Bed Tax Incidence

Refer to the reading by Melinda Burns of the Santa Barbara News-Press on Measure B, the proposed increase (which subsequently passed) in the bed-tax in the City of Santa Barbara to pay for creek and beach clean-up.1 You work for the Mayor's office who has asked you to prepare a one-page memo (with supporting appendices if necessary) outlining to her who in fact will end up paying for this clean-up and who will benefit. As usual, she would like the memo backed up by analysis in an appendix.

Admittedly, the data available to you is quite sparse. But that is often the case. Use what information you have or can find and make assumptions in other cases.

Some “facts/oversimplifications” you may assume:
1. There are 3,500 hotel rooms in the City of Santa Barbara and 1,500 hotel rooms to the west on the Southcoast, including in Goleta. Assume all these rooms are identical and people don’t really care if they stay in Goleta or the City of Santa Barbara. But that’s it – forget about rooms in Montecito, etc.
2. The variable cost of providing a hotel room (electricity, maid service, other labor costs, etc) is $30 per room: $20 for labor (maids, clerks, etc) and $10 for non-wage expenses like electricity. About the only thing excluded is building construction and maintenance costs, including mortgage payments.
3. The (linear) demand is such that at a price of $100 per room, demand is for 6,000. If the price went to $200, the demand would be cut in half.
4. Assume the bed tax is $10 per room per night in the City of Santa Barbara.

Issues to be covered:
1. Identify the groups of people who might be positively or negatively impacted directly by the tax (not by the cleanup). Include tourists, hotel owners, workers, others. Discuss the nature of their impact (10 points).
2. Identify the groups of people who might be positively or negatively impacted directly by the cleanup. Include tourists, hotel owners, workers, residents of SB, others. Discuss the nature of their impact (10 points).
3. Identify qualitatively the impact of the tax and the cleanup in terms of income classes and in terms of residents and nonresidents (10 points).
4. Show graphically the effect of a $10 tax on beds covering the entire South Coast (including Goleta) on prices of hotels. This involves showing the supply of hotel rooms as well as the demand. Be as accurate as possible, using as much of the above information as you can. (10 points).
5. Show graphically the effect of the $10 tax on beds in Santa Barbara city (no tax elsewhere) on the price of hotels in Santa Barbara city (compared to no tax). (10 points).
6. In terms of the direct incidence of the tax (ie, excluding creek cleanup), identify who ultimately pays for the tax. Try to be as quantitative as possible and support your arguments. (20 points)
7. In your memo to her, be as constructive as possible in providing information that is useful to a political decision-maker and supported. (30 points)