

TAXES TODAY

eNewsletter for
Tax Professionals

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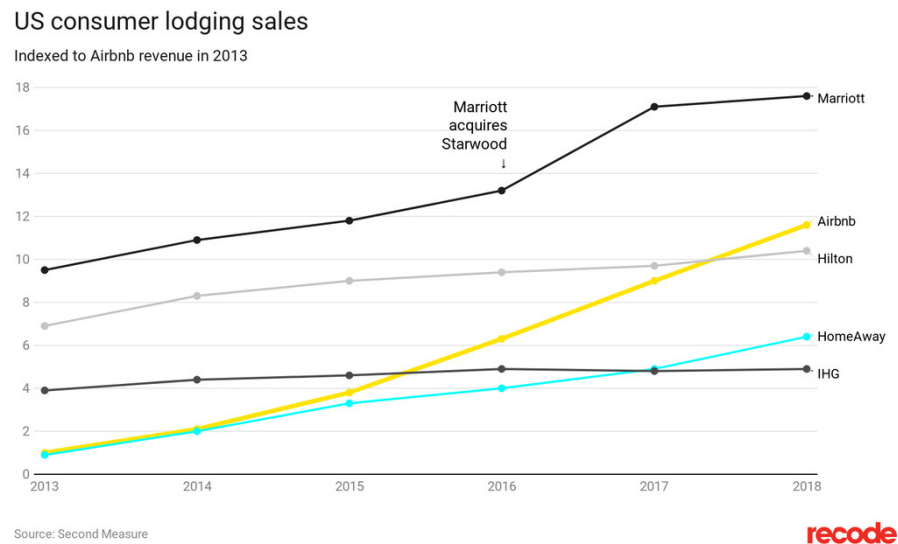
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Airbnb and VRBO: The Tax 411

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It's no secret that online rental platforms, such as [Airbnb](#), [VRBO](#), and [HomeAway](#), have become dominant players in the competitive industry of short-term lodging.

Indeed, the chart below clearly shows the rapid shift of revenue within this industry:



Consistent with this national (in fact, [global trend](#)), we at Towerpoint Wealth have seen a movement among our own clients to rent their properties for shorter-terms. And while a discussion on the merits and risks of the short-term rental approach is central to our conversations with clients, **they often seem most focused on the tax rules and potential tax pitfalls associated with short-term rentals.**

The two most common tax questions our clients ask regarding short-term rental properties are the following:

1. Do I need to report the rental income on my tax return?
2. Are there any other tax considerations I need to be aware of?

As with a "traditional" rental, if the property was not rented for a total of more than 14 days during the calendar year, then the rental income is not taxable (and, accordingly, expenses non-deductible).

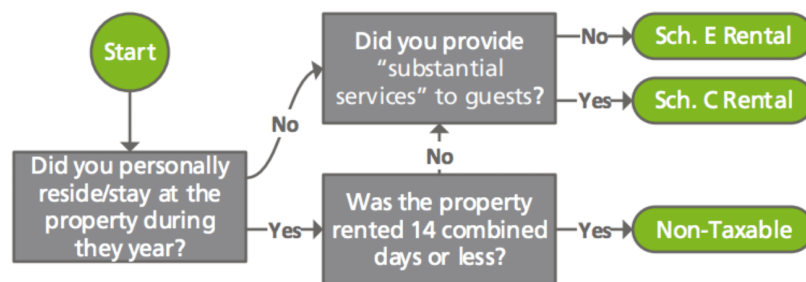
This is known as the ["Masters" exemption](#) and there are clearly ways to take advantage of it. The exemption was fittingly named for local Augusta residents that regularly rent their homes for as much as \$25,000 in tax-free cash over the four-day iconic Masters tournament. Another more local example that comes to mind is

Levi's Stadium hosting the Super Bowl in 2014. [Bay Area property owners rented their apartment, condo, and homes over the Super Bowl weekend for exorbitant prices](#), while enjoying all of this revenue tax-free.

That being said, most of our clients engaged in short-term rentals choose to rent their property for more than 14 days during a year. In this case, the rental income they receive is generally included in taxable income (with expenses at least partially deductible).

Where to Report the Rental Activity

The first step to properly prepare your tax return is to determine where the rental activity should be reported. Short-term rental activities can be classified into three different classes, using the following flowchart:



Schedule E Rentals – Most common classification; occurs when a host does not provide “substantial services” to their guests. This income is not subject to self-employment tax.

Schedule C Rentals – A rental will typically fall into this category when “substantial services” are provided to guests, though there are other rare cases where this can occur. This income is subject to the self-employment tax.

Source: <https://www.passiveairbnb.com/airbnb-taxes-schedule-c-schedule-e/>

The chart above provides a "traditional" perspective on rental property income but there are several important considerations for shorter-term rentals, such as those typically made using Airbnb and VRBO.

The first important determination, and one that is continually a matter of debate, is whether the income is reported on a property owner's federal tax return as income on [Schedule C](#) or [Schedule E](#).

When the average rental period is less than seven days, as is common for many short-term rentals, the IRS deems the activity to not be a "true" rental activity and because of this, **many experts agree that the income is required to be reported on Schedule C.**

Further, if the short-term rental property provides "hotel-like" (substantial) services, such as cleaning the room and changing the sheets each day of guest occupancy, providing meals, having a concierge service, etc., **the IRS may classify the short-term rental as a business, subjecting the property owner to self-employment tax as well.**

The reality is that the majority of short-term rental properties do not provide "hotel-like" services as most common short-term rental accommodations (known as insubstantial services) such as, running water, heating and air conditioning, and Wi-Fi, are outside the classification of "hotel-like." **For short-term rentals in this category, rental income is generally still reported on Schedule C but is not subject to self-employment tax.** *Note: There are differing viewpoints on this, with many tax professionals opting to include any short-term rental income not subject to self-employment tax on Schedule E.*

There is industry agreement that rental income is reported on Schedule E if:

- the average rental period falls between seven and thirty days and "hotel-like services are not provided to guests OR
- the average rental is above thirty days.

The takeaway is that as most short-rental properties are rented for less the seven days, individuals need to be careful to not provide "hotel-like" services as doing so will subject them to the self-employment tax.



Shifting our attention to the second most common short-term rental question our clients ask, there are indeed many other tax considerations to be aware of.

The one that has caused the most confusion is related to the [occupancy tax](#) (also commonly known as the hotel tax, lodging tax, or tourist tax). The occupancy tax is an additional tax levied on a visitor's stay in a short-term rental property or a hotel.

Until recently, property owners, while legally responsible for paying the occupancy taxes associated with guest bookings, were not consistently and accurately tax compliant for two reasons:

- There was confusion regarding if it was, in fact, the property owner's responsibility to collect and remit these taxes, or the short-term rental platforms'.
- Occupancy taxes, while levied at the state level, are also often levied at the city and county level. This requires the property owner to know and calculate the state and city or county occupancy tax rate for each booking, to then collect these taxes from the guest, and finally, in a timely manner, remit these taxes to each one's tax authority consistent with the specific filing requirements. Clearly, this process is fraught with potential missteps.

Recently, cities and counties have taken notice of a broad lack of compliance with occupancy taxes and are "ramping up" enforcement. In response to this, and also to get ahead of state legislation that will make it mandatory for short-term rental platforms to collect and remit all (state, city, and county) occupancy taxes, some short-term rental platforms, such as Airbnb and VBRO, have begun collecting and remitting taxes on behalf of property owners.

We expect other short-term rental platforms to follow suit.

We are here to help.

As always, please feel free to reach out and call (916-405-9166) or email (spitchford@towerpointwealth.com) with any questions, thoughts, or needs you may have. At Towerpoint Wealth, we are happy to be a direct and no-strings-attached resource for you.



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