

# MAKING SENSE OF MANDATORY RESORT FEES

APRIL 10, 2018



More than 1,000 hotels in the U.S. require guests to pay a mandatory resort fee, stated as a fixed dollar amount per room per night of occupancy, in addition to the base room rate. According to the American Hotel & Lodging Association (AHLA), approximately 7% of U.S. hotels charge resort fees. Resort fees cover such services as parking, phone calls, in-room Wifi, daily bottled water, coffee maker, health club access, and so on. Included services vary from hotel to hotel.<sup>1</sup> Hotels still include some services such as housekeeping, basic toiletries and television in their base room rate. By making the resort fee mandatory, a resort-fee hotel is bundling some services with the room but is disclosing a separate fee. The average resort fee in the U.S. is around \$21.<sup>2</sup> Resort fees generate about \$2.7 billion in annual revenues to domestic hotels.<sup>3</sup> The number of resort fee hotels and resort fee revenues in the U.S. are increasing rapidly.

In Hawaii, there are at present, over 100 hotels that have mandatory resort fees; nightly per room fees range from \$5 to \$40, excluding taxes.<sup>4</sup> (According to the Hawaii Tourism Authority there were 153 hotel properties in Hawaii in 2017.<sup>5</sup>) More expensive hotels tend to bundle together more amenities and charge higher resort fees; budget hotels provide only basic services and generally have no resort fees. Travel-Hawaii.com estimates Hawaii's resort-fee hotels collected \$271 million in resort fees in 2015.<sup>6</sup>

Bundling more and upgraded amenities is not unique to tourist accommodations. First class airfare includes meals and alcoholic beverages, more space and more comfortable seats, and early boarding; in the economy section, passengers typically have to pay extra, and even then they may not be able to purchase first-class amenities. But airlines do not partition first class airfare into two parts, one for transportation and another for amenities. A less obvious example of bundling is when businesses offer physical commodities in different sizes. For example, rice comes in large and small bags; a 25 lb. bag of rice represents 25 units of a 1 lb. bag. Supermarkets display a single price for the large bag of rice on the shelf, although it may also disclose the price per unit separately in smaller print.

Hotels are required to disclose their resort fees to would-be guests at the time of booking, but not when the room rates are initially displayed. For example, when a consumer accesses a hotel's website and searches for room rates, what the hotel website displays prominently to the potential guest at first inquiry is the base room rate. It may take another or several clicks elsewhere on the website to find out that there is also a mandatory resort fee and the specific services (if disclosed) the fee covers. When the booking is finally made, a cost summary is presented to the guest detailing the price of the room, taxes, and mandatory resort fee (if any). The practice of separating a total price into several prices is referred to in academic literature as partition pricing, and disclosing one of the component prices early and another later in the purchasing process is referred to as drip pricing. Resort fee hotels employ both pricing strategies.

<sup>1</sup> See, for example, [ResortFeeChecker.com](http://ResortFeeChecker.com). Included services may not be exhaustive.

<sup>2</sup> Elliott, Christopher, "Hotel resort fees, hidden charges bemoaned by travelers are climbing higher than ever", *washingtonpost.com*, July 20, 2017 at [https://www.washingtonpost.com/lifestyle/travel/hotel-resort-fees-hidden-charges-bemoaned-by-travelers-are-climbing-higher-than-ever/2017/07/20/a56256d0-68b1-11e7-a1d7-9a32c91c6f40\\_story.html?utm\\_term=.f27e17af864b](https://www.washingtonpost.com/lifestyle/travel/hotel-resort-fees-hidden-charges-bemoaned-by-travelers-are-climbing-higher-than-ever/2017/07/20/a56256d0-68b1-11e7-a1d7-9a32c91c6f40_story.html?utm_term=.f27e17af864b); also Elliott, Christopher, "Mandatory resort fees are on the rise—again," *Chicago Tribune*, July 28, 2017 at <http://www.chicagotribune.com/lifestyles/travel/ct-mandatory-resort-fees-on-the-rise-20170728-story.html>.

<sup>3</sup> <https://hotellaw.jmbm.com/resort-fees-2-7-billion-issue.html>

<sup>4</sup> <http://travel-hawaii.com/hawaiiresortfees.html>

<sup>5</sup> <http://www.hawaii-tourism-authority.org/default/assets/File/reports/accommodations/2017%20VISITOR%20PLANT%20INVENTORY%20REPORT%20-%2001-17-2018.pdf>

<sup>6</sup> <http://travel-hawaii.com/hawaii-resort-fee-study.html>

Critics of resort fees argue that not disclosing the total price (inclusive of resort fees) at initial inquiry makes it difficult for consumers to comparison shop for the best deal. A January 2017 study released by the Federal Trade Commission (FTC) finds that (p. v):<sup>7</sup>

separating mandatory resort fees from posted room rates without first disclosing the total price is likely to harm consumers by increasing the search costs and cognitive costs of finding and choosing hotel accommodations. In this situation, a consumer's choice is either to incur higher total search and cognitive costs or to make an incomplete, less informed decision that may result in a more costly room, or both.

The Attorneys General for the District of Columbia and 46 states initiated a nation-wide investigation in 2016 to ascertain whether resort fee hotels are engaging in deceptive price advertising.<sup>8</sup>

The American Hotel & Lodging Association (AHLA) defends mandatory resort fees by claiming that resort fees “were created in an effort to provide consumers with the best value by grouping amenity fees into one cost. If consumers were charged individual fees for all amenities, the cost would likely be prohibitive.”<sup>9</sup> That is assuming guests use “all amenities”. When resort fees are mandatory, guests pay for hotel amenities they do not use.<sup>10</sup>

In his March 20, 2018 appearance before the Hawaii State Legislature, House Committee on Tourism, President and CEO of the Hawaii Lodging & Tourism Association testified that “Hotel surveys have revealed that guests prefer an all-inclusive resort fee rather than being charged for each service used, as was the practice in the past.”<sup>11</sup> FTC notes that “hotels can still bundle the same resort services with the room and charge the same total price.” Most importantly, resort fee hotels should disclose the total price at first inquiry and not only the posted room rate, so the would-be guest would not be misled into thinking that the price of the room is less than what it actually is. For the same reason, the U.S. Department of Transportation is expected to soon require airlines to disclose fees for carry-on and checked luggage at the start of fare inquiry.<sup>12</sup>

<sup>7</sup> Sullivan, Mary W., *Economic Analysis of Hotel Resort Fees*, Bureau of Economics, Federal Trade Commission, January 2017 at <http://uhero.hawaii.edu/assets/TaxationOfTimeshareOccupancy.pdf>.

<sup>8</sup> In the Superior Court of the District of Columbia, Civil Division, District of Columbia v. Marriot International, Inc., Case No. 17-0003900, Filed June 7, 2017.

<sup>9</sup> <https://www.ahla.com/issues/resort-fees> Hoteliers explain that separating the base room rate from resort fees also allows hotels to reduce payments to travel agencies for hotel room bookings/sales. (Sullivan, 2017, p.3.) Adams and Yellen summarize economic explanations for commodity bundling. Briefly, cost savings, complementarity in consumption, and the ability to sort consumers by their willingness to pay (reservation prices) explain commodity bundling. (Adams, William James and Janet L. Yellen, “Commodity Bundling and the Burden of Monopoly,” *Quarterly Journal of Economics*, Vol. 90, No. 3, August 1976, pp. 475-498.)

<sup>10</sup> The same complaint is frequently lodged against television cable service which typically bundles many more channels than what subscribers watch. However, research suggests that unbundling cable service may not save consumers money. Barro, Josh. “Why Unbundling Cable Would Not Save You Money,” *The New York Times*, May 15, 2014 at <https://www.nytimes.com/2014/05/15/upshot/why-unbundling-cable-would-not-save-you-money.html>.

<sup>11</sup> [https://www.capitol.hawaii.gov/Session2018/Testimony/SB2699\\_SD2\\_TESTIMONY\\_TOU\\_03-20-18\\_PDF](https://www.capitol.hawaii.gov/Session2018/Testimony/SB2699_SD2_TESTIMONY_TOU_03-20-18_PDF) That may be true. My friend, Roger Blair (chair of economics at the University of Florida) notes that transactional efficiencies also make bundling profitable – no need to contract over every component of a hotel stay. Both hoteliers and consumers benefit.

<sup>12</sup> Silk, Robert, “Bag-fee disclosure rule is back,” *Travel Weekly*, March 22, 2018 at <http://www.travelweekly.com/Travel-News/Airline-News/Bag-fee-disclosure-rule-is-back>.

The downside for hotels if they adopted FTC's suggestion is that they may be required to pay more local hotel occupancy taxes. Hawaii Revised Statutes Chapter 237D states: the transient accommodations tax (TAT) is "assessed and collected each month...on the gross rental or gross rental proceeds received from furnishing transient accommodations." (The current tax rate is 10.25%.) A tax department brochure (Tax Facts 96-2) explains that "gross rental proceeds do not include separate charges for guest amenities such as meals, telephone calls, and laundry services, and it also does not include any GET (general excise tax) or TAT that is visibly passed on to the guest or tenant. However, gross rental proceeds do include fees such as maintenance fees, cleaning fees and management fees that are not usually charged separately to guests or tenants."<sup>13</sup> Thus, amenities offered in conjunction with the room and charged separately are exempt from the TAT, but amenities that are included in the base room rate are subject to the TAT. Not surprisingly, some hotel amenities which used to be covered by the basic room rate (e.g. in-room coffee maker and in-room safe) when resort fees were not widely employed are now included in the mandatory resort fee. The brochure further explains that if a tour package includes airfare, hotel room, and car rental, "only the portion of the total package price allocated to the hotel room is subject to TAT."<sup>14</sup>

One could make a strong case that mandatory resort fees are an inseparable part of the "gross rental proceeds received by hotels from furnishing transient accommodations" because resort fee hotels will not furnish a room to a would-be guest unless he/she agrees to pay both the base rate and the resort fee. The two, together, make up the full rental price of the hotel room, and thus all the proceeds received from the occupant should be subject to the TAT under current law. As the expression goes, "If it [the resort fee] looks like a duck [room rate], swims like a duck, and quacks like a duck, then it probably is a duck."

Those who disagree can point to the example in the brochure that explains that airfare and car rental bundled with lodging in a prepaid package are not subject to the TAT because they are different products. To illustrate, consider the bundle of amenities covered by the mandatory resort fee at the Outrigger Waikiki Beach Hotel. The hotel's Waikiki Connection Fee of \$30 per room per night plus taxes provides unlimited rides on the Waikiki Connection Trolley, Wi-Fi, local and international phone calls up to 60 minutes daily, two bottles of water daily in room, local weekday newspaper, free breakfast for children five years and younger with purchase of an adult meal from menu at the hotel's restaurants, daily Hawaiian cultural activities (e.g. ukulele lessons, flower lei making, hula lessons, etc.), Outrigger souvenir tote bag per room, and shopping and dining coupon book with savings at over 40 retailers.<sup>15</sup> The argument can be made that hula and ukulele lessons, trolley rides to visitor attractions, bottled water and tote bag, and discounts at the hotel restaurants is each a different product from the hotel room and, like airfare and car rental in a package tour, should also be exempt from the TAT. Pushing this argument is problematic because it makes the TAT impossible to administer; one has to first define what is a hotel product. That is a difficult task. Is in-room Wifi and a hotel room a single product or separate products? Luxury hotels come with added and upgraded amenities; are the extra and luxury amenities separate products from the room? (A luxury hotel would not be luxurious without premium amenities.)

In actual practice, Hawaii hotels pay the state's general excise tax (GET) on both the base room rate and mandatory resort fee, but pay the TAT only on the base room rate, presumably because the mandatory fee is "separately charged". If hoteliers combined the base room rate and the mandatory resort fee into a single price, the entire amount would be subject to the TAT. To eliminate any ambiguity in the current law, state lawmakers introduced legislation (SB 2699 SD2) during the 2018 legislative session to apply the TAT to mandatory resort fees by including them in the definition of gross rental proceeds of transient accommodations.<sup>16</sup> It is expected to generate about \$20 million more TAT revenues per year.

<sup>13</sup> State of Hawaii, Department of Taxation, *Tax Facts 96-2, Transient Accommodations Tax*, Revised, March 2018 at <http://files.hawaii.gov/tax/legal/taxfacts/96-2.pdf>.

<sup>14</sup> My experience has been that this is extremely difficult, and probably impossible, to do accurately.

<sup>15</sup> <https://www.outrigger.com/landing-pages/resort-fees/waikiki-connection-fee>

<sup>16</sup> <https://legiscan.com/HI/text/SB2699/id/1767837/Hawaii-2018-SB2699-Amended.html>

Hawaii's lawmakers are keen on raising more revenue to pay for future spending obligations, and exporting taxes to tourists is viewed as a politically safe way to do it.<sup>17</sup> In this case, it is also consistent with maintaining horizontal equity between resort-fee and non-resort fee lodging suppliers. Sound tax policy does not tax goods and services differently depending on how the price is presented to the consumer.

Hawaii Tourism Authority (HTA) CEO recently presented testimony at the Legislature against SB 2699 SD2 stating that "HTA is opposed to measures that would increase the cost for residents and visitors to vacation in the Hawaiian Islands."<sup>18</sup> Indeed, higher taxes on lodging means higher after-tax prices for lodging. Hoteliers and tourists are made worse off, but residents (overall) gain from additional tax revenues collected that could be spent on them, as long as not too many visitors are deterred from visiting Hawaii.<sup>19</sup> However, there could be unintended consequences as the higher cost of hotel rooms confers an even more of a competitive edge to short-term vacation rentals that operate illegally in Hawaii and do not pay the TAT.<sup>20</sup> Taxing mandatory resort fees may also induce hoteliers to unbundle some amenities to lower their tax liabilities; this could reduce anticipated tax revenues to the State.

(I am grateful to Robert Ebel and Roger Blair for helpful comments during the writing of this essay. All errors are mine.)

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*UHERO Briefs are circulated to stimulate discussion and critical comment. The views expressed are those of the individual authors.*

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<sup>17</sup> Dayton, Kevin, "Even with collections booming, lawmakers seek tax increases," *Honolulu Star Advertiser*, March 11, 2018, pp. A1 and A14.

<sup>18</sup> [https://www.capitol.hawaii.gov/Session2018/Testimony/SB2699\\_SD2\\_TESTIMONY\\_TOU\\_03-20-18\\_.PDF](https://www.capitol.hawaii.gov/Session2018/Testimony/SB2699_SD2_TESTIMONY_TOU_03-20-18_.PDF)

<sup>19</sup> Mak, James. "Taxation of Travel and Tourism," in Larry Dwyer and Peter Forsyth (eds.), *International Handbook on the Economics of Tourism*, Cheltenham, UK: Edward Elgar Publishing Limited, 2006, pp. 251-265. Most research indicates that demand for visitor accommodations is not very sensitive to changes in room rental prices.

<sup>20</sup> A recent study on the impact of Airbnb on hotel pricing and occupancy in a number of major cities is inconclusive. Honolulu was not included in the study. King, Danny, "Airbnb's impact on hotel pricing, occupancy inconclusive, study says," *Travel Weekly*, January 19, 2017 at <http://www.travelweekly.com/Travel-News/Hotel-News/Airbnb-impact-hotel-pricing-occupancy-inconclusive-study-says>