

OFFICE OF THE CITY AUDITOR
PERFORMANCE AUDIT
November 2022

Kansas City Misses Out on Millions in Tax Revenue from Short Term Rentals



**KANSAS CITY
MISSOURI**

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Honorable Mayor and Members of the City Council:

This audit focuses on the impact short term rental activity has on the city's convention and tourism taxes and fees. A [companion audit](#) focuses on short term rental permit compliance. We originally planned to issue a single report addressing both issues. However, we decided to issue separate reports to ensure the Mayor and City Council receives information about the impact of short term rentals on the city's convention and tourism tax as they consider the city's legislative priorities for the 2023 session of the Missouri General Assembly.

Short term rental units represent an estimated 7% to 11% of the city's overall hotel room supply – the equivalent of two downtown convention hotels. Missouri state statutes currently prevent Kansas City, but not other Missouri cities, from assessing and collecting a Convention and Tourism (C&T) tax on short term rentals. State statute defines a hotel and motel in Kansas City in a way that excludes short term rentals from this tax. Had the C&T tax been assessed and collected on short term rentals in Kansas City from July 2021-August 2022, we estimate the city would have raised about \$2.28 million.

The Hotel, Motel Occupancy Fee section of city code defines a hotel and motel the same as the C&T tax. The city's own definition of hotels and motels prevents the city from assessing and collecting this \$1.50 per occupied night fee on short term rentals. Had the occupancy fee been assessed and collected on short term rentals during the same period, we estimate the city would have raised more than \$350,000.

The city has different options to change the tax and fee. The city's ability to assess and collect the C&T tax on short term rentals is dependent upon the state legislature changing state law to be consistent with other Missouri cities currently collecting the tax. After the change in state law, the City Council could then propose a citywide vote to change the definition of a hotel and motel in the C&T section of city code. This change in city code would make the tax apply uniformly to all those in the accommodation industry. Such a change would also have a positive impact on the city's ability to fund tourism and convention activities that are currently being supplemented by the city's general fund.

In contrast, the City Council, with voter approval, could establish an occupancy fee for short term rentals directly without action by the state legislature. This is because the state statute enabling the city's general power to establish fees does not prescribe how a hotel or motel must be defined.

We make recommendations to the Mayor and City Council to continue including changes to the Convention and Tourism Tax as a legislative priority and taking steps to assess a Hotel, Motel Occupancy Fee on short term rentals.

We would like to thank management and staff in the City Planning and Development and Law departments for their assistance and cooperation during this audit. The audit team for this project was Terry Bray, Jonathan Lecuyer, and Suzanne Polys. This audit was based in part on public audit suggestions.

A handwritten signature in blue ink that reads "Douglas Jones". The signature is fluid and cursive, with the first name "Douglas" and last name "Jones" clearly legible.

Douglas Jones, CGAP, CIA, CRMA
City Auditor

Kansas City Misses Out on Millions in Tax Revenue from Short Term Rentals

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Introduction

Audit Objective

Do short term rentals impact city convention and tourism taxes and hotel, motel occupancy fees?

To answer our objective, we compared other Missouri cities' enabling tax statutes to Kansas City's tax statute, and estimated the impacts on potential tax revenues.

We conducted this audit in accordance with Government Auditing Standards with the exception of reporting the views of responsible officials as the recommendations are addressed to the City Council as a body.

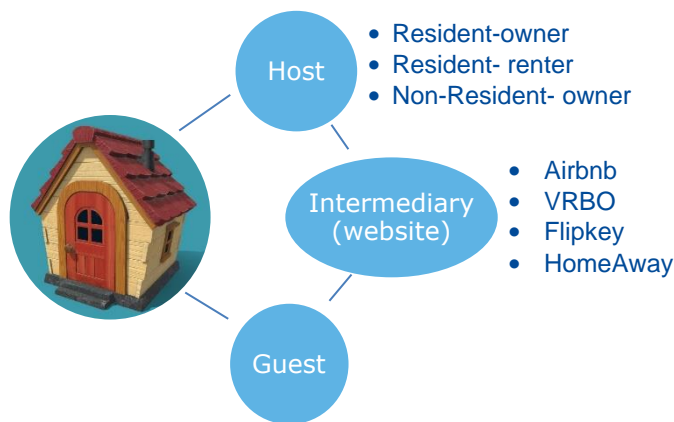
See Appendix A for more information about the audit objective, scope, methodology, and compliance with standards.

Background

Short Term Rental Regulations

A short term rental is when a person or business ("host") provides a ("property" or "unit") house, apartment, or other non-traditional hotel residence for rent as overnight lodging for less than 30-days. A host may be an owner, renter, or investor that does not occupy the property.

Exhibit 1: Short Term Rental Parties Identified by City Code



The host typically lists the unit on an intermediary website. Common third-party websites include companies like Airbnb, VRBO, Flipkey, and HomeAway. Short term rentals grew in popularity throughout the U.S. during the 2010's.

The city council passed an ordinance to regulate the operation of short term rentals in early 2018.¹ The ordinance identifies the parties governed by city code (see Exhibit 1.) and requirements to obtain a permit, and outlines health and safety occupancy requirements.

¹ [Ordinance 170771](#), April 12, 2018.

Kansas City Misses Out on Millions in Tax Revenue from Short Term Rentals

Findings and Recommendations

City Cannot Collect Millions in Taxes and Fees from Short Term Rentals

Estimated Lost Revenues

(Jul 2021 – Aug 2022)

\$2.28 million

Convention and Tourism Tax

\$353,600

Hotel, Motel Occupancy Fee

The city is unable to collect the convention and tourism tax² (C&T tax) and the hotel and motel occupancy fee³ from short term rental activity. The inability to collect these revenues impacts programs and facilities like Visit KC, the Neighborhood Tourism and Development Fund, the convention center, and the T-Mobile Center. The city can establish fees like the hotel and motel occupancy fee locally, however changing the convention and tourism tax requires action from the state legislature.

Convention and Tourism Tax on Short Term Rentals Would Generate Millions

State law prevents the city from collecting the C&T tax from short term rentals that is paid by most hotel/motel businesses in the city.⁴ Missouri state statute defines a hotel under the Kansas City's C&T tax as a building "having more than 8 bedrooms for the accommodation of such guests".⁵ City code related to the C&T tax mirrors the definition from the state statute as required.⁶ The city's short term rental code limits units to no more than 2 people per bedroom, not to exceed 8 guests per dwelling unit.⁷ This effectively limits short term rental units to 4 bedrooms, which means the C&T tax definition of a hotel does not apply to short term rentals in Kansas City.

The city would have collected an estimated \$2.28 million dollars from July 2021-August 2022 had the C&T tax applied to short term rentals. State statute requires the city to distribute the C&T tax among Visit KC (40%), the Neighborhood Tourism and Development Fund (10%), and the city's convention and entertainment centers (50%). Exhibit 2 shows how the C&T tax would have been allocated if it had been collected from short term rentals.

² Code of Ordinances, Kansas City, Missouri, [Sec. 68-551](#). Assesses a 7.5% tax on the amount of sales or charges for all sleeping rooms paid by guests of hotels/motels/tourist courts.

³ Code of Ordinances, Kansas City, Missouri, [Sec. 40-111](#). Assesses a \$1.50 fee per occupied room by a guest per day on all hotels/motels/tourist courts in the city.

⁴ Note, this is not the general citywide sales tax applied to sales transactions.

⁵ [RSMo §92.325](#) (1994).

⁶ Code of Ordinances, Kansas City, Missouri, [Sec. 68-551](#).

⁷ Code of Ordinance, Kansas City, Missouri, [Sec. 88-321-02A\(6\)](#) and [88-321-03A\(7\)](#).

Exhibit 2: Estimated C&T Tax Revenue Distributed by Use if C&T Tax Applied to Short Term Rentals

Required Use	Potential Revenue
Visit KC	\$910,876
Neighborhood Tourism & Development Fund	\$227,719
Convention Facilities	\$1,138,595
Total	\$2,277,190

Sources: City Auditor’s Office calculations and Host Compliance data July 2021- August 2022.

Other Missouri Cities Collect Convention and Tourism Taxes from Short Term Rentals

Other Missouri cities collect convention and tourism type taxes from short term rental transactions. State statute defines Convention and Tourism taxes for cities in different sections. State statute defines hotels in Kansas City’s C&T tax section differently than other Missouri cities that collect similar taxes from short term rentals. (See Exhibit 3.)

Exhibit 3: State Statute Definition of Hotels by Missouri Cities

City	RSMo	>8 Room Definition	Tax applied to STR
St. Louis-Convention and Tourism Tax	67.619	No	Yes
St. Louis-Convention and Sports Tax	67.657	No	Yes
St. Charles	67.1158	No	Yes
Independence	67.1366	No	Yes
Kansas City	92.327	Yes	No

Sources: Revised Missouri State Statutes and City Auditor analysis.

Changing the city’s convention and tourism tax rules would require several steps.⁸

1. The state would need to change the definition of hotel in the taxes’ enabling statute. This requires lobbying state representatives to act on the city’s behalf.
2. The council would need to move for a citywide vote to adopt the new definition of the tax locally.

From 2019-2020, the City Council included changing the state statute definition of a hotel for Kansas City as a ‘major’ legislative priority.^{9,10} The city changed the issue to a ‘position’ in the 2021

⁸ Staff communicated these steps to address the C&T tax issue in their report at the time the city adopted short term rental regulations in 2018.

⁹ Committee Substitute Resolution 180389, December 13, 2018; Second Committee Substitute Resolution 190968, December 12, 2019.

¹⁰ Each year the City Council passes legislative priorities for their lobbyist to use to help provide the Missouri State Legislature information on the major priorities and positions of state laws that may be under consideration.

and 2022 legislative priorities.¹¹ The city’s lobbyist told us that a bill related to this topic was filed in the Missouri legislature in the 2020 session. To date, no change has occurred.

Available short term rental units represent a significant portion of the city’s overall hotel room supply – between 7-11% of the total. The estimated over 1,800 short term rental units in August 2022 are the equivalent of two downtown convention hotels. Nearly all the remaining portion of the city’s hotel room supply pay the city’s C&T tax.

Changing Kansas City’s definition of a hotel to be consistent with other Missouri cities would have a positive impact on the city’s ability to fund tourism and convention type activities that are currently being supplemented by the city’s general fund.

Recommendation

To improve the city’s ability to promote tourism and convention activities and create tax parity between hotels, motels, and short term rentals, the City Council should continue their legislative priority to change the state statute that limits Kansas City’s ability to tax short term rentals like other businesses in the accommodation industry.

Hotel, Motel Occupancy Fees Not Applied to Short Term Rentals

City code does not require short term rental units to pay the occupancy fee paid by most of the hotel and motel industry in Kansas City. The hotel, motel occupancy fee requires businesses accommodating guests to pay a \$1.50 fee per occupied room night. City code for the occupancy fee defines a hotel or motel the same as the C&T tax section. The occupancy must occur in a building “having more than 8 bedrooms for the accommodation of such guests” to be considered a hotel.¹² As a result of this city code definition, the city cannot apply this fee to short term rentals.

The city would have collected an estimated \$353,638 from July 2021-August 2022, had the hotel, motel occupancy fee applied to short term rentals.

Short term rental room nights are a significant part of the city’s overall accommodation industry. Their 235,759 occupied room nights from July 2021-August 2022, represents an estimated 8%-12% of all room nights annually in Kansas City depending on the year. By comparison, VisitKC reports that meeting and convention

¹¹ Committee Substitute Resolution 200780, December 10, 2020; Committee Substitute for Resolution 210949, December 2, 2021.

¹² Code of Ordinances, Kansas City, Mo, [Sec 40-111](#).

activity generated about 364,750 occupied room nights in 2019¹³, only a slightly higher portion of total city occupied room nights.

Local Vote Can Change City Fees

The city does not need state legislative action to create or change a hotel, motel occupancy fee in city code. State statute authorizes the city to establish a fee on short term rentals and there are no restrictive definitions.

Unlike the convention and tourism tax, the section of state statute enabling a city hotel, motel occupancy fee does not define a hotel. State statute allows cities to “adopt regulations and rules relating to any matters pertaining to the administration and enforcement of any ordinances”.¹⁴

The dedicated use of the current hotel, motel occupancy fee may impact how the city approaches an occupancy fee for short term rentals. The city established the existing hotel, motel fee “for the purpose of providing funds for the acquisition, development, construction, operation, and maintenance of a downtown arena... ..The city is authorized to impose the license fee on hotels, motels and tourist courts... until all project financing for the Downtown Arena is fully paid.”¹⁵ To not call into question revenue sources for existing debt, the city likely would need to create a separate occupancy fee for short term rentals.

A fee of this type would likely require a citywide public vote under the Hancock Amendment. The City Council could propose to voters a new fee related to short term rentals. A successful election could add a new section of city code directed only at short term rentals that sets the fee and its use.

Recommendation

To optimize city revenues and create tax parity, the City Council should take steps to assess an occupancy fee on short term rentals similar to the hotel, motel occupancy fee already paid by most of the accommodation industry under the Code of Ordinances Sec. 40-111.

¹³ 2019 is the last year hotel room nights were not affected by the pandemic.

¹⁴ RSMo § 92.045 (1994).

¹⁵ Ordinance 040554, May 20, 2004.

Recommendations

1. The City Council should continue their legislative priority to change the state statute that limits Kansas City's ability to tax short term rentals like other businesses in the accommodation industry.
2. The City Council should take steps to assess an occupancy fee on short term rentals similar to the hotel, motel occupancy fee already paid by most of the accommodation industry under the Code of Ordinances Sec. 40-111.

Appendix A: Objective, Scope and Methodology, and Compliance Statement

We conducted this performance audit of short term rental regulations, taxes, and fees under the authority of Article II, Section 216 of the Charter of Kansas City, Missouri, which establishes the Office of the City Auditor and outlines the city auditor's primary duties.

A performance audit provides "objective analysis, findings, and conclusions to assist management and those charged with governance and oversight, with among other things, improving program performance and operations, reducing costs, facilitating decision making by parties with responsibility for overseeing or initiating corrective action, and contributing to public accountability."¹⁶

Why We Did This Audit

The widespread use of short term rentals may impact the city's ability to collect convention and tourism taxes and hotel, motel, or tourist court fee assessed in Kansas City. These taxes and fees are used for convention center operations, a range of tourism activities, and to retire arena debt. Evaluating these impacts can help the city strategize what steps to take in response to the proliferation of short term rentals.

Audit Objective

This report is designed to answer the following question:

- Do short term rentals impact city convention and tourism taxes and hotel, motel occupancy fees.

Scope and Methodology

Our audit methods for short term rental tax and fee impacts included:

- Reviewing city ordinances to identify taxes and fees applicable to short term rentals.
- Reviewing city code and state statute to determine limitations on the city's ability to change certain taxes and fees that may apply to short term rentals.
- Interviewing city staff to identify limitations on city taxes and impacts.

¹⁶ Comptroller General of the United States, [Government Auditing Standards](#) (Washington, DC: U.S. Government Printing Office, 2018), pp. 10, 11.

- Comparing Missouri state statutes enabling various cities to levy convention and tourism type taxes to determine differences in applicability to short term rentals.
- Reviewing city budgets to identify fund balances and trends impacted by the convention and tourism tax and hotel, motel occupancy fee.
- Obtaining a special report from Host Compliance estimating short term rental booking values and room nights in Kansas City to identify potential impact on taxes and fees.
- Subpoenaing and receiving from two intermediaries' data on short term rental activity in Kansas City to compare to Host Compliance estimates.

Statement of Compliance with Government Auditing Standards

We conducted this performance audit in accordance with generally accepted government auditing standards with the exception of reporting the views of responsible officials as the recommendations are addressed to the City Council as a body. We do not believe the absence of a response affects the audit results.

Government auditing standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. No information was omitted from this report because it was deemed confidential or sensitive.

Scope of Work on Internal Controls

We did not assess internal controls as part of this audit as they were not relevant to the audit objective.

Data Reliability

We used an estimate from Host Compliance¹⁷ for the total value of sales activity and room nights for short term rental activity from July 2021- August 2022. We requested a special report on behalf of the city to obtain this information from Host Compliance. We assessed the reasonableness of Host Compliance's estimate by comparing it to information provided to us by short term rental intermediaries. We also verified the independence and qualifications of Host Compliance to provide their estimate. We determined the estimate was sufficiently reliable for our audit work.

¹⁷ Host Compliance is a web platform used by the City Planning and Development Department. They provide the department with services to identify short term rental listings and other related data.