LRBb0656

1999 DRAFTING REQUEST

Assembly Amendment (AA-AB133)

Received: **06/11/99**

Received By: **dykmapj**

Wanted: **Soon**

Identical to LRB:

For: **Legislative Fiscal Bureau 6-3847**

By/Representing: **Russell**

This file may be shown to any legislator: **NO**

Drafter: **dykmapj**

May Contact:

Alt. Drafters:

Subject: **Tax - real estate transfer fee**
Tax - sales
Tax - miscellaneous

Extra Copies: **JK**

Pre Topic:

LFB:......Russell -

Topic:

Timeshares

Instructions:

See Attached Paper 123 alternative 4 (current law)

Drafting History:

Vers.	Drafted	Reviewed	Typed	Proofed	Submitted	Jacketed	Required
/?	dykmapj 06/11/99	gilfokm 06/11/99		_______ _______			
/1			martykr 06/11/99	_______ _______	lrb_docadmin 06/11/99		

FE Sent For:

<END>

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FE Sent For:

<END>

Legislative Fiscal Bureau
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June 7, 1999 | Joint Committee on Finance | Paper #123

Real Estate Transfer Fee and Sales Tax on Time-Share Properties (General Fund Taxes -- Other General Fund Taxes)

[LFB 1999-01 Budget Summary: Page 47, #3]

CURRENT LAW

Time-Share Property. Section 707.0 (32) of Wisconsin statutes defines "time-share property" as one or more time-share units subject to the same time-share instrument, together with any real estate or rights to real estate appurtenant to those units. In addition, to qualify as "time-share property" under this definition, an owner's interest in the property must provide the right to use or occupy a unit during at least four separate periods over at least four years.

Real Estate Transfer Fee. Sales of real estate are subject to a real estate transfer fee, which is set at $3 per $1,000 of value. A real estate transfer return is filed and the fee is collected at the county level by the register of deeds when the deed or other instrument of conveyance is submitted for recording. Proceeds from the real estate transfer fee are divided between the state and the county in which the fee is collected, with the state receiving 80% and the county retaining 20%.

Current statutes on the real estate transfer fee do not specifically refer to time-share property. However, the Department of Revenue (DOR) has interpreted the law as subjecting "fixed-time" time-share sales, in which the use of the rooms or lodging is fixed at the time of sale as to the starting day and lodging unit, to the real estate transfer fee. "Flex-time" time-share sales, described below, are not subject to the real estate transfer fee.

Sales Tax. Under current law, the furnishing of short-term lodging for continuous periods of less than 30 days is one of eleven service categories subject to the 5% general sales tax. The statutes specify that the sales tax applies to the furnishing of rooms or lodging through the sale of time-share property as defined in s. 707.02(32) (described above) if the use of the rooms or lodging is for continuous periods of less than one month and if the use of the rooms or lodging is not fixed at the time of the sale as to the starting date or lodging unit. Such time-share properties are frequently referred to as "flex-time" time-shares. Annual maintenance charges associated with flex-time time-shares, which include a share of property taxes, are subject to the sales tax as well.

GOVERNOR

Modify the treatment of conveyances of time-share properties with respect to the real estate transfer fee and the sales tax as follows:

a. Exempt from the real estate transfer fee and the requirement to file a real estate transfer return transfers of time-share property as defined in section 707.02(32) of the statutes.

b. Subject all sales of time-share property for continuous periods of less than one month to the sales tax. Specify that charges associated with taxable time-share property would be taxable at the time the charges are incurred, even if those charges were not taxable at the time of the initial sale of the time-share property.

c. Amend additional statutes to make them consistent with the exemption of time-share property from the real estate transfer fee. Currently, transfers of time-share property as defined in s. 707.02 (32) are subject to certain reporting requirements related to disclosure by owners of residential real estate. In addition, such time-share property is subject to a requirement that the small claims procedure be the exclusive procedure used in circuit court in actions relating to the return of earnest money tendered pursuant to a contract for purchase of property. However, in both cases the statutes specify that transfers that are exempt from the real estate transfer fee are also exempt from such requirements. The bill would specify that these requirements would no longer apply to transfers of time-share property as defined under s. 707.02 (32). However, transfers of time-share property that do not meet the definition under s. 707.02 (32) would continue to be subject to the requirements on disclosure and on the specified use of the small claims procedure.

DISCUSSION POINTS

1. Time-share ownership denotes exclusive use of accommodations for a particular number of days within a specified time period, either in perpetuity or for a predetermined number of years. Typically, the interval of use is one or two weeks per year.

2. Under current law, as described above, sales of time-share properties are subject to either the 0.3% real estate transfer fee or the 5.0% sales tax, depending on how the sale is classified. It the deed of sale specifies the starting date of occupancy and the specific lodging unit purchased, then the sale is considered a transfer of real estate and is subject to the real estate transfer fee. If either is not fixed at the time of sale, then the sales tax on short-term lodging applies.

3. While sales of fixed-time time-shares are currently regarded as interests in real estate, it could be argued that these short periods of occupancy resemble occupancy in hotel and

motel lodging and should, instead, be subject to the sales tax.

4. A survey done by DOR of 12 time-share resorts in Wisconsin in 1997 revealed that 36.4% of time-share units were available on a fixed-time basis and 63.6% were available on a flex-time basis. However, the Department reported that most resorts sold time-share properties on a fixed-time basis and executed separate legal agreements that provide flexibility in use similar to that enjoyed with flex-time time-shares. Such an arrangement allows the purchaser to buy the time-share as a fixed-time unit and pay the much lower real estate transfer fee, rather than the sales tax. The separate legal agreement states that the purchaser may use different facilities at a different time than specified in the deed.

5. Another way to gain increased flexibility is to participate in an exchange service. Many time-share resorts are affiliated with an exchange company that administers exchange services for its members. Time-share owners may elect to become members of the affiliated exchange company, which charges an annual membership fee as well as an exchange fee for specific exchanges. To exchange, members place their intervals into the exchange company's pool of resorts and weeks available for exchange and choose an available time and resort from the pool.

6. It can be argued that the flexibility afforded through such mechanisms makes time-share ownership more comparable to arranging temporary hotel or motel lodging than to owning real property.

7. Under current law, the sales tax treatment of annual fees depends upon the treatment of the original sale and the purpose of the fee. If the original sale is treated as a transfer of real estate, then any annual fee is subject to sales tax if it is for recreation purposes, but not if it is for maintenance and taxes. If the original sale is considered taxable lodging, then the entire annual fee is taxable.

8. The Governor's proposal would provide consistency in the tax treatment of sales of time-share property and annual fees by: (a) subjecting all sales of time-shares for use for continuous periods of less than 30 days to the sales tax; (b) subjecting all fees associated with such time-shares to the sales tax; and (c) eliminating the real estate transfer fee currently imposed on sales of fixed-time time-shares. The sales tax would first apply to purchase prices of sales of fixed-time time-shares made on the first day of the second month after publication. However, the sales tax would also be imposed on the annual maintenance fees for fixed-time contracts currently in existence.

9. Under the bill, time-share property that would be sold for 30 days or longer would not be subject to either the sales tax or the real estate transfer fee. Such sales are currently subject to the real estate transfer fee. Although transactions for this length of time are apparently infrequent, the Committee may wish to modify the Governor's proposal to impose the transfer fee on sales of such time-shares.

10. The administration has estimated that the change in the tax treatment of fixed-time time-shares and associated maintenance fees would lead to a net increase in general fund tax

collections of $1,200,000 in 1999-00 and $1,440,000 in 2000-01. The estimate for the first year assumes an effective date of September 1, 1999. However, assuming that the bill would be published in August, 1999, the effective date of the provisions would be October 1, 1999. Based on the October 1, 1999, effective date, it is estimated that increased general fund taxes in the first year would be $1,080,000, a reduction of $120,000 from the amount used in the bill. It should be noted that these estimates represent the net effect on the general fund, consisting of a gain in sales tax collections and a loss in real estate transfer fees.

11. The Governor's recommendation would affect county taxes as well, both through the county sales tax and the share of real estate transfer fees retained by counties. It is estimated that counties would experience a net gain from the bill of $100,000 in the first year and $135,000 in the second year.

12. According to tax officials in Wisconsin's neighboring states, Illinois, Iowa, Michigan and Minnesota tax sales of time-share property as follows:

Illinois. Illinois, which has only a small number of time-share properties within its borders, imposes a real estate transfer fee on sales of such properties and does not tax annual maintenance fees.

Iowa. Iowa, which has only one time-share resort, imposed the sales tax on both fixed- and flex-time time-shares. There is no tax on annual maintenance fees.

Michigan. In the state of Michigan, sales of time-shares are subjected to a real estate transfer fee, as are all sales of deeded property. There are no taxes imposed on annual maintenance fees.

Minnesota. Minnesota reports that there is neither a sales tax nor a real estate transfer fee imposed on sales of time-share properties. There are no taxes imposed on annual maintenance fees.

13. Among other states contacted, most states impose the real estate transfer fee on the sale of both types of time-share properties and do not impose a tax on maintenance fees. In the state of Washington, however, a real estate transfer fee is imposed on the portion of a sale that is real property and the sales tax applies to the portion of the sale that is personal property. No distinction is made between the types of time-shares and there are no taxes imposed on annual maintenance fees.

14. Opponents of Governor's recommendations argue that there is an ownership interest in time-shares that distinguishes them from transient hotel or motel use, as evidenced by the following:

- Wisconsin statutes specify that a time-share property constitutes a real property interest.

- Time-shares are conveyed by warranty deed under the supervision of a licensed real estate broker.

- Owners are responsible for a portion of real estate taxes on their time-share properties and are eligible for a second home tax exemption under federal tax laws.

For these reasons, opponents of the Governor's proposal argue that the sale of time-shares should be taxed as a transfer of real estate rather than as a sale of personal property.

15. It should be noted that a similar argument was put forth by a condominium resort in a case before the Wisconsin Court of Appeals, Telemark Development Inc. v. Department of Revenue, April 30, 1998, (Telemark). However, the court ruled that the sales tax on short-term lodging could be imposed, even though time-share interests take on aspects of real property in some chapters of the statutes.

16. Opponents of the bill suggest that the tax treatment of time-share properties should parallel that of condominiums, which would mean that sales of time-shares would be subject to the real estate transfer fee and that there would be no sales tax on annual maintenance fees. It is argued that imposing the sales tax on annual maintenance fees amounts to a tax on tax because the fees are used to pay real estate taxes and other maintenance costs that could include materials already taxed.

However, if these purchases are likened to staying at a hotel, then there is no difference in tax treatment. Entire charges for stays at hotels are taxed, including the portion of the charges that are paid by the hotel for property taxes and maintenance.

17. In addition to the opposition to the sales tax on time-share maintenance fees in general, opponents of the bill specifically object to the provision that would tax such fees on fixed-time contracts currently in existence.

18. Opponents of these provisions also argue that imposing a sales tax on time-share sales violates the uniformity and the equal protection clauses of the state constitution.

However, the court determined in Telemark that applying the sales tax to sales of flex-time time-shares does not violate the uniformity clause of the constitution. It is likely that the same interpretation would apply with respect to the proposed imposition of the sales tax on sales of fixed-time time-shares.

The court further determined that taxation of flex-time time-share sales under the sales tax and fixed-time time-share sales under the real estate transfer fee had not been shown to result in discrimination under the equal protection clause of the constitution. Under the bill, fixed-time time-share and flex-time time-share sales would be treated the same. Presumably, if the different treatment of the two types of time-shares under current law does not violate the equal protection clause, neither would the consistent treatment of time-shares under the bill.

19. It has been suggested that prospective time-share buyers might choose to buy time-

share weeks in states other than Wisconsin in order to avoid paying a sales tax on the annual maintenance fees.

20. Finally, opponents of the bill argue that imposition of the sales tax on time-shares would hurt the average person. According to the American Resort Development Association, 23% of time-share owners have annual incomes under $50,000, 32% have incomes between $50,000 and $75,000, and 45% have annual incomes that exceed $75,000.

21. The Senate Committee on Insurance, Tourism, Transportation and Corrections has formally adopted a motion to delete the Governor's proposal and, instead, impose the real estate transfer fee on the sale of both types of time-shares. Under this proposal, the sales tax would no longer be imposed on flex-time time-shares or on annual maintenance fees. While real estate transfer fees would increase, sales tax collections would decrease and there would be a net negative effect on general fund tax collections as well as on county tax revenues.

ALTERNATIVES

1. Approve the Governor's proposal to (a) exempt from the real estate transfer fee and the requirement to file a real estate transfer return transfers of time-share property as defined in section 707.02(32) of the statutes; (b) subject all sales of time-share property for continuous periods of less than one month to the sales tax; and (c) specify that charges associated with taxable time-share property would be taxable at the time the charges are incurred, even if those charges were not taxable at the time of the initial sale of the time-share property.

However, modify the fiscal effect to reflect an effective date of October 1, 1999, and estimate increased general fund tax collections under the proposal of $1,080,000 in 1999-00 and $1,440,000 in 2000-01. The revised first year estimate is $120,000 smaller than the administration's estimate.

Alternative 1	GPR
1999-01 REVENUE (Change to Bill)	- $120,000

2. Approve the Governor's proposal as modified. In addition, specify that the sales tax on sales of time-share property and on maintenance fees would also apply to time-share properties sold for use for intervals of 30 continuous days or longer. It is anticipated that the fiscal impact of this provision would be minimal. Therefore, estimate the fiscal effect to be the same as the Governor's proposal as modified above.

Alternative 2	GPR
1999-01 REVENUE (Change to Bill)	- $120,000

3. Delete the Governor's recommendation. Instead, exempt the sale of flex-time time-shares from the sales tax and specify that the real estate transfer fee would apply to all sales of time-share property, including those properties used for intervals of 30 continuous days or longer. Eliminate the sales tax on maintenance fees of all time-share properties, even if such fees were taxable at the time of the initial sale of the time-share property.

Estimate the fiscal effect to be a net reduction of general fund tax collections of $70,000 in the first year and $90,000 in the second year. Compared to the estimates in the bill, which projected increased general fund collections, this alternative would reduce general fund tax collections by $1,270,000 in the first year and $1,530,000 in the second year.

It is anticipated that this alternative would reduce county tax collections by $9,700 for the biennium, assuming an effective date of October 1, 1999.

Alternative 3	GPR
1999-01 REVENUE (Change to Bill)	- $2,800,000

4. Maintain current law.

Alternative 4	GPR
1999-01 REVENUE (Change to Bill)	- $2,640,000

Prepared by: Faith Russell

1999 **Date (time) needed** ____________ LRB b0656/1

JK & PJD:kmg:___

LFB BUDGET AMENDMENT
[ONLY FOR LFB]

See form **AMENDMENTS — COMPONENTS & ITEMS.**

LFB AMENDMENT
TO 1999 ASSEMBLY BILL 133 AND 1999 SENATE BILL 45

>>FOR JT. FIN. SUB. — NOT FOR INTRODUCTION<<

At the locations indicated, amend the bill as follows:

#. Page . . . . , line . . . . :

#. Page . . . . , line . . . . :

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JK:kmg:km

1999 – 2000 LEGISLATURE

A

~~SENATE~~ AMENDMENT ,

TO 1999 SENATE BILL 45

At the locations indicated, amend the bill as follows:

1. Page 907, line 10: delete lines 10 to 25.

2. Page 908, line 1: delete lines 1 to 17.

3. Page 1297, line 15: delete lines 15 to 21.

4. Page 1308, line 12: delete lines 12 to 18.

5. Page 1476, line 18: delete lines 18 to 21.

(END)

State of Wisconsin
1999 – 2000 LEGISLATURE

LRBb0656/1
JK&PJD:kmg:km

LFB:......Russell – Timeshares

FOR 1999–01 BUDGET — NOT READY FOR INTRODUCTION

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