CITY COUNCIL COMMUNICATION FORM

FROM: Dan Foote, City Attorney

THROUGH: N/A

DATE: April 13, 2021

ITEM: Fiscal Sustainability -- Taxation of Timeshare/Fractional Ownership Accommodations

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X	DIRECTION
X	INFORMATION
	ORDINANCE
	MOTION
	RESOLUTION
	PROCLAMATION

I. REQUEST/ISSUE & BACKGROUND INFORMATION:

This item is an information and direction item relating to a potential tax on occupancy of property held in timeshare or fractional ownership plans. There three parts to this memo. The first part is an overview of the various types of timeshare/fractional ownership plans and the relationship between these plans and the purchasers of interests in these plans. The second part describes the taxability of timeshare/fractional ownership uses and property under the City's current tax rules. The last part outlines methods by which timeshare/fractional ownership uses could be taxed by the City

STRUCTURE OF TIMESHARE/FRACTIONAL OWNERSHIP

"Fractional ownership" and "timeshare" are terms that are used somewhat interchangeably to describe an arrangement whereby a timeshare/fractional ownership plan purchases or constructs a vacation property and then sells some sort of fractional or divided interest in that property. Other terms used in this industry include "destination club" and "vacation club". For simplicity's sake, these will all be referred to by the term "timeshare".

At its most fundamental level, the purchase of a timeshare interest gives the purchaser the right to use the timeshare plan's property. The purchaser pays some amount of money up front and then also an annual fee usually referred to as a maintenance fee.

Use rights and ownership structures have evolved over time and are quite diverse, even within a single plan or building. Each timeshare plan has unique elements to it. No two plans are identical, but there are some generally accepted categories that can be helpful to distinguish between different plan types.

Fixed Week

In its simplest form, timeshare means the purchaser has the right to use a specified unit for a specified time period. That is, the purchaser occupies the same unit during the same week of every year. This is known as "fixed week" ownership, although the time period does not necessarily have to be a week.

Floating Week

A more flexible type of timeshare is the "floating week". This type of interest gives the purchaser the right to reserve the use of one or more units and to do so without being restricted to a particular week of the year.

Points

The most flexible type of timeshare is known as a "points" system. The purchaser acquires a certain number of points from the plan manager. These points function as a type of currency that can be used to reserve accommodations from the lodging portfolio owned by the plan. Some points systems allow the points to be exchanged for other services.

Ownership vs Membership

The ownership structure of timeshare plans also varies considerably between plans. The simplest type of ownership is a recorded fee simple title interest in a specific unit for a specified period of time. Fee simple title means the ownership of real estate. It is the same type of ownership interest one would have in one's home, except that it is shared with other owners.

More complicated ownership structures might include a recorded fee simple title interest in one or more units without any specified period of occupancy.

Other plan structures convey no ownership interest at all to the purchaser of a timeshare interest. The plan manager retains ownership of the various vacation properties in the plan outright and merely sells a right to use those properties without any ownership interest. Or, the vacation properties might be placed in a trust, and the timeshare purchaser acquires a right to use the trust property and is, in effect, the beneficiary of a trust.

In sum, purchasing a timeshare interest sometimes means that the purchaser becomes the owner of real property, sometimes is beneficiary of a trust, and sometimes is the member of a vacation club with the right to use property but no ownership rights.

Many factors influence the structure of a timeshare plan, including tax considerations for the plan manager, compliance with state laws, securing the interest of the timeshare purchaser in the event of bankruptcy or other default of the timeshare plan, providing flexibility in use, etc.

APPLICATION OF SALES TAX AND PROPERTY TAX TO TIMESHARE PROPERTY AND USES

Sales Tax

Timeshare properties get used in one of three ways. In the first, the timeshare owner or member books their unit through their plan and occupies the unit. This type of transaction is not subject to City sales tax because City sales tax applies to the "purchase price" on the "sale" of goods and certain specified services, which include lodging services.

With an owner/member timeshare use, there is arguably no "sale" in the sense of the timeshare owner/member exchanging money for lodging services. The timeshare owner/member has already acquired the right to those services by purchasing the timeshare interest.

In addition, there is no "purchase price". The timeshare owner/member has paid their annual maintenance fee, but that fee is not the same as the fair market value of the lodging services received. In addition, the maintenance fee must be paid whether or not the timeshare interest is used, so payment of the maintenance fee does not really fit well with the concept of "purchase price".

For these reasons, the City does not attempt to collect sales tax on timeshare use by owner/members.

A second type of timeshare use transaction is an exchange. There are entities called exchange companies, Resort Condominium International ("RCI") and Interval International ("II") being the most prominent, whose business is brokering the exchanges of timeshare interests between owners in different timeshare plans. For example, an owner in the Marriott Vacation Club who wishes to vacation in a unit in the Wyndham program may exchange their Marriott Vacation Club interest for a Wyndham interest through the RCI or II programs.

An exchange like this is, in theory, subject to sales tax because sales tax applies not only to cash transactions but also to barter transactions where no money changes hands. The purchase price for the exchange would be the value of the timeshare interest traded for the timeshare interest that is used.

However, there are a number of practical difficulties in applying City sales tax to timeshare exchange transactions. Because no cash changes hands, it is difficult to establish a purchase price. In addition, City sales tax is paid by the purchaser and collected by the vendor. In an exchange executed by RCI or II, it is unclear who the vendor is. Potentially, the vendor could be RCI and/or II, which are out of state entities, or an out of state timeshare owner. In either case, the City would have difficulty asserting taxing jurisdiction.

The third type of timeshare transaction occurs when a plan manager has excess timeshare inventory that is not needed to satisfy its obligations to its owner/members. In that case, the plan manager may sell that inventory on the open market in a cash transaction. For example, it is possible for a person who is not a member of the Marriott Vacation Club to book lodging at the Steamboat Sheraton for cash. These transactions are clearly subject to sales tax and the local plan managers collect and remit sales and lodging tax on these transactions.

Property Tax

Property owned by a timeshare plan is taxed as residential property. Thus, it is assessed at the same rate as primary residences, secondary residences, and vacation home rental properties. This assessment rate means timeshare property is taxed at fraction of the rate of commercial lodging property such as hotels. The Uniformity Clause of the Colorado Constitution mandates this property tax treatment of timeshare property.

TRANSIENT OCCUPANCY TAX

It appears that timeshare owner/member and exchange uses described above create similar or even identical demands for City services as a cash purchase for lodging services. A person occupying a timeshare unit pursuant to a timeshare interest or exchange is just as likely to benefit from or use City transit, streets, public safety, and parks services as a person occupying one of Steamboat's many vacation home rental properties paid for with cash. The cash transaction generates offsetting revenue to the City via sales and lodging tax while the timeshare transactions do not generate offsetting revenue to the City.

If there is a desire to address this inequity, the recommended approach would be the adoption of a Transient Occupancy Tax or Transient Accommodations Tax ("TOT" or "TAT"). A TOT/TAT taxes the short term occupancy of lodging accommodations. It is different from a sales tax in that the taxable event with a sales tax is a "sale" whereas with a TOT/TAT the taxable event is the "occupancy" on a short term basis of lodging accommodations. This is a critical distinction because a TOT/TAT could apply even to owner occupancies or exchanges where there is no cash payment. The amount of the TOT/TAT could be determined by estimating the fair market value of the lodging accommodations or it could be applied as a flat fee on the basis of the numbers of beds or bedrooms or floor area or some other criteria.

There is some precedent for the application of a TOT/TAT to timeshare owner/member occupancies and to timeshare exchanges. The principal example is the State of Hawaii, which applies such a tax to all timeshare occupancies. The Hawaii tax is applied as a percentage of the annual maintenance fee paid by the timeshare owner/member.

II. SUMMARY AND ALTERNATIVES:

Staff requests direction as to whether Council wishes to continue to consider some form of tax applicable to timeshare transactions. Council may take no action, request further background information, direct staff provide more information on the details of a proposed tax, or prepare for Council review an ordinance referring a timeshare tax to the voters.

III. STAFF RECOMMENDATION:

Staff does not have a recommendation at this time on this informational item.

IV. FISCAL IMPACT:

A timeshare tax would be a revenue measure. It is difficult to estimate the revenue that could be generated from a timeshare tax because the extent of the tax base is unknown. In other words, while staff may be able to identify the majority of local timeshare properties, the proportion of taxed versus untaxed occupancies of these properties is unknown and unlikely to be determinable from public sources of information.

V. LEGAL ISSUES:

As described above.

VI. CONFLICTS OR ENVIRONMENTAL ISSUES:

The imposition of a TOT/TAT on timeshare owner/member transactions and, to a lesser extent, on exchange transactions may generate opposition from the timeshare industry and from timeshare owners. The principal objection would likely be that taxing an owner's use of the owner's property is unfair and inconsistent with the concept of ownership. If this is of concern to Council, the scope of a TOT/TAT could be restricted so as not to apply to owner occupancy of a timeshare unit.

Limiting the scope of a TOT/TAT is possible, but would be complicated due to the diversity of ownership structures in the timeshare industry. Some timeshare plans clearly create ownership interests, some clearly do not, and many are somewhere in the middle. If Council were to go this direction, one option would be to exempt from the TOT/TAT transactions where an owner occupies a unit to which the owner has a recorded fee simple title interest specific to that unit. A second option would be to exempt all owner/member transactions and apply the TOT/TAT only to exchange transactions. A third option would be simply to amend the sales tax code to apply to exchange transactions.

VII. CONSISTENCY WITH COUNCIL GOALS AND POLICIES:

Adoption of a timeshare tax would address the Council's adopted fiscal sustainability goal of diversifying City revenue sources.

ATTACHMENTS:

Attachment #1: Powerpoint