an *operator*) a tax on \$70.

If this was all there was to the change, then it is clear that New York would be going too far. Where New York may have previously collected tax only on \$50, it would now collect tax on \$120 (\$50 + \$70 = \$120). This aggregate tax base exceeds the \$100 full value of the room by \$20.

New York solves this problem by following the lead of the EU VAT. It allows the virtual intermediary a credit for the full amount of the tax it has paid against the tax it collects from the guest.

*Room remarketers.* A carrot and stick is applied to virtual intermediaries under the amendments to the Hotel Room Occupancy Tax. Not only is the virtual intermediary (room remarketer) deemed to be an *operator* (required to collect the tax from the guest it resells to) but it is allowed a credit for the full amount of the tax it has paid to the owner

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class certification under Fed. R. Civ. P. 23 because it is not clear that all the members of the class imposed a hotel tax that was similar to the Nassau County hotel tax).

<sup>19</sup> A room remarketer is defined in New York Tax Law §1101(c)(8), effective September 1, 2010 as:

A person who reserves, arranges for, conveys, or furnishes occupancy, whether directly or indirectly, to an occupant for rent in an amount determined by the room remarketer, directly or indirectly, whether pursuant to a written or other agreement. Such person's ability or authority to reserve, arrange for, convey, or furnish occupancy, directly or indirectly, and to determine rent therefor, shall be the "Rights of a room remarketer". A room remarketer is not a permanent resident with respect to a room for which such person has the rights of a room remarketer.

<sup>20</sup> New York Tax Law §1101(c)(4), effective September 1, 2010.

<sup>21</sup> In an abundance of caution, New York also modified the definition of *occupant*. Prior to Chapter 57 of the Laws of 2010 an occupant was defined as:

A person who, for a consideration, uses, possesses, or has the right to use or possess, any room in a hotel under any lease, concession, permit, right of access, license to use or other agreement, or otherwise.

After Chapter 57 of the Laws of 2010 an occupant is defined as:

A person who, for a consideration, uses, possesses, or has the right to use or possess, any room in a hotel under any lease, concession, permit, right of access, license to use or other agreement, or otherwise. "Right to use or possess" includes the rights of a room remarketer as described in paragraph eight of this subdivision.

Thus, a room remarketer (virtual intermediary) is an occupant of a New York room when it acquires the right to "use or possess" the room it re-sells to the eventual guest.

of the hotel in its capacity as an *occupant* of the same room. This is precisely how the EU VAT operates.

A simple example using a 10% tax rate is helpful. If a virtual intermediary secures a room in New York for \$50 that it resells to a guest for \$70, it would: (a) pay a tax of \$5 to the hotel owner, (b) collect a tax of \$7 from the guest, and then (c) deduct the \$5 it paid from the \$7 it collected and remit \$2 with its return. In this manner the correct amount of tax (\$7) is remitted on the true consumption base (\$70). However, it is remitted in slices (\$5 from the hotel owner, and \$2 from the virtual intermediary).

Room remarketers must register, and receive a certificate of authority number.<sup>22</sup> Returns are due quarterly.<sup>23</sup> Only registered operators qualify for a refund or credit of taxes paid, and they must furnish their certificate of authority number and the number of the *operator* of the hotel to whom they paid tax.<sup>24</sup> An application for credit or refund is filed using Form AU-11, *Application for Credit or Refund of Sales or Use Tax*.<sup>25</sup> Just as under the EU VAT room remarketers are allowed to immediately take the credit for the tax paid (to the hotel *operator*) on the return where they report the amounts they have collected from the guest. The tax remitted is a net amount.

If an application for credit has been filed, the room remarketer may immediately take the credit on the return that is due coincident with the application for credit, or immediately after the room remarketer files the application for credit. However, the taking of the credit on the return is deemed to be part of the application for credit.<sup>26</sup>

Thus, just as under the EU VAT,<sup>27</sup> a room remarketer in New York remits tax based on the value it has added to the supply. The remarketer's base is the full amount charged to its customer (not merely the amount for the accommodation), and will include any mark-up added by the remarketer.<sup>28</sup>

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<sup>22</sup> New York Tax Law §1134(a)(1), effective September 1, 2010. This is equivalent to the requirement under the EU VAT that a taxable person must register [VAT DIRECTIVE, ART. 9(1)], and receive a VAT identification number [VAT ID] [VAT DIRECTIVE, ART. 214]. The SIXTH COUNCIL DIRECTIVE of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover tax – Common system of value added tax: uniform basis of assessment (77/388/EEC) 1977 O.J. (L 145) 1 was repealed and replaced on November 28, 2006 with the RECAST VAT DIRECTIVE. Council Directive 2006/112/EC on the Common system of value added tax, O.J. (L 347) 1. Citation throughout this document will be referenced VAT DIRECTIVE.

<sup>23</sup> New York Tax Law §1136(a)(1).

<sup>24</sup> TSB-M-10(10)S at 2. A similar requirement to identify taxable persons by VAT ID numbers on invoices is found under VAT DIRECTIVE, ART. 22(3). THE VAT ID has been called the “admission ticket to deduction.” AG Sir Gordon Slynn in ECJ Case 123/87 *Léa Jorion, née Jeunehomme, and Société anonyme d'étude et de gestion immobilière 'EGI' v Belgian State*.

<sup>25</sup> Available at: [http://www.tax.ny.gov/pdf/current\\_forms/st/au11\\_fill\\_in.pdf](http://www.tax.ny.gov/pdf/current_forms/st/au11_fill_in.pdf)

<sup>26</sup> TSB-M-10(10)S (August 13, 2010) at 2.

<sup>27</sup> VAT DIRECTIVE, ART. 206.

<sup>28</sup> New York State Department of Taxation and Finance, Office of Tax Policy Analysis, Taxpayer Guidance Division, *Summary of 2010 Sales and Use Tax Budget Legislation*, TSB-M-10(18)S (December 6, 2010) at 2.

In addition, rent subject to the sales tax on occupancy of a room or rooms in a hotel now includes any service or other charge or amount paid as a condition of occupancy to a

The constitutionality of this tax base has been challenged in the New York Supreme Court of New York County. The challenge was unsuccessful. The virtual intermediary community was particularly concerned that under these rules, "... Remarketers are now liable for informing the consumer of the breakdown of the HROT (Hotel Room Occupancy Tax) between the rent and service fees ..."<sup>29</sup>

This provision in the law effectively allows consumers to compare fees among remarketers, as well as identify the actual price charged for the room by the hotel. The further contention in the suit was that by including the remarketer's fees in the base that New York was in fact imposing "... new tax on travel booking services ..."<sup>30</sup> This argument was also rejected.

### CONCLUSION

For all intents and purposes, New York has adopted a limited purpose, European-style, credit-invoice VAT to solve the problem presented in the Hotel Room Occupancy Tax by virtual intermediaries. Without raising rates or expanding the tax base New York City expects to receive significantly more revenue from the Hotel Room Occupancy Tax in 2011 and 2012.<sup>31</sup>

If the amendments to New York's Hotel Room Occupancy Tax (the New York VAT) attract the benefits normally attributed to VAT adoption (as opposed to the retail sales tax) we should see two results: (1) a larger and more stable and revenue flow into the Treasury because of the VAT's fractioned payment mechanism, and (2) a more easily audited tax because of the VAT's self-enforcement characteristic.

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room remarketer. Accordingly, the full amount charged by a room remarketer to its customer for the right to occupy a room in a hotel in New York State constitutes rent for occupancy of a room in a hotel, and is subject to sales tax. Furthermore, since the new law provides that in these circumstances, a room remarketer is an operator of a hotel, the room remarketer must collect the sales tax, and where applicable, the fee of \$1.50 per unit, per day imposed in New York City (NYC \$1.50 fee) from its customer, and remit the amount collected to the Tax Department.

<sup>29</sup> *Expedia, Inc. v. The City of New York, Department of Finance*, 650761/09 (October 29, 2010) at ¶5.

<sup>30</sup> *Id.*, at ¶10.

<sup>31</sup> New York City Independent Budget Office, *Analysis of the Mayor's Preliminary Budget for 2012 – IBO's Reestimate of the Mayor's Preliminary Budget for 2012 and Financial Plan through 2015*, (March 2011) at 26 indicates that Hotel Room Occupancy Tax revenues are expected to expand significantly. Although attributed in part to increased tourism in New York City, these increases coincide with the conversion of the retail sales tax on hotel accommodations to a VAT. The allegations raised by the virtual intermediaries in *Expedia, Inc. v. The City of New York, Department of Finance* support the inference that the New York VAT is at least partly responsible for these anticipated increases. The New York City Independent Budget Office observes:

Hotel occupancy tax collections for the first seven months of 2011 (July 2010 – January 2011) recorded a 20.9% increase compared to the same period in 2010 and this strong growth is expected to continue through the second half of the year. For 2011, IBO forecasts tax revenue of \$421 million – growth of 16.6% above 2010 revenues of \$361 million.

Available at: <http://www.scribd.com/doc/51113671/13/Hotel-Occupancy-Tax>

*Fractioned payments.* This principle is so central to the EU VAT that it is generally described as a leading feature of the tax, and a major reason for adopting it.<sup>32</sup> In the case of the New York Hotel Room Occupancy Tax revenue will be remitted in two parts (fractioned payments) – the first by the hotel owner after an initial sale to a remarketer, and the second by the remarketer when he makes the onward sale to the guest.

The consumption tax base of the New York Hotel Room Occupancy Tax is not expanded by the amendments. In the example used in this paper, the true measure of consumption, the price the guest actually paid for the room, is \$70. Just because the remarketer pays \$50 and characterizes the additional \$20 he charges for the room as a fee attributable to his “demand collection system,” does not change the guest’s subjective valuation for the room. Both the US retail sales tax and the EU VAT measure the tax base subjectively – the value (in money) placed on the supply by the final consumer.

*Self-enforcement.* Although this characteristic of the VAT is under serious challenge in the fully developed EU VAT<sup>33</sup> – notably when exemptions, intangibles, and cross-border fact patterns are involved<sup>34</sup> – the simplicity of the New York Hotel Room

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<sup>32</sup> Fractioned payments is considered a bedrock principle by the International Monetary Fund’s study of VAT. See: Liam Ebrill, Michael Keen, Jean-Paul Bodin & Victoria Summers, *THE MODERN VAT 3*, at Box 1.1 indicating that the fractioned payment mechanism makes the VAT stable, secure, and eliminates tax-distortions in the market (emphasis added):

The key features of the Value-Added Tax are that it is a broad-based tax levied at multiple stages of production, with – crucially – taxes on inputs credited against taxes on output. That is, while sellers are required to charge the tax on all their sales, they can also claim a credit for taxes that they have been charged on their inputs. The advantage of such a system is that *revenue is secured by being collected throughout the process of production* – unlike a retail sales tax – but without distorting production decisions, as, in particular, a turnover tax does.

The ABA description is similar, but places an emphasis on comparative revenue yield. See: Alan Schenk, reporter, *Value Added Tax – A Model Statute and Commentary 2*:

An invoice method VAT may be viewed as *comparable to a retail sales tax collected in installments* because, with the same tax base and rate, a multistage VAT and a single stage retail sales tax that are shifted to consumers will raise the same of revenue.

<sup>33</sup> European Commission, *Green paper – On the future of VAT: Towards a simpler, more robust and efficient VAT system* (COM(2010) 695/4 indicating at 3-4:

After some 40 years, the time has come to have a critical look at the VAT system with a view to strengthening its coherence with the single market, its capacity as a revenue raiser by improving its economic efficiency and robustness, and its contribution to other policies whilst reducing the cost of compliance and of collection. ... Any such improvements require a comprehensive VAT system that can adapt to changes in the economic and technological environment and is solid enough to resist attacks of fraud of the kind experienced in recent years.

<sup>34</sup> For example, consider: Richard T. Ainsworth, *MTIC Fraud Infects Tradable CO2 Permits*, 55 TAX NOTES INT’L 733 (Aug. 31, 2009) (discussing structural problems in the EU VAT allowing fraud in cross-border tradable services); Richard T. Ainsworth, *CO2 MTIC Fraud – Technologically Exploiting the EU VAT (Again)*, 57 TAX NOTES INT’L 357 (Jan. 25, 2009) (predicting the range of services potentially subject to VAT fraud in the EU); Richard T. Ainsworth, *The Italian Job – Voice Over Internet Protocol MTIC Fraud in Italy*, 58 TAX NOTES INT’L 721 (May 31, 2010) (examining the fraud in VoIP at Italia Telecom and Fastweb); Richard T. Ainsworth, *VAT Fraud: The Tradable Service Problem*, 61 TAX NOTES INT’L

Occupancy Tax allows this traditional strength of the VAT to shine.<sup>35</sup> Self-enforcement is one of the principle reasons that countries have switched from a retail sales tax to a VAT.<sup>36</sup>

Self-enforcement in the context of the Hotel Room Occupancy Tax means that because (a) all New York remarketers must register and pay tax on the rooms they purchase for re-sale, and (b) because the tax paid to the hotel is refundable *only if* the remarketer collects and remits tax from the guest, then (c) the structure of the tax compels compliance. In other words, the Hotel Room Occupancy Tax is self-enforcing because remarketers cannot avoid paying tax to the hotel, and would be foolish to forgo a refund of this amount by not collecting tax on the resale.

As a result, in these difficult economic times when the call for “no new taxes” is heard in tandem with a demand for more revenue to pay for necessary programs, New York seems to have accomplished the impossible. By adopting a limited purpose, European-style, credit-invoice VAT in the hotel tax it has increased revenue and decreased enforcement costs without raising rates or expanding the tax base. Other jurisdictions should take notice.

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217, 218-20 (January 17, 2011) (discussing the morphing of Missing Trader Intra Community fraud into Missing Trader Extra Community fraud).

<sup>35</sup> Liam Ebrill, *supra* note 32, at 140 indicates:

VAT literature initially emphasized the self-checking mechanism of the VAT (through the chain of invoices that are required at each stage through the retailer). This could be seen as consistent with implementing self-assessment procedures – if the VAT is a “self-enforced” tax, it should also be “self-assessed.”

<sup>36</sup> Ben Terra, SALES TAXATION – THE CASE OF THE VALUE ADDED TAX IN THE EUROPEAN COMMUNITY (1988) at 149 notes (citing to the Canadian Department of Finance TAX REFORM REPORT (June 1987) at 27:

The difference of VAT, as a multi-stage sales tax and the retail sales tax is one of degree. However, the retail sales tax, by virtue of its technique of levying, has a greater susceptibility to non-compliance.

VAT, by dispersing the collection of the tax over a number of points, reduces both the incentive to misreport and the revenue consequences of misreporting. On balance a VAT is superior to a RST in this regard.