



ISSUE BACKGROUNDER

INDEPENDENCE INSTITUTE

MYOPIA IN GLENDALE

The Unintended Consequences of Hotel Occupancy Taxes

Glendale Colorado is contemplating an increase in the hotel occupancy tax rate. Glendale is not the first city in Colorado to attempt to boost revenue by imposing higher hotel occupancy taxes. This tax appeals to government officials because the tax falls primarily on travelers from outside the city, rather than on residents. However this view of higher hotel occupancy taxes is myopic, as revealed by New York's experience.

New York increased hotel occupancy taxes by 5% in 1990. That increase left New York City with the highest occupancy tax of any city in the country. The impact of the increase in the occupancy tax was predictable. Convention travelers and tourists chose other cities with lower tax rates. Jobs were lost not only in the hotel industry, but also in a wide range of industries providing services to travelers. A recent economic analysis reveals that New York lost more in other state and local tax revenues than it gained from the boost in occupancy tax revenues.¹ This idea is hard to accept, but there are numerous examples of this perverse impact of higher tax rates on tax revenues at both the national and local level.

One might argue that the experience in New York, with the highest hotel occupancy rates in the country, is not relevant to Colorado. But in fact there is even more reason to expect this perverse

outcome if a city such as Glendale increases hotel occupancy tax rates. This is a very competitive hotel market in which hotel occupancy taxes are lower than the national average. For example, the hotel occupancy tax in Denver is 6.75% of the average room price, which is significantly below the average for other major cities in the U.S. It would be very easy for travelers to shift hotels from the City of Glendale to Denver since they serve basically the same market. Therefore, we would expect even a modest increase in occupancy tax rates in Glendale to result in a significant reduction in the demand for hotel rooms. We would also expect the decrease in travelers to reduce other tax revenues, offsetting the effects of the higher occupancy tax rates. Of course the magnitude of this response could only be estimated with a more rigorous analysis comparable to that conducted for New York. Nonetheless, government officials contemplating the increased hotel occupancy tax rate for Glendale should not be myopic in ignoring the perverse impact of such taxes on tax revenues.

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¹Charles W. de Seve, 'Update on The Destructive Impact of New York's Hotel Occupancy Tax' American Economics Group, Inc. Washington, D.C. 1994.