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SB24-033: The Impact of Changing Tax Classification on Short-Term Rentals

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SB24-033: The Impact of Changing Tax Classification on Short-Term Rentals

PURPOSE OF WHITE PAPER

This white paper has been developed to analyze the potential impacts of Colorado SB24-033, previous known as Bill C and Bill 6, which would reclassify certain short-term rental residential properties as lodging properties for real estate property taxation purposes.

BACKGROUND

For a number of years, Senator Chris Hansen of Denver (Senate District 31) has been advocating for legislation that would change the real property taxation of short-term rentals in Colorado. During the interim period prior to the 2024 legislative session Senator Hansen was successful in advancing a bill through the Legislative Oversight Committee Concerning Tax Policy and Task Force. The bill was approved by the Legislative Council on November 16, 2023 for submission to the Legislature and was introduced at the beginning of the 2024 Legislature as SB24-033.

As currently drafted, this bill would treat short-term rentals (rented for periods of less than 30 days) that are not the owner's primary residence and which were rented for more than 90 days in the prior year as lodging property with respect to property tax years beginning on and after January 1, 2026.

In addition, the bill would value short-term rental property based on the "market" approach, thereby not taking into consideration the "cost" or "income" approaches usually applied to other nonresidential property. The bill also provides a mechanism for county assessors to gather information from short-term rental owners beginning in 2024 to determine whether the property should be taxed as residential property or as lodging property.

Under this bill, lodging properties will be treated as a subclass of nonresidential property for purposes of the valuation for assessment and hence would be taxed at the higher nonresidential property tax rate instead of the lower residential property tax rate.

The bill also provides that it is effective following the 90-day period after the final adjournment of the general assembly, provided, however, that if a referendum petition is filed pursuant to section 1(3) of Article V of the state constitution, it will be effective only after approval by the voters in the November 2024 general election.

The bill does not identify how enactment would change the behavior of short-term rental owners. To help determine what behavorial changes would occur amongst short-term rental owners, the Colorado Lodging and Resort Association (CLARA) recently conducted a survey of short-term rental owners. They received responses from approximately 2,500 short-term rental owners, and a summary of those responses is set forth below.

METHODOLOGY

The attached spreadsheets analyze the economic impact of short-term rentals in the Estes Valley based upon the following data sources:

- The Root Policy Group 2022 study commissioned by the Town Board upon which the Town Board based its ordinance implementing a "Workforce Housing Linkage Fee"
- The Dean Runyan September 2022 study of the Economic Impact of Travel within the Estes Park Local Marketing District commissioned by Visit Estes Park
- The results of the recent Colorado Lodging and Resort Association (CLARA) survey of approximately 2,500 short-term rental owners as to the action such owners will take if this bill is enacted in its current form

From the data in the first two reports, this white paper derives the visitor spending of visitors staying in short-term rentals within the Estes Valley and determines the amount of such spending attributable to short-term rental charges, upon which both lodging tax and sales tax is imposed, and other visitor spending subject only to sales taxes. The attached spreadsheets then calculate the lodging taxes and sales taxes derived by the 860 licensed short-term rentals in the Estes Valley and the average contribution by each short-term rental to such taxes.

The attached spreadsheets then analyze the likely impact of the enactment of the bill on short-term rental owners in the Estes Valley if those owners make the changes consistent with those set forth in the CLARA survey results, to wit:

- 54% of owners would reduce their rentals to 90 days or less
- 32% would cease renting on a short term basis either because they would sell their property, cease all rental or change rental to long-term (>30 days) rental only

The impact of owners reducing their rentals to 90 days or less is determined by the difference between the average rentals shown in the Root Policy Group study and what the taxes those rentals would generate if rented for 90 days per year rather than the current average rental days. The impact of owners ceasing to rent their property on a short-term basis is determined by removing from the data set all of the visitor spending and resulting taxes associated with those short-term rentals. The final sheet then summarizes the likely total impact of these changes on visitor spending and lodging and sales taxes within the Estes Valley.

DISCUSSION

The fiscal note for SB24-033 indicates that the bill would increase tax collections to local taxing districts by an aggregate of $392 million. This fiscal note appears to assume that all existing short-term rentals would be taxed as commercial property rather than residential property for property tax purposes. That estimate likely substantially overstates the impact on local property tax collections for a number of reasons. First, under SB24-033 only STRs which are not principal residences will be affected and only those rented for more than 90 days in the prior year. Perhaps more importantly, that fiscal note does not appear to account for behavioral changes by STR owners as a result of enactment of the bill.

The advocates for this legislation are characterizing the bill as providing equity amongst various types of similar-use properties. In particular, its advocates are stating that the bill will provide equity for hotels as compared to short-term rental residential properties.

Notwithstanding this characterization by the bill proponents, the intended impact of the bill will be to increase local property taxation by taxing certain short-term rentals at a higher tax rate than currently. As a result, the enactment of SB24-033 would serve to increase revenues going to local taxing districts and grow the size of local government. Since the bill would increase taxes, upon filing of a referendum petition, the proposed legislation would be required to go to the voters because of the requirements of TABOR.

The equity argument of the proponents ignores the inequity of the treatment of non-owner- occupied short-term rentals as compared to owner-occupied properties rented for short-term stays and long-term rentals. While the bill would tax non-owner-occupied short-term rentals as nonresidential property, owner-occupied short-term rentals and long term rentals would remain taxed as residential properties.

PROPERTY TYPE	TAX CLASSIFICATION
Principal residence short-term rentals	Residential
Short-term rentals rented for 90 days or less	Residential
Short-term rentals rented for more than 90 days	Nonresidential
Hotels and motels are only rented on a short-term basis	Nonresidential
Long-term rentals	Residential

The categorization of these different types of properties in this manner is based on the alleged "commercial" nature of the use. However, the proponents of the bill cannot distinguish between a short-term rental which is not a principal residence, and a short-term rental which is a principal residence on that basis. Nor can a long-term rental property be distinguished from a short-term rental property on the basis of commercial use since both types of properties generate rental income.

As a result, it appears that the legislation is simply targeted at owners choosing to rent their properties on a short-term basis rather than a long-term basis in a misguided attempt to weed out short-term rentals which are essential visitor capacity for tourist destinations such as the Estes Valley.

LIKELY IMPACTS OF LEGISLATION

The promoters of SB24-033 do not attempt to address the consequences of this legislation. Among such consequences are:

- Increased property tax funding for local governments and the resulting growth of local government due to the reclassification of short-term rental properties as nonresidential property.
- Behavioral changes for owners of short-term rentals that may be characterized as nonresidential property, such as:
    - Some owners will simply limit the number of days rented to 90 days or cease renting their property altogether. This will have the following consequences:
        - Reduction of the available lodging for visitors, particularly in mountain towns which already have limited visitor capacity during certain periods during the year.

This will, in turn, adversely affect tourism for mountain towns and sales and lodging tax collections on which these towns are highly dependent.

- Some owners will instead choose to sell their properties, thus resulting in a flooding of the market and a likely reduction in residential real estate values.
- Creation of inequity in the treatment of short-term rentals taxed as nonresidential property and long-term rentals and principal residence short-term rentals taxed as residential property.
- Valuing these short-term rental properties only using the market approach would establish a lack of parity between the valuation of these short term rentals and hotel properties and other commercial properties, in which the cost and income approach would be predominant.

The legislature should study the economic impacts of the bill on tourism and the real estate market in mountain towns. That impact is likely to be significant and may outweigh any perceived benefits of increased funding for local governments.

FINDINGS

The Colorado Lodging and Resort Association (CLARA) completed its data collection of a survey of short-term rental owners. The survey asked short-term rental owners what changes they would make concerning the rental of their properties if this bill were to be enacted. The survey received approximately 2,500 responses, which are summarized below:

- 54% of owners said they would reduce the number of days they rent their properties to 90 days or less so as to avoid the reclassification.
- 3% already rent their properties for less than 90 days per year and hence would make no changes
- 13% would sell their properties
- 8% would not rent at all
- 11% would no longer rent short-term and would rent for periods of greater than 30 days.

As a result of this survey, it appears than an aggregate of 32% of short term rental owners would avoid the tax reclassification by ceasing renting on a short-term basis and 54% of owners would reduce their annual rentals to 90 days or less. This white paper assumes that the remaining percentage of short-term rental owners would continue renting without change even with the tax classification change.

The CLARA survey allows the data to be analyzed in a granular way to get a better indication of the likely impacts to tourism in the Estes Valley and to state and local tax collections if the bill is enacted. In particular, it permits a reasonable estimate of the loss of tourism revenues and lodging and sales tax collections resulting from both ceasing short-term rentals altogether and from reduction in rentals to 90 days or less.

The loss of tourism revenue associated with short-term rental owners who decide not to rent on a short term basis, either because they convert to long-term rental, sell their properties or simply cease renting altogether is estimated to total approximateliy $32 million per year due to the lost visitor occupancy capacity. This in turn would decrease state and local lodging tax and sales tax collections by approximately $2.9 million. Included in the decreased tax collections is a reduction of over $500,000 of lodging tax devoted to workforce housing mitigation under ballot measure 6E adopted by the voters in 2022.

The loss of tourism revenue associated with short-term rental owners who decide to reduce their rentals to not more than 90 days per year is estimated to total approximateliy $46 million per year due to the lost visitor occupancy capactiy. This in turn would decrease state and local lodging tax and sales tax collections by approximately $2.5 million. Included in the decreased tax collections is a reduction of over $400,000 of lodging tax devoted to workforce housing mitigation under ballot measure 6E adopted by the voters in 2022.

Together lost tourism revenue is estimated to be approximately $78 million per year and lost state and local lodging and sales tax collections Is estimated to total nearly $5.5 million, including a loss of over $900,000 of lodging tax devoted to workforce housing mitigation under ballot measure 6E adopted by the voters in 2022.

Analysis of Tax Impact of Reduction of STR rentals in Estes Valley

	Town	County	Total		
Licensed STRs	493	367	860		
Average days/year rented*	167	167			
Total days rented	82,331	61,289			
Average daily rental*	$ 328	$ 328			
Gross rental income	$ 27,004,568	$ 20,102,792	$ 47,107,360	$ 54,776	Av. / STR rent
				46.86%	% rent/total spend
State sales tax (@ 2.9%)**	$ 783,132	$ 582,981	$ 1,366,113	$ 62,121	Av. other spend
County sales tax (@.8%)**	$ 216,037	$ 160,822	$ 376,859	$ 53,424,302	Total other spend
Town sales tax (@5%)**	$ 1,350,228	$ -	$ 1,350,228		
Lodging tax (@2%)**	$ 540,091	$ 402,056	$ 942,147		
Lodging tax (@3.5%)**	$ 945,160	$ 703,598	$ 1,648,758		
Total lodging taxes generated	$ 3,834,649	$ 1,849,457	$ 5,684,106		

If STRs limited to 90 days/yr rental:

	Town	County	Total
Licensed STRs	493	367	860
Average days/year rented	90	90	
Total days rented	44,370	33,030	
Average daily rental	$ 328	$ 328	
Gross rental income	$ 14,553,360	$ 10,833,840	$ 25,387,200
State sales tax (@ 2.9%)**	$ 422,047	$ 314,181	$ 736,229
County sales tax (@.8%)**	$ 116,427	$ 86,671	$ 203,098
Town sales tax (@5%)**	$ 727,668	$ -	$ 727,668
Lodging tax (@2%)**	$ 291,067	$ 216,677	$ 507,744
Lodging tax (@3.5%)**	$ 509,368	$ 379,184	$ 888,552
Total lodging taxes generated	$ 2,066,577	$ 996,713	$ 3,063,290

Lost tax revenues

	Town	County	Total
State sales tax (@ 2.9%)**	$ 361,085	$ 268,800	$ 629,885
County sales tax (@.8%)**	$ 99,610	$ 74,152	$ 173,761
Town sales tax (@5%)**	$ 622,560	$ -	$ 622,560
Lodging tax (@2%)**	$ 249,024	$ 185,379	$ 434,403
Lodging tax (@3.5%)**	$ 435,792	$ 324,413	$ 760,206
Total foregone lodging taxes	$ 1,768,072	$ 852,744	$ 2,620,815
Lost lodging tax revenues per STR reducing rental to 90 days or less	$ 3,586	$ 2,324	$ 3,047

* Per study relied upon by Town of Estes Park in setting vacation home "linkage fee".

** Per tax rates in effect now.

Analysis of Tax Impact of Reduction of STR rentals in Estes Valley

	Town	County	Total
Reduced rental income if <90 days	$ 12,451,208	$ 9,268,952	$ 21,720,160
Percentage Rent as Total Spending*	47.78%	45.62%	46.86%
Lost STR visitor spending other than rent	$ 13,608,248	$ 11,048,786	$ 24,657,034
State sales tax (@ 2.9%)**	$ 394,639	$ 320,415	$ 715,054
County sales tax (@.8%)**	$ 108,866	$ 88,390	$ 197,256
Town sales tax (@5%)**	$ 680,412	$ 552,439	$ 1,232,852
Sales tax from STR visitor spend excl. rent	$ 1,183,918	$ 961,244	$ 2,145,162
Licensed STRs	493	367	860
Per STR	$ 2,401	$ 2,619	$ 2,494

* Based on Visit Estes Park study of tourism spending of STR visitors.

** Assumes all Town STR visitor spending other than rent is subject to sales tax.

** Assumes all County STR visitor spending other than rent is made in the Town and subject to Town sales tax.

Analysis of Tax Impact of Reduction of STR rentals in Estes Valley

Impact of Reduced Rental:

	Town	County	Total	
Lost sales and lodging tax from rentals:				
State sales tax (@ 2.9%)**	$ 361,085	$ 268,800	$ 629,885	
County sales tax (@.8%)**	$ 99,610	$ 74,152	$ 173,761	
Town sales tax (@5%)**	$ 622,560	$ -	$ 622,560	
Lodging tax (@2%)	$ 249,024	$ 185,379	$ 434,403	
Lodging tax (@3.5%)**	$ 435,792	$ 324,413	$ 760,206	
Total foregone lodging taxes	$ 1,768,072	$ 852,744	$ 2,620,815	
Lost sales tax from other STR visitor spend				
State sales tax (@ 2.9%)*	$ 394,639	$ 320,415	$ 715,054	
County sales tax (@.8%)*	$ 108,866	$ 88,390	$ 197,256	
Town sales tax (@5%)*	$ 680,412	$ 552,439	$ 1,232,852	
Sales tax from STR visitor spend excl. rent	$ 1,183,918	$ 961,244	$ 2,145,162	
Total lost sales and lodging taxes				54% reducing rental
State sales tax (@ 2.9%)**	$ 755,724	$ 589,214	$ 1,344,939	$ 726,267
County sales tax (@.8%)**	$ 208,476	$ 162,542	$ 371,018	$ 200,349
Town sales tax (@5%)**	$ 1,302,973	$ 552,439	$ 1,855,412	$ 1,001,923
Lodging tax (@2%)	$ 249,024	$ 185,379	$ 434,403	$ 234,578
Lodging tax (@3.5%)**	$ 435,792	$ 324,413	$ 760,206	$ 410,511
Total foregone sales & lodging taxes	$ 2,951,989	$ 1,813,988	$ 4,765,977	$ 2,573,628
Licensed STRs	493	367	860	
Per STR	$ 5,988	$ 4,943	$ 5,542	
Lost lodging spend due to reduced rental	$ 12,451,208	$ 9,268,952	$ 21,720,160	
Lost other spend due to reduced rental	$ 13,608,248	$ 11,048,786	$ 24,657,034	
			$ 46,377,194	

Analysis of Tax Impact of Reduction of STR rentals in Estes Valley

Impact of non-rental:

	Town	County	Total	Per STR (860)	
Gross rental income	$ 27,004,568	$ 20,102,792	$ 47,107,360	$ 54,776	
State sales tax (@ 2.9%)	$ 783,132	$ 582,981	$ 1,366,113	$ 1,589	
County sales tax (@.8%)	$ 216,037	$ 160,822	$ 376,859	$ 438	
Town sales tax (@5%)	$ 1,350,228	$ -	$ 1,350,228	$ 1,570	
Lodging tax (@2%)	$ 540,091	$ 402,056	$ 942,147	$ 1,096	
Lodging tax (@3.5%)	$ 945,160	$ 703,598	$ 1,648,758	$ 1,917	
Total lodging taxes generated	$ 3,834,649	$ 1,849,457	$ 5,684,106	$ 6,609	
Percentage rent of total spend	47.78%	45.62%	46.86%		
Spend other than rent	$ 29,513,992	$ 23,962,951	$ 53,424,302	$ 62,121	
State sales tax (@ 2.9%)	$ 855,906	$ 694,926	$ 1,550,831	$ 1,803	
County sales tax (@.8%)	$ 236,112	$ 191,704	$ 427,816	$ 497	
Town sales tax (@5%)	$ 1,475,700	$ -	$ 1,475,700	$ 1,716	
	$ 2,567,717	$ 886,629	$ 3,454,347	$ 4,017	
Total STR spending	$ 56,518,560	$ 44,065,743	$ 100,531,662	$ 116,897	
State sales tax (@ 2.9%)	$ 1,639,038	$ 1,277,907	$ 2,916,945	$ 3,392	$ 933,422
County sales tax (@.8%)	$ 452,148	$ 352,526	$ 804,674	$ 936	$ 257,496
Town sales tax (@5%)	$ 2,825,928	$ -	$ 2,825,928	$ 3,286	$ 904,297
Lodging tax (@2%)	$ 540,091	$ 402,056	$ 942,147	$ 1,096	$ 301,487
Lodging tax (@3.5%)	$ 945,160	$ 703,598	$ 1,648,758	$ 1,917	$ 527,602
Total sales and lodging taxes generated	$ 6,402,366	$ 2,736,086	$ 9,138,452	$ 10,626	$ 2,924,305

Survey behavior change:		Number of STRs	Tax per STR	Lost tax
Will rent <91 days	54%	464.4		
Will sell	13%	111.8	$ 10,626	$ 1,187,999
Will not rent	8%	68.8	$ 10,626	$ 731,076
Will convert to long term rental	11%	94.6	$ 10,626	$ 1,005,230
	32%	275.2		$ 2,924,305
Lost vistior spend due to non-rental		275.2	$ 116,897	$ 32,170,132

Analysis of Tax Impact of Reduction of STR rentals in Estes Valley

	Non-rental	Reduced rental	Total
Reduction in visitor spend:	$ 32,170,132	$ 46,377,194	$ 78,547,326
Reduction in lodging and sales tax:			
State sales tax (@ 2.9%)	$ 933,422	$ 726,267	$ 1,659,689
County sales tax (@.8%)	$ 257,496	$ 200,349	$ 457,845
Town sales tax (@5%)	$ 904,297	$ 1,001,923	$ 1,906,219
Lodging tax (@2%)	$ 301,487	$ 234,578	$ 536,065
Lodging tax (@3.5%)	$ 527,602	$ 410,511	$ 938,113
	$ 2,924,305	$ 2,573,628	$ 5,497,932