



# Staff Report

## City of Manhattan Beach

**TO:** Honorable Mayor Aldinger and Members of the City Council

**FROM:** Robert V. Wadden Jr., City Attorney; Bruce Moe, Finance Director

**DATE:** September 4, 2007

**SUBJECT:** Approve Retainer Agreement With The Law Firms of Kiesel, Boucher & Larson L.L.P. and Baron & Budd, P.C. to Represent the City On a Contingency Basis As a Participant In a Class Action Lawsuit to Collect Unpaid Transient Occupancy Tax From On-Line Hotel Booking Agents.

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### **RECOMMENDATION:**

Staff recommends that the City Council approve the proposed retainer agreement for representation in the pending Transient Occupancy Tax class action and authorize the City Manager to execute it.

### **FISCAL IMPLICATION:**

No immediate fiscal impact will result from this action as the retainer agreement is a contingency agreement and will not involve any immediate output of funds. Should the class action ultimately succeed the City may recover revenue from unpaid transient occupancy tax.

### **BACKGROUND:**

Several California cities, including the cities of Los Angeles and San Diego, have filed a class action law suit against on-line hotel booking agents such as Hotels.com and Expedia for failing to pay transient occupancy tax ("TOT") on the full consumer cost of hotel rooms they book to consumers. Unless the City participates in the class action it may be barred from future recovery of the unpaid tax.

### **DISCUSSION:**

#### **(a.) The Legal Issue**

The City of Manhattan Beach levies a tax on any transient rental which is 30 days or less in duration. The tax is ten percent (10%) of the retail room rate and while it is paid by the occupant it is collected by the party to whom the rental fee is paid. In most cases this is a hotel. However in recent years on-line booking agents have begun renting blocks of rooms from hotels at discount rates and then offering them over the internet at a higher rate. At the time the hotels collect the price of the reserved block of rooms they collect a transient occupancy tax which is ten percent of the rate being charged the agents which is then added to the cost of the room. When the agents book the room over the internet to travelers an appropriate percentage is added to the base rate to cover both the appropriate transient occupancy tax and a booking fee. The retail charge for the room is always higher than that being paid by the booking agent to the hotel. However, no portion

of the “taxes and fees” charge by the booking agent is turned over to the tax authority. Instead, the entire amount is pocketed by the booking agent in addition to the room rate differential. For example: company X books a block of rooms from a local hotel at \$100 per night; company X pays \$110 per night per room to the hotel which pays the \$10 to the local taxing jurisdiction; company X then rents the rooms over the internet for \$150 per night with an additional charge for taxes and fees of 10% for TOT and 3% booking fee, thus collecting \$169.50 from the traveler booking the room. However company X does not pay anything to the taxing authority and keeps the entire amount of taxes and fees as additional profit. Under its local ordinance the taxing authority should have collected \$15 per night for the rental of the hotel room in its jurisdiction but only received \$10.

(b.) The Lawsuit

The City of Los Angeles and several other cities have filed an action in Los Angeles Superior Court against Hotels.com and other booking agents to collect the difference between the TOT paid and that due on the retail rate of the room. The plaintiff cities sought to have the action certified as a “class action” so the entire issue as it affects every city in the State may be litigated. Of course this also increases the legal fees for the plaintiffs’ attorneys if there is an award or settlement. The defendants challenged the validity of the action claiming that the plaintiffs had not completed the necessary administrative process for collecting the tax before filing suit and arguing that cities have too many difference in their local TOT ordinances to constitute a coherent class. On July 27 the court ruled by granting a stay of, but not dismissing, the class action and ordering the plaintiffs to complete their administrative collection process while the action is stayed. It appears that the class action suit will be allowed to move forward once each plaintiff city has exhausted their administrative collection process. If Manhattan Beach wishes to collect unpaid TOT for rooms rented on-line at local hotels it would be prudent for the City to join the class action. To do so we must retain the attorneys representing the class to represent us.

(c.) The Agreement

The proposed Agreement is a joint agreement with the two law firms<sup>1</sup> retained by the plaintiff cities in the class action. The City is not obligated to provide any on-going fees or costs during the pendency of the lawsuit and will have no liability for fees if there is no recovery or settlement. Should the plaintiffs prevail or the matter is settled the attorneys will be entitled to either thirty percent (30%) of the “gross recovery” (including the damages award plus any statutory attorney fees) or the entire amount of any statutory attorney fees awarded, whichever is greater. In addition after calculation of these fees the city must reimburse the law firms from the remainder of the award for any costs or expenses advanced and not directly reimbursed by the settlement or judgment. The scope of services is limited to representation in the class action litigation but does include the attorneys being involved in the exhaustion of the administrative collection process.

Attachments: Legal Services Agreement

cc: Geoff Dolan, City Manager

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<sup>1</sup> There are two law firms because the law suit resulted from the consolidation of two separate actions, one involving Los Angeles and the other involving San Diego, involving separate counsel for the original plaintiffs.

## LEGAL SERVICES AGREEMENT

1. Parties. This "Agreement" is made and entered this \_\_\_\_<sup>th</sup> day of \_\_\_\_\_, 2007, by and among Kiesel Boucher Larson, LLP and Baron & Budd, P.C. ("Special Counsel") and the City of Manhattan Beach, a municipal corporation.
2. Retention of Firms Rather Than Particular Attorney. City is retaining the law firms, and attorney services to be provided to City will not necessarily be performed by any particular attorney.
3. Term. This Agreement, which is intended to fulfill the requirements of California Business and Professions Code section 6147, will begin on the date indicated above and will continue until the completion of the Litigation (defined below).
4. Scope. City hereby retains Special Counsel to represent it in litigation seeking damages, attorneys' fees, costs, and all other appropriate relief for the non-payment or underpayment to the City of transient occupancy taxes by online booking companies such as Hotels.com, Expedia.com, Travelocity and others (collectively, the "Litigation").

As provided herein, Special Counsel is authorized to take appropriate legal steps to prosecute the Litigation as it pertains to liability, damages, civil penalties, injunctive relief, interest, and restitution/disgorgement of profits and to participate in any settlement negotiations. City will be truthful and cooperative with Special Counsel, disclose to Special Counsel all facts relevant to the Litigation, keep Special Counsel reasonably informed of developments, and be reasonably available to attend any necessary meetings, depositions, preparation sessions, hearings and trial.

The City designates \_\_\_\_\_ as the authorized representative to direct Special Counsel and to be the primary individual to communicate with Special Counsel regarding the subject matter of Special Counsel's representation of the City under this agreement. This designation is intended to establish a clear line of authority and to minimize potential uncertainty, but not to preclude communication between Special Counsel and other representatives of the City.

Special Counsel will obtain prior approval from the City concerning all substantive matters related to the Litigation including dispositive motions, selection of consultants and experts, and resolution of the Litigation. The City agrees to consult in good faith with Special Counsel prior to making a recommendation regarding any such substantive matter.

5. Resources. Special Counsel and the City Attorney will provide sufficient resources, including attorney time, to prosecute the Litigation faithfully and with

due diligence. Legal services under this Agreement will be performed only by competent personnel under the supervision and in the employment of Special Counsel and City, or retained by Special Counsel as consultants. To assist in the prosecution of the case, City will provide sufficient resources to calculate damages and gather other necessary information on the transient occupancy tax.

6. Conflicts. The City may be joined in a class action. Therefore, the City might be representing its own interests in the Litigation and serve as representative of a class of government entities seeking similar relief.

The City and Special Counsel acknowledge that other individual government entities may seek to become named parties in the Litigation and be represented in the Litigation by Special Counsel. The City recognizes that there may be potential conflicts or actual conflicts of interest if Special Counsel represents other cities within the case. The City understands that it would be to its benefit for other parties to become named parties as it may enhance the case and lower expenses for the City. Accordingly, the City has conferred with the City Attorney and has determined that it is in its own best interests to waive any and all potential or actual conflicts of interest which may occur as a result of Special Counsel representing other government entities in this or similar litigation. The City therefore waives all such potential or actual conflicts of interest.

7. Representation of Related Interests. Special Counsel shall have the right to represent other individuals, business entities, municipalities, governmental agencies or governmental subdivisions in other transient occupancy tax actions or similar litigation without the consent of the City, subject to the Rules of Professional Conduct relating to conflicts of interest.
8. Compensation. The employment of Special Counsel will be on a contingency fee basis. Specifically, if Special Counsel is successful in obtaining and collecting a recovery for the City -- whether by settlement, arbitration award, Court judgment or otherwise -- Special Counsel will receive attorneys' fees in the amount of Thirty Percent (30 %) of the Gross Recovery (defined below). This fee is not set by law but is negotiable between the City and Special Counsel. The sole contingency upon which the City will pay compensation to Special Counsel is a recovery and collection on behalf of the City, whether by settlement, arbitration award, Court judgment or otherwise.

The City and Special Counsel intend to seek an order for payment by defendants of the City's attorneys' fees and Costs (as defined in paragraph 10 below), if the City prevails, in whole or in part, in the Litigation. The City agrees to use its best efforts to support any such application. If the amount of the statutory fee awarded as reimbursement for Special Counsel's time and effort, and collected from the defendants, exceeds the amount called for under the contingency fee calculation, Special Counsel shall retain all of the statutory fee awarded and

collected as a reasonable fee, in lieu of the contingency fee. If the amount of the statutory fee awarded as reimbursement for Special Counsel's time and effort, and collected from the defendants, is less than the amount called for under the contingency fee calculation, Special Counsel shall receive as a reasonable fee the amount called for under the contingency fee calculation in lieu of the statutory fee.

9. The term "Gross Recovery" shall include, without limitation, the then present value of any monetary payments agreed or ordered to be made and the fair market value of any property or services agreed or ordered to be transferred or rendered for the benefit of the City by the adverse parties to the Litigation or their insurance carrier(s), whether by settlement, arbitration award, court judgment, or otherwise, without reduction for recovery of Costs as defined in paragraph 10. Gross Recovery shall also include any statutory attorneys' fees paid by the defendants.

If payment of any part of the relief received by the City will be in the form of property or services ("In Kind"), the value of such property and services for purposes of calculating the Gross Recovery shall be calculated based on the present value, as of the time of the settlement, the final arbitration award, or final Court judgment, of the In Kind relief to be received thereafter. The attorneys' fees for the value of the In Kind relief shall be paid out of any initial lump-sum payment by the defendants. If the initial lump-sum payment is insufficient to pay the attorneys' fees in full, the balance will be paid from subsequent payments on the recovery before any distribution to the City.

If the parties disagree with respect to the value of any In Kind relief, they will proceed as follows: Within thirty (30) days each party will select an appraiser qualified to conduct an appraisal of the value of the In Kind relief. Each party's selected appraiser will thereafter meet and confer. If resolution of the dispute is not reached within sixty (60) days of the initial meet and confer, the appraisers will select a third qualified appraiser within fifteen (15) days. The third appraiser's valuation will be final and binding on the parties. Notwithstanding the foregoing, if there is *no* money recovery and the City receives In Kind relief, attorneys' fees will be based on the value of the In Kind relief, which will be determined through the mutual agreement of the parties. If the parties disagree with respect to the value of any In Kind relief, they will proceed with an appraisal process as set forth above. If there is no money recovery, and only in kind relief all attorneys' fees and Costs due Special Counsel under this Agreement shall be paid from City funds at the time of recovery and collection.

10. Costs. It will be necessary for Special Counsel to incur and advance certain court costs and other types of expenses for the City. These Costs and other expenses may include, but are not limited to, the following: filing and service fees; costs for

investigative services; travel expenses (including air fare, ground transportation, vehicle mileage, lodging and meals); deposition expenses and court reporter fees; outside trial services providers; trial equipment rental and operation fees; preparation of exhibits and graphics; the costs of briefs and transcripts on appeal, and miscellaneous copying, postage, shipping, and courier expenses. In addition, it will be necessary to employ expert witnesses. City agrees that Special Counsel may, in its discretion, employ and pay these expert witnesses, and that such expenditures shall be included within Costs.

City agrees to reimburse Special Counsel for all reasonable Costs out of its share of the Gross Recovery, after the attorneys' fee specified in paragraph 8 has been calculated and deducted.

City understands that Special Counsel may incur certain expenses, including, for example, expenses for travel, experts, and copying that jointly benefit multiple clients. City agrees that Special Counsel may divide such expenses among such clients on a reasonable basis, and deduct the City's portion of those expenses from the City's share of any recovery. Special Counsel may, in its discretion, allocate the expenses equally among the relevant clients, pro rata based on each client's share of the relief obtained, or on any other reasonable basis of which all affected clients are fully informed.

In some instances, it may be necessary for Special Counsel to retain special outside counsel to assist on matters other than prosecuting the City's claims as described in paragraph 4 above. (Examples of such instances include the following: a defendant may seek bankruptcy protection; a defendant may attempt to fraudulently transfer some of its assets to avoid paying the City's claim; a complex, multi-party settlement may require an ethics opinion from outside counsel; or a separate lawsuit may need to be filed against a defendant's insurance company). City agrees that Special Counsel, with written permission of the City, may retain such special outside counsel to represent the City when Special Counsel deems such assistance to be reasonably necessary. In such an instance, the fees of such special outside counsel shall be advanced by Special Counsel, shall be deemed a part of Costs, and as such shall be reimbursed to Special Counsel by the City from its share of the Gross Recovery. If there is no recovery, Special Counsel will be solely responsible for payment of the Costs.

11. Reasonableness. The City and Special Counsel have discussed the reasonableness of the contingency fee provided for in this Agreement, as opposed to use of an hourly rate, a fixed fee, quantum meruit, or some other possible basis for calculating the attorneys' fees to be paid to Special Counsel. The City and Special Counsel agree that under all the circumstances a contingency fee is the most reasonable and equitable way to compensate Special Counsel in light of the effort required and the risks to be undertaken in the Litigation. The City and Special Counsel further understand that the substantial effort required to prosecute

the action and the substantial Costs to be incurred by Special Counsel may not be compensated for or reimbursed if there is no recovery. Therefore, the City agrees that it will not contest the reasonableness or fairness of this contingency fee contract.

12. Possible Efforts by Defendants to Invalidate Agreement. The City and Special Counsel are aware that in the past defendants in litigation involving public entities have challenged and sought to invalidate contingency fee arrangements between public entities and outside counsel. The City and Special Counsel believe that any such challenges to this Agreement lack merit and that this contingency fee arrangement is valid and in the public interest. The City Attorney agrees to join Special Counsel in opposing any such challenge. However, in the event that this contingency fee Agreement is found to be invalid, Special Counsel agrees to continue to represent the City in the Litigation with the understanding that, if there is no recovery, the City will owe nothing for attorneys' fees or Costs. If there is a recovery (including collection of the recovery), and this contingency fee Agreement is found to be invalid, the City shall pay a reasonable fee for the services rendered, plus Costs. If the parties are unable to agree on the reasonable fee for the services rendered, or for any other disputes arising under this agreement, such disputes shall be determined by arbitration proceedings before the Judicial Arbitration and Mediation Services (JAMS).
13. Division of Attorneys' Fees. Special Counsel may divide the attorneys' fees received for the legal services provided under this Agreement with other attorneys or law firms retained as associate counsel and approved by the City Attorney in writing. The terms of the division, if any, will be disclosed to the City. The City is informed that, under the Rules of Professional Conduct of the State Bar of California, such a division may be made only with the City's written consent after a full disclosure to the City in writing that a division of fees will be made and of the terms of such division. The City will not unreasonably withhold approval of associate counsel retained by Special Counsel or unreasonably refuse to consent to a proposed division of fees among counsel.
14. Legal Services Specifically Excluded. Special Counsel does not agree to provide any representation beyond that described in paragraph 4. In particular, the City agrees that Special Counsel has no obligation or responsibility to provide representation in the following matters:
  - a. Proceedings before any federal, state or municipal administrative or governmental agency, department or board. However, with the City's permission, Special Counsel may elect to appear at such administrative proceedings to protect the City's rights.

- b. Defending any legal action against the City commenced by any person in connection with claims brought against the City related to the Litigation.

If the City wishes to retain Special Counsel to provide any legal services not provided under this Agreement, a separate written agreement between Special Counsel and the City will be required, following negotiation of and agreement on the additional compensation to be paid by City for that representation.

- 15. Power of Attorney: City gives Special Counsel a power of attorney to execute all reasonable and necessary documents connected with the handling of the Litigation, including pleadings, contracts, checks or drafts, dismissals and orders, and all other documents that the City could properly execute. The City's claims will not be settled without obtaining the City's consent.
- 16. Assignment. This Agreement may not be assigned by Special Counsel. Special Counsel is expressly employed because of its unique skills, ability and experience and, therefore, it is understood that no substitution or assignment may be made unless the City Attorney expressly approves such substitution or assignment in writing.
- 17. Attorneys' Lien. Special Counsel will have a lien to the fullest extent of California law for attorneys' fees and Costs on all claims and causes of action that are the subject of its representation of the City under this Agreement and on all proceeds of any recovery collected (whether by settlement, arbitration award, Court judgment, or otherwise).
- 18. Withdrawal of Attorney. Special Counsel may withdraw as permitted under the Rules of Professional Conduct of the State Bar of California. The circumstances under which the Rules permit such withdrawal include, but are not limited to, the following: (a) the City consents, (b) the City's conduct renders it unreasonably difficult for Special Counsel to carry out the employment effectively, or (c) the City fails to pay attorneys' fees or Costs as required by this Agreement. If Special Counsel properly withdraws from representing the City because it is required to do so by the Rules of Professional Conduct, the City agrees to compensate Special Counsel for the reasonable value of the legal services provided, plus reimbursement for Costs. In such a situation, both attorneys' fees and reimbursement of Costs will be paid by the City to Special Counsel at the time of recovery and collection by the City; provided, however, City is only obligated to compensate Special Counsel if there is a recovery and collection of the recovery.

City may discharge Special Counsel at any time, with or without cause. If the City discharges Special Counsel, City agrees to compensate Special Counsel for the reasonable value of the legal services provided plus reimbursement for Costs.



Both payment of attorneys' fees and reimbursement of Costs will be paid by the City to Special Counsel at the time of discharge.

19. Settlement. Special Counsel will not settle the City's claims without the approval of the City, which will have the absolute right to accept or reject any settlement. Special Counsel will notify the City promptly of the terms of any settlement offer received by Special Counsel.
20. Confidentiality. This Agreement establishes the relation of attorney-client among the parties hereto. Special Counsel is to hold all money and property of the City in trust for the City's benefit, is not to divulge its confidences, and is entitled to the candid cooperation of City employees in all matters related to the Litigation.
21. Disclaimer of Guarantee. Although Special Counsel may offer an opinion about possible results regarding the subject matter of this Agreement, Special Counsel cannot guarantee any particular result. The City acknowledges that Special Counsel has made no promises about the outcome and that any opinion offered by Special Counsel in the future will not constitute a guarantee.
22. Execution. This Agreement is executed in duplicate copies, and a copy signed by Special Counsel and the City is being provided to the City at the time of execution.
23. Entire Agreement. This Agreement fully expresses all understandings of the parties concerning all matters related to their agreement for specialized legal services, and this Agreement constitutes the entire agreement and understanding between the City and Special Counsel for the services to be performed.

SPECIAL COUNSEL:

CITY:

Kiesel Boucher Larson LLP

City of Manhattan Beach, A Municipal Corporation

By: \_\_\_\_\_  
Paul R. Kiesel

By: \_\_\_\_\_  
\_\_\_\_\_, Mayor/City Attorney

Baron & Budd, P.C.

By: \_\_\_\_\_  
Russell Budd