Vermont Legislative Joint Fiscal Office

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FISCAL NOTE

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S.204 An act relating to the registration of short-term rentals – Senate Economic Development, Housing and General Affairs recommendation of amendment, further amended by Senate Finance
https://legislature.vermont.gov/assets/Documents/2018/Docs/CALENDAR/sc180316.pdf#page=1

Bill Summary
The bill would require that properties in the state that meet the definition of "short-term rental[1]" must register with the VT Department of Health (VDH) on an annual basis. In order to register, the registrant would need to self-certify that the property is in compliance with public health and safety requirements and that meals and rooms taxes are remitted on a timely basis. An annual fee of $65 would be required for each property when registration documents are submitted. VDH would then issue a one-year initial certificate of compliance and would have the authority to subsequently inspect registered short-term rental properties and verify that all compliance requirements are met. Enforcement authority would lie with the Commissioner of VDH. A registrant would be required to post the certification number on a short-term rental internet platform in order to advertise on that platform. The bill would go into effect on July 1, 2018 and short-term rentals would be required to register on January 1, 2019.

Fiscal Summary - Brief

Summary of S.204 JFO *Preliminary* Costs/Revenues[2]					
		FY2019		**Future Years**	
		General Fund	Other Funds	General Fund	Other Funds
Costs (includes one-time cost but excludes optional costs)			($255,000)		($364,000) +
Revenues		$20,000-$40,000[3]	$115,000-$155,000	$190,000	$215,000
Net (red indicates an estimated shortfall)		$20,000-$40,000	($100,000-$140,000)	$190,000	($149,000) +

Projected costs estimated for the implementation of this bill exceed the total estimated short-term rental registration revenues and any potential general fund revenues in State FY2019. In future years,

[1] Per 18 VSA §4301(a)(14) a "Short-term rental" means a furnished home, condominium, or other dwelling rented to the transient, traveling, or vacationing public for a period of fewer than 30 consecutive days and for more than 14 days per calendar year.
[2] JFO estimated costs differ from costs estimated by VDH.
[3] This revenue reflects additional tax compliance as a result of audits performed by the Tax Dept. and would potentially be collected regardless of whether this bill is passed.

the special fund gap between costs and revenues would remain, but would disappear when estimated general fund revenues are included, but all revenues would be highly dependent on the impacts that this bill has on the rapidly evolving short-term rental market in Vermont. No appropriation for VDH is currently in the bill to cover staffing and other operating costs in FY19. The estimates for FY19 revenue (tax and registration) are dependent on VDH having the short-term rental registration program up and running by January 1, 2019. Any delays in implementation would very likely decrease the FY19 revenue. In future years, registration revenue would be dependent on VDH having the resources in place to monitor and verify compliance with the short-term rental registration requirement. Meals and rooms tax revenue increases, which would go to the general fund, are estimated to be minimal in initial years but the increases would compound over time. Ultimately, the best way to ensure better meals and rooms tax compliance would be for the Tax Dept. to negotiate agreements with online platforms through which the platform would collect and remit taxes on behalf of short-term rental hosts (similar to the existing Airbnb agreement). Some additional income tax compliance has been assumed as a result of this bill if it were to pass.

Fiscal Summary - Detailed

<u>Costs</u>

Costs to Implement S.204 – JFO estimates (different from VDH cost estimates)				
		SFY2019[4]		**Future Years**
		One-time	**Ongoing**	
Dept. of Health				
Staff (2.0 new FTE in FY19, up to 3.0 FTE in future years)			$115,000	$235,000 +
Operating costs			$15,000	$24,000 +
IT system upgrade		$ 75,000		
Allocated Costs			$50,000	$105,000 +
Sub-Total		*$ 75,000*	*$180,000*	*$364,000*
Registration Compliance Monitoring - *optional*			$70,000-212,000[5]	$70,000-$212,000
Total		***$75,000***	***$250,000-$392,000***	***$434,000-$576,000***

The estimates in the table above are derived from numbers provided by VDH for one-time and ongoing Departmental costs to administer the provisions of S.204, if enacted, but JFO makes different assumptions than VDH for the staffing needed to support this program. VDH estimated four new staff positions would be needed, which are as follows: Admin Service Tech (1), Program Specialist (1), and Field Inspector (2). Staff costs include salaries and benefits. JFO estimates that two of these positions would likely be needed in FY19 to get the program up and running, with an additional field inspector potentially needed in FY20 depending on compliance and/or the number of complaints received.

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[4] Ongoing costs for FY19 are estimated to be approximately 3/4 of a full year as staffing would likely take time beyond the effective date of this bill, which is July 1, 2018.

[5] Denver budgeted $70,400 for compliance monitoring in 2017. VDH estimated that compliance monitoring would be $212,000.
http://www.denvergov.org/content/dam/denvergov/Portals/723/documents/STR%20EXL%20Budget%20Request%202017.pdf

Additionally, JFO estimates that full staffing in FY19 would likely take several months, so costs for FY19 reflect 75% of a full year of costs for 2.0 FTE. There is potential for some staffing needs to be contracted out, which could result in some efficiencies and cost savings depending on the workload that this bill generates.

Operating costs are non-personal services expenses for travel, supplies, equipment. Allocated costs, or indirect costs, cover internal services (i.e. fee-for-space, VISION, ADS) and other staff support. The one-time IT system upgrade would be needed to support the new registration function. The optional cost for registration compliance monitoring would give VDH an additional tool to understand the breadth of the short-term rental market in Vermont. This type of tool has been used by Denver to determine the number of *unique* short-term rental properties in the city[6]. In future years, personnel, operating and allocated costs would likely increase incrementally, due to pay act, increased health benefit costs, and other general inflationary pressures.

It is difficult to make a direct comparison between staffing needs for a potential short-term rental program in Vermont against a similar program elsewhere because there is not currently another state that has a statewide registration program and in the cities that do require short-term rental registrations it is often to lessen housing market pressures through a stricter regulatory environment, which differs from what is envisioned in Vermont under this legislation. In Denver there are currently three positions within the Excise and Licensing Department that deal with short-term rentals – one program coordinator and two inspectors.[7] The fiscal note for Seattle's short-term rental registration legislation estimated that two FTEs would be needed.[8] In cities with registration programs, inspectors often visit properties that are suspected to be non-compliant either through platform monitoring or from complaints. If VDH implements a minimal short-term rental program limited to an online registration mechanism and education/outreach, then staffing costs would be lower but compliance would likely suffer. Greater compliance would be achieved by maintaining the capacity to enforce the new regulations, including inspections when needed.

In addition to any costs incurred by VDH to implement the provisions of this bill, there may be some costs, in staff time, to the Department of Public Safety (DPS) to train VDH inspectors (in the event that inspectors are hired) on how to verify compliance with building safety requirements when inspecting short-term rental properties. These costs would be higher in the first year of implementation and would be minimal in future years, assuming no inspector turnover and no major building safety regulation changes.

The Department of Taxes (Tax) estimates that there would be some additional business licensing activity and audit activity surrounding the implementation of this bill, but the additional activity would not require additional staffing or resources.

[6] Presentation to Denver Short-term Rental Advisory Committee by Host Compliance LLC, February 28, 2017. http://www.denvergov.org/content/dam/denvergov/Portals/723/documents/Host%20Compliance%20Presentation.pdf

[7] https://www.denvergov.org/content/dam/denvergov/Portals/723/documents/STR%20EXL%20Inspector%20Overview.pdf

[8] http://seattle.legistar.com/View.ashx?M=F&ID=5541135&GUID=606D7515-8261-43CC-A8E0-67B966715B42

Revenues

Potential Revenues from S.204				
	SFY2019		Future Years	
	General Fund	Other funds	General Fund	Other funds
Short-term rental registration revenues *(New)*	n/a	$115,000-$155,000		$215,000
Personal Income tax revenues *(Previously uncollected)*	$5,000-$10,000	n/a	$40,000	n/a
Meals & Rooms tax revenues *(Previously uncollected)*	$15,000-$30,000	n/a	$150,000	n/a
Total New Annual Revenue	***$20,000-$40,000***	***$115,000-$155,000***	***$190,000***	***$215,000***

The numbers in the table above were estimated in the analysis described in detail in the following pages of this fiscal note. The revenue numbers are highly preliminary and should be monitored closely as this bill is implemented. Research of other locations that have implemented short-term rental regulation and registration laws highlights low registration compliance and reductions in the numbers of active short-term rentals as hosts seek to avoid potential enforcement action.

Analysis

Short-Term Rentals – The Vermont Market

Several variables must be identified, either by actual data or by proxy, prior to any analysis of the possible revenues from short-term rental registration fees, or increases to meals and rooms tax remittances, and even changes to personal income taxes paid. The variables are as follows:

1. How many unique short-term rentals are there in Vermont? *Unique* for purposes of this analysis means the number of short-term rentals that are not duplicated across multiple rental platforms.
2. How much revenue does the average short-term rental generate per year?
3. What percentage of short-term rental hosts are either under-reporting or not reporting rental revenues for purposes of taxation?

Currently, no states require short-term rental registration and fee payment at the state level. However, numerous cities have enacted regulations and/or registration requirements for short-term rentals. Three cities that have registration requirements, and whose populations most closely mirror that of Vermont, are: Denver, Seattle and Portland, OR. A report from the Puget Sound Sage[9] in June 2016 estimated approximately 4,170 Airbnb listings in Seattle with an additional 2,500 listings across a small sampling of other platforms. The same report estimated the number of Airbnb listings in Portland, OR at 3,128. The number of unique short-term rentals in Denver was estimated to be 3,866 as of January 2018 in a report[10] to the Denver Short-Term Rental Advisory Committee.

[9] http://pugetsoundsage.org/wp-content/uploads/2016/12/PSS_ShortTermRentals.pdf

[10] http://www.denvergov.org/content/dam/denvergov/Portals/723/documents/STRAC_PP_1.30.18.pptx

In its 2017 report[11] to the Vermont Legislature, the Short-Term Rental Working Group indicated that a sampling across multiple rental platforms yielded approximately 5,100 listings on Airbnb and a further 10,500 listings on three other platforms. These numbers likely include duplicate properties, any lodging establishments that may advertise on short-term rental platforms and properties that do not meet the definition of short-term rental. Additionally, the sampling was taken during the busy peak summer/fall season in Vermont when property owners throughout the state may have been advertising on rental platforms. In other times of the year, tourist activity is primarily in ski resort areas, other winter sport areas or the Burlington area, which would impact short-term rental activity. The same report highlighted that there are approximately 3,600 active Airbnb hosts in Vermont, who each generate approximately $5,900 in short-term rental revenue each year. Approximately 88% of hosts only rent a single unit, 8% rent two units and the remaining hosts rent three or more units. Airbnb has an agreement with the State of Vermont to collect all meals & rooms taxes on behalf of hosts and remit the taxes to the State.

In its analysis of the potential tax impacts of S.204, the Tax Department performed a search of open meals & rooms accounts to isolate accounts with no corresponding withholding account, no business name, and with tax remittances between $200 and $9,000 over the course of a year. The lack of a withholding account generally would mean that there are no paid employees, which could mean that the account is associated with a short-term rental. Based on the results of the search, Tax found approximately 4,800 open meals and rooms accounts that meet the guidelines above. Each account represented approximately $1,500 in meals & rooms tax remittances over the course of a year, which would represent $16,700 per account in taxable revenue. This represents significantly more short-term rental revenue than what was indicated in the working group report. Based on audits of vacation rentals, the Tax Department also has estimated approximately 60% compliance with meals & rooms tax remittance.

Based on the information above, the following assumptions have been made for this fiscal note:

1. <u>Airbnb listings = ~4,000</u> (3,600 Airbnb hosts; 88% of whom rent one unit = ~3,200 units; 8% of whom rent two units = ~600 units; 4% rent three or more units, of which many are probably lodging establishments = ~200 units)
2. <u>Other listings = ~8,000</u> (4,800 meals and rooms accounts divided by 60% meals and rooms compliance rate)
3. <u>Total *unique* units = ~6,000</u>[12] (Equal to the sum of Airbnb listings and Other listings divided by 2 to solve for duplication across rental platforms and for units that don't meet the definition of short-term rentals)

Short-Term Rental Registration Fees

Several cities in the U.S. have recently enacted registration fees for short-term rentals, or similar properties. The most robust available data comes from the city of Denver, which has a short-term rental advisory committee that meets regularly and is given updates on the numbers of unique short-term rental properties in the city and the numbers that are compliant with the registration requirement in a given month. For the first six months of the registration requirement in Denver, the average

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[11] Short-Term Rental Working Group report required by Act 76 of 2017. https://legislature.vermont.gov/assets/Legislative-Reports/2017-Act76-ShortTermRental.pdf

[12] This number is higher than the unique number in cities of similar population.

compliance rate was 35%[13]. Over the first full year, the compliance rate rose to 54%. VDH has estimated that it would take 6-12 months to get a short-term rental regulatory program up and running if the needed funds were appropriated in advance. This analysis assumes that the registration program would be operational by January 1, 2019 and assumes that in the first six months compliance would be 30%-40% of 6,000 units, which would cover the remainder of SFY19. In SFY20, compliance would be estimated to be 55% of 6,000 units. The annual registration fee would be $65 and would be deposited into the Food & Lodging Fees special fund within VDH.

SFY2019 registration fee revenues: ~$115,000-$155,000
SFY2020 registration fee revenues: ~$215,000

Taxes

Per the assumption made above, Vermont has approximately 6,000 unique short-term rental units. Of that number, it is assumed that 60% of hosts are *mostly* in compliance with meals & rooms tax and personal income tax liability reporting requirements (10% unreported liability rate). The remaining 40% of hosts are assumed to be only *partially* in compliance with liability reporting (40% unreported liability rate). The current meals & rooms tax rate is 9%. For the purposes of calculating potential personal income tax liability, the lowest state marginal rate of 3.55% will be used.

For the purposes of determining the level of short-term rental revenue subject to the meals & rooms tax and/or personal income tax, this fiscal note will offer a "high" number and a "low" number. The high number represents annual remittances made to Tax by the open meals and rooms accounts discussed above, which were approximately $1,500 per account representing approximately $17,000 in short-term rental revenue per account (which could include multiple properties). The low number represents the number in the working group report as the average annual revenue brought in by Airbnb hosts, which was $5,900 (rounded to $6,000 for this analysis). This analysis assumes that the average host would deduct approximately 35% in eligible business deductions from taxable income. See the full analysis in the table at the end of this document.

The Tax Department estimates that the creation of a short-term rental registry could improve its ability to identify and audit non-compliant hosts and ultimately increase annual tax revenues to the State. The additional information provided through registration could allow Tax to more quickly identify audit priorities and to ultimately perform an additional 10 to 20 audits per year. The average audit performed by Tax on operators within the vacation rental industry results in a collection of $2,000 in unreported taxes. **With the additional capacity, this bill could generate an additional $20,000 to $40,000 in tax revenue per year from audits alone**. This analysis assumes that any uncollected taxes remitted through an audit would be 75% meals & rooms and 25% personal income. This additional, previously uncollected revenue could begin to be collected in State FY2019.

Finally, there could be some additional influx of meals & rooms tax revenue and personal income tax revenue due to the requirement to self-certify compliance with state tax law in order to acquire a short-term rental license. The amount of uncollected tax liability from the table above that might subsequently be collected by the State in future years due to the implementation of this bill, outside of Tax audit actions, is highly variable and is possibly the most unpredictable part of this fiscal note. A conservative estimate would suggest potential additional tax compliance at a rate of 10% of the unreported liability per year if S.204 were to be passed into law. **This could result in approximately**

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[13] Licensing and enforcement update to the Denver Short-term rental advisory committee on January 30, 2018. http://www.denvergov.org/content/dam/denvergov/Portals/723/documents/STRAC_PP_1.30.18.pptx

$70,000-$200,000 in additional meals & rooms tax revenue to the State each year and approximately $18,000-$52,000 in additional personal income tax revenue each year. This new revenue would likely not materialize until State FY2020 once the new law has been implemented and in place for a full year and would likely level off at approximately half of the cumulative annual uncollected tax liability. Over time, some hosts would either continue to not remit taxes going forward, would attempt to remain below the 14 day short-term rental threshold or would stop advertising on web platforms.

Estimated Potential Unreported and Uncollected Meals & Rooms Tax - STR			
	Mostly Compliant	Partial Compliant	Total
a) Unique short-term rentals	3,600	2,400	6,000
b) Annual Revenue per rental – High	$17,000	$17,000	
c) Annual Revenue per rental – Low	$6,000	$6,000	
d) M&R tax non-reporting rate	10%	40%	
e) M&R Tax owed – High (((a x b) x d) x 9%)	***~$551,000***	***~$1,469,000***	***~$2,020,000***
f) M&R Tax owed – Low (((a x c) x d) x 9%)	***~$194,000***	***~$518,000***	***~$712,000***

Estimated Potential Unreported and Uncollected Personal Income Tax - STR			
	Mostly Compliant	Partial Compliant	Total
a) Unique short-term rentals	3,600	2,400	6,000
b) Annual Revenue per rental – High	$17,000	$17,000	
c) Annual Revenue per rental – Low	$6,000	$6,000	
d) Taxable Income (%) – after deductions	65%	65%	
e) Personal income tax non-reporting rate	10%	40%	
f) PI tax owed – High (((a x b) x d) x e) x 3.55%)	***~$141,000***	***~$377,000***	***~$518,000***
g) PI tax owed – Low (((a x c) x d) x e) x 3.55%)	***~$50,000***	***~$133,000***	***~$183,000***