

AGENDA
GRAND MARAIS PLANNING COMMISSION
December 5, 2018, 4:00 P.M.

A. CALL TO ORDER

B. ROLL CALL

C. ADOPT AGENDA

D. APPROVE MINUTES

E. PUBLIC HEARINGS

None.

F. OLD BUSINESS

1. County Assessor, Vacation Rental Report

G. NEW BUSINESS

ADJOURN

Planning Commission
Minutes
November 7, 2018

Meeting was called to order by Chair Tim Kennedy at 4:00 p.m.

Members present: Tim Kennedy, Stacey Hawkins, Todd Miller, Hal Greenwood, and Michael Garry

Absent:

Staff Present: Mike Roth, Patrick Knight, and Haden Hinchman

Motion by Greenwood, seconded by Garry to approve the proposed agenda. Approved unanimously.

Motion by Garry, seconded by Hawkins to approve the minutes of the October 3, 2018 meeting. Approved unanimously.

Jackie Heilicher is requesting a conditional use permit to operate a single unit lodging facility on property she owns and is selling zoned MU Commercial Residential Mixed Use.

John Oberholzer, realtor for Heilicher, presented the proposal. She is in the process of selling the house to Cascade Vacation Rental to be used as a single unit lodging facility. Whether the sale goes through or not, Heilicher would like to the ability to operate the lodging unit. No other comments were received from the public.

The Commission discussed the proposal. The applicant has described space for 2-3 off street parking spaces accessed by the alley. The existing single car garage will be converted to a third bedroom for the property. The three bedrooms would be able to be licensed by the department of health for 5 occupants. The commission discussed setting an occupancy limit as a condition of the permit.

The Commission made the following findings:

1. **The use conforms to the land use or comprehensive plan of the City.**
Lodging is an allowed conditional use in the MU zone.
2. **The use is compatible with the existing neighborhood.**
Similar lodging and a mix of commercial and residential uses already exists in the zone.
3. **The use will not impede the normal and orderly development and improvement in the surrounding area of uses permitted by right in the zone district.**

The structure and adequate off-street parking already exist, and lodging already coexists with the neighborhood.

4. **The location and character of the proposed use is considered to be consistent with a desirable pattern of development for the area.**

The small-scale lodging is described in the zoning purpose statement as consistent with the current character.

Motion by Greenwood, seconded by Miller to recommend approving the conditional use permit with the following conditions: the property will provide two off-street parking spaces, the property will be rented as a single operating unit, and the property will be rented to a maximum of 6 occupants. Approved Unanimously.

The Commission continued its discussion about small scale lodging in the Downtown Waterfront district. They looked at possible changes to the ordinance to better define standards for small scale lodging. The Commission wanted to continue discussion next meeting on small scale standards after researching what other cities standards look like. They discussed possible parking changes or requirements for new construction in the DW district. The Commission also expressed interest in continuing the rezoning process for Creechville.

There being no further business, the meeting adjourned at 5:24 p.m.

City of Grand Marais

MEMO

TO: Grand Marais Planning Commissioners
FROM: Mike Roth
DATE: December 3, 2018
SUBJECT: Vacation Rental Report, County Assessor

County Assessor Todd Smith will be at the meeting to discuss recent County actions regarding vacation rentals. Attached are a recent news release and a staff report for background.



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MEDIA RELEASE

Short-Term Vacation Rentals in Cook County a Hot Topic

November 21, 2018 – Short-term vacation rentals, properties advertised on sites like VRBO, Airbnb, HomeAway, etc., are a hot-trend in Cook County, around the country and the world. For some, these are lucrative operations, and properties are being purchased specifically for this purpose. As this trend increases, licensing and appropriate property tax classification have become questions for many jurisdictions, as consistent standards do not yet exist. Due to Cook County’s popularity as a prime, year-round tourist destination, Cook County has some of the highest percentages of short-term vacation rentals in the state, and is leading the way on development of standards and classification.

What is a Short-Term Vacation Rental?

- A dwelling that is rented short-term (less than 30 days at a time); and/or
- The intent of the occupant to reside for short-term vacation purposes; and/or
- The management or advertising of the dwelling unit as a tourist home or “vacation rental,” on websites such as Airbnb or VRBO, HomeAway, etc., and/or
- The use of a system of reservations, deposits, confirmations, credit cards, or other forms of electronic payment.

Property Classification & Background

In recent years, the emerging trend of renting residential real estate on a short-term basis caught the attention of the Cook County Assessor’s Office and elected officials as it has been the driving force of real estate value increases in a particular area. After further investigation and determining that roughly 10% of the taxable real estate value was being rented short-term, the classification of these properties was questioned.

The County Assessor’s Office has now completed an extensive amount of research across the State, with other jurisdictions and with the Department of Revenue (DOR) to develop the appropriate classification. Many counties statewide have been struggling with how to address this growing issue and to-date, consistent standards do not yet exist.

A comprehensive study, *the 2018 Short-Term Rental Classification Report*, was completed in 2018, by the Cook County Assessor’s Office on the property tax classification of short-term rental properties in Minnesota. (To receive a full copy of the report please email Assessor@Co.Cook.MN.US and request a copy). Through this research around 300 short-term rental cabins/houses were found, in addition to over 300 resort units who list through short-term rental sites, were identified.

The majority of the short-term rental properties in Cook County are classified as Seasonal Residential Recreational Non-Commercial(SRR). The SRR class does not fit an income-producing property as it specifically states ‘Non-Commercial’ in the classification and description of the class. The SRR classification fits the family cabin with seasonal and recreational use, not producing an income.

MEDIA RELEASE

To classify an income-producing property that is used year-round, similar to a seasonally used cabin, did not seem equitable to the taxpayers of Cook County. With the SRR Classification, some of the property tax is exported to the State in the form of “State General Tax” and does not remain locally. A threshold was identified in which a short-term rental is no longer a Seasonal Residential Recreational property and is considered a residential rental property – when it is rented more than 30 days and less than 250 days within a calendar year.

Through analyzation of Department of Revenue Publications reports, info & ed opinions, previous case law, state statute and examining other jurisdictions, the Assessor determined the appropriate classification is residential non-homestead for the majority of short- term rental properties.

If a property is rented less than 30 days, the rental use would be considered incidental to any other use. If a property is rented short-term over 250 days, it will be classified as a commercial use. All properties rented short-term between 30-250 days, unless qualified as a seasonal resort will be classified as one of the residential non-homestead classifications.

New Classification and What It Means

In November 2018, the Cook County Assessor opted to implement a 2019 Classification Change for Short-Term Vacation Rentals in Cook County, which will be realized/payable in 2020. Most properties listed as rentals are currently classified as Seasonal Recreational and will be changed to Residential Non-Homestead. As a result of changing the classification on these properties, the Cook County Net Tax Capacity and Referendum Market Value will increase while these properties will no longer be subject to the State General property tax. County Auditor Braidy Powers indicates this will keep a greater portion of the taxes that currently go to the State, here in the County and in some cases property owners may see a reduction in their overall tax rates. The Assessor’s Office regularly updates the list of parcels available for short-term rentals in the County. The County Auditor estimates this change in classification will divert over \$300,000 or approximately 3% of the 2018 property tax levy* currently going to the state general property tax, to the County’s general fund and local referendum levies. **The amount of property tax collected county wide - 2018 County Budget.*

How Will a Classification Be Determined?

All short-term rentals will be examined on a case-by-case basis to determine the number of days rented during the year. Criteria the Assessor’s Office will use to determine the appropriate classification are influenced by The Minnesota Department of Revenue, The Appraisal Standards Board/Appraisal Foundation, The Internal Revenue Service, Appraiser Peer’s, and general real-estate and appraisal concepts.

Ultimately the goal of the Assessor’s Office is to classify these properties according to Minnesota statute 273.13.

Short-Term Rental Property - Tax Classification Report

Region IX Presentation

August 17th, 2018

Presented by

Todd Smith & Bob Thompson

Cook County Assessor's Office

MAAO Region IV

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Introduction:

This report was drafted as the result of a comprehensive study of the property tax classification of short-term rental properties, also referred to as Vacation Rentals or Vacation Rental By Owner (VRBO). Since the emergence of online marketing platforms like AIRBNB (2008) and VRBO.com (1995), the presence of short-term rentals has been increasing at a rapid rate both locally and nationally.

During the 2018 Cook County Board of Appeals, a number of taxpayers informally appealed or inquired about a 10% value increase to their cabin properties. The Assessor's office recognized a number of recent sales in a particular neighborhood which were outside the acceptable sales ratio. The sales required the Assessor to increase values by 10% in the defined neighborhood, Cascade Beach Rd, a four mile road along Lake Superior, between Lutsen & Grand Marais, MN. Cascade Beach Rd has 117 parcels, 110 improved, of those, 23 are advertised as short-term rentals. Upon providing sales information to the appellants, it was discovered that three of the recent sales were purchased by one corporation and have since become short-term rental endeavors.

The Assessor's office, having already addressed the valuation portion of these properties, was now questioning the classification of short-term rental properties. The County Assessor is responsible for determining which of the Minnesota use classifications is appropriate (MN Statute 273.13). When a property is being used to produce an income, a commercial classification may be appropriate, however there are a number of income-producing properties which are not classified as commercial property.

The Assessor often uses the Minnesota Department of Revenue (DOR) Property Tax Manual when classifying the use of a property. In addition to the DOR tax manual, the Assessor looks to how similarly used properties are classified within their jurisdiction and how peers in other jurisdictions are classifying similar properties. Ultimately applying the appropriate use classification to comply with MN Statute 273.13, is to be determined by the County Assessor.

Cook County determined six potential classifications for short-term rental properties. Each classification has specific requirements laid out in state statute. The Minnesota Association of Assessing Officers (MAAO) also maintains a list of frequently asked questions posed to the DOR, some of which pertain to classifying short-term rental properties.

There is previous case law that some might argue establishes a clear and undisputable commercial use classification. This report outlines the potential tax court arguments that could arise with simply applying a commercial classification on all short-term rental properties.

This report illustrates the various factors analyzed & considered and is summarized by how Cook County will be classifying short-term rental properties moving forward.

Potential Classifications:

The DOR suggest classifying properties based on their primary use. There are six different classifications which were analyzed for the potential classification of the various different short-term rental properties. Properties with a dual use can be split-classed based on space/area but cannot be split-classed based on time/duration.

- 1) 3a – Commercial/Industrial
- 2) 4b(1) – Residential Non-homestead 1-3 Units
- 3) 4bb – Residential Non-homestead Single Unit (Not Previously SRR)
- 4) 4c(1) – Seasonal Residential Recreational Commercial (Resort)
- 5) 4c(12) - Seasonal Residential Recreational Non-Commercial (Cabin)
- 6) 5(2) – All Other Property

Some short-term rentals were discovered to be homesteaded properties, either offering the entire house or simply offering to host guest in a portion of the home while the homeowner remains present. The DOR property tax manual provides two examples of when a homestead could be rented without jeopardizing the homestead classification.

- 1) An active service member renting while on deployment, with the intent of returning
- 2) If the owner of the property is required by the Department of Human Services to rent out the property in order to pay for the cost of care received in a nursing home

Previous case law suggest homesteads have historically been protected by tax court judges, a homestead rented short-term could simply be an incidental use.

Of the six potential classifications, our office analyzed if one single classification could be applied to all short-term rentals, if they should each be studied and analyzed for the purposes of split-classification, or if they simply are something else altogether and do not fit any classification besides the “5(2) – All Other Property” classification. In order to determine primary use, the Assessor would have to rely on numbers provided by the property owner. Some IRS forms indicate number of days rented & number of days for personal use, the Assessor would have to formally request those forms.

Burden on Local Government:

The burden on local government to track what properties are rented short-term is substantial. Cook County has a vacation rental committee, the committee has determined that rental licensing was the quickest and easiest way to track short-term rental activity. The alternative was interim/conditional use permits, Cook County land services estimated each conditional use permit would require 10-15 hours of staff time and was not feasible. A private company which provides annual tracking of short-term rentals charges a fee based on the number of operating rentals. This type of research and tracking is unprecedented for an Assessor’s office staff. Cook County has over 600 short-term rentals, conditional use permits would amount to 6,000 Land Services staff hours conservatively (or roughly three full-time staff annually).

Resources for Determining Classification by Use:

1) Physical Characteristics:

The majority of the time, an Appraiser can determine the classification of a property by looking at the improvements. The first paragraph of module three in the DOR property tax manual states *“In Minnesota, property is classified according to its use on the annual assessment date of January 2. If a property is improved with a structure, the use of the property is typically quite clear – residential, commercial, industrial, etc. If there is not a structure, the use of the property may be less evident.”*

Based on the Physical characteristics, the majority of short-term rentals would be viewed as residential homes or cabins with the exception of some being located in buildings previously used for more obvious commercial uses (such as retail or service-industry buildings).

2) Knowledge of Property:

If a jurisdiction is requiring short-term rental licensing or permitting it eases the burden on the Assessor’s Office to determine which properties are being used as short-term rentals. Cook County dedicated an Assessor’s Office staff member to track down all of the short-term rentals advertised on the various marketing platforms. The process involved browsing various “Host” websites, locating by GIS imagery, searching property records and comparing Assessor photos with advertisements. There are multiple private companies that provide short-term rental tracking services for local governments.

3) Department of Revenue Property Tax Manual:

In analyzing short-term rentals, it was determined that there are six potential classifications, each has been listed below along with a summary of the DOR Property Tax Manual description of that classification.

- a. **3a – Commercial/Industrial & Public Utility:** *Commercial, industrial, and utility real and personal property is class 3a. In general, commercial properties are office buildings, retail stores, malls, hotels, banks, restaurants, service outlets, etc.; whereas industrial properties are often manufacturing, warehouse, and distribution facilities.*
- b. **4b(1) – Residential Non-homestead 1-3 Units:** *Non-homestead residential real estate, typically either the primary residence of someone or a vacant dwelling not used for any purpose, less than four units that does not qualify as class 4bb, other than seasonal residential recreational.*
- c. **4bb – Residential Non-homestead Single Unit (Not Previously SRR):** *Non-homestead residential real estate containing one unit, other than seasonal residential recreational property.*
- d. **4c(1) – Seasonal Residential Recreational Commercial (Resort):** *Devoted to commercial temporary and seasonal residential occupancy for recreation purposes (resorts) for not more than 250 days in the year preceding the year of assessment. The property must contain three or more rental units. Must provide recreational activities on site (exception for populations under 2,500 if a state administered DNR trail is present). At least 40% of the property’s annual gross lodging receipts must be from business conducted during 90 consecutive days. *Additional requirements for 20+ units or townships with a population over 2,500 and no DNR trail.*
- e. **4c(12) - Seasonal Residential Recreational Non-Commercial (Cabin):** *Non-commercial seasonal residential recreational property, e.g. cabins, is real and personal property devoted to non-commercial temporary and seasonal residential occupancy for recreation purposes.*
- f. **5(2) – All Other Property:** *All other property not otherwise classified and not meeting the requirements for class 2b, rural vacant land.*

4) Department of Revenue Info & Education Opinions:

In researching short-term rentals and commercial use of a residential structure, 14 FAQ's to the DOR appeared to have some relevance, of those 14, four were posed by either a current or past Cook County Appraiser. Of the questions posed, some were similar with different responses, it was noted that of the 14 FAQ's there was seven different DOR representatives responding and in one response it was unknown who responded, the questions date back to July, 2002.

Over the course of the past 16 years not only have new classifications been created but tax policy objectives in the legislature change over time. The DOR Property Tax Manual states: *"The Uniformity Clause of the Minnesota Constitution allows for different classifications of property to be taxed at different rates. Each classification of property has a unique classification rate which is set by the Minnesota Legislature. The Legislature may change these classification rates to accomplish various tax policy objectives."*

Our office recognizes these changes and therefore focused on the most recent DOR opinions. In a response our office received in June 2018 the DOR recommended a primary use test. A couple of questions immediately resulted from the primary use method.

- a. Does 183+ days establish a primary use?
- b. Do vacant days count as seasonal recreational days(4c(12)) or vacant dwelling used for nothing days(4b(1))?

The issue we discovered with the primary use method, is that a two unit property in which the primary use is short-term rental(rented over 183 days) is then classified as commercial, while a three(+) unit would have to cross the 250 day threshold to become commercial. We believe this could be viewed as a tax unfairness by one and two unit property owners. An alternative would be to set the commercial threshold at 250 days on all short-term rental properties.

5) Department of Revenue Publications:

In October 2017, the DOR issued a Memo titled *"Guidance on Residential Non-Homestead Classification"*. The memo addresses parcels with multiple non-homestead unit/dwellings. All of the examples provided in the memo indicate the unit/dwellings which are not the homesteaded unit/dwelling should be classified as one of the Residential Non-homestead classification options without stipulating whether or not it is someone's primary residence, or vacant and used for nothing.

The *"Assessment and Classification Practices Report(Residential)"* dated February 2007 addresses dual-use properties. The recommendation is that a primary use test be applied when a dual-use is evident. The report specifically addresses whether a property used seasonally and rented in the interim should have to be rented a minimum number of months in order to receive the non-homestead classification. The report indicates the committee decided against the minimum recommendation as there is no such minimum for the homestead classification.

The *"Assessment and Classification Practices Report(Resort)"* dated February 2006 addresses individually owned units in a resort community. The report indicates that an individually owned unit within the resort, if rented over 30 days should be classified as a residential non-homestead and if more than three units are owned they should be treated as apartments.

These publications appear to support the residential classifications due to the rental activity involved.

Previous Case Law Related to Short-Term Rentals.

Two previous tax court cases appear to be relevant in determining the use and classification of short-term rental properties. In one case an investor argues that he used a property as an investment of like-kind property after a 1031 exchange, the Commissioner of Revenue argued it was used as a residence due to the amount of personal use exceeding 10% of the number of days rented. The other case was a short-term rental which the tax court upheld the County Assessor's 3a Commercial classification.

- a. In March 2013 R.J. & J.B. Danielson appealed to the Commissioner of Revenue whether a property obtained as part of a 1031 exchange was in fact used in a trade or business, namely, as a rental property. The Commissioner of Revenue cited "IRS Publication 527" which defines investment use versus personal use for income tax purposes.
 - IRS Publication 527 states: *"If a dwelling is used for personal use 14 days or 10% of the days it is rented at fair rental price (whichever is greater) the dwelling is used as a residence (rather than an investment, trade or business)"*
- b. In June 2014 T.C. Hewitt LLC was the petitioner in a tax court case versus McLeod County. The petitioner challenged a 3a Commercial classification which was the result of short-term rental activity. With detailed data regarding the primary & additional uses and citing "The Assessment & Classification Practices Report" (which states only someone's primary residence or a vacant dwelling used for nothing can receive the Residential Non-Homestead classification) the tax court upheld the 3a Commercial classification.
 - The Assessment & Classification Practices Report does state that in order for a property to receive the Residential Non-homestead classification the dwelling is either someone's primary residence or is vacant and not used for any purpose.
 - The Assessment & Classification Practices Report also discusses "dual-use properties" under that section the following statement is made: *"The committee considered requiring that a property be rented for a certain number of months to receive the nonhomestead class instead of 4c(1) seasonal residential recreational but decided against this recommendation because there is no such requirement for the homestead class."*
 - This appears to be a contradiction within the report and indicates a property can be Residential Non-Homestead without being someone's primary residence.

6) Similar Use, Peers and USPAP

The most similar use to short-term residential rentals is a long-term residential rental. The differences being increased income resulting from shorter, more frequent leases. Investment Real Estate that is not used as a main home or cabin, is typically purchased by an investor after doing market research, analyzing operating-income statements and ensuring a return on investment.

Assessors do not classify similarly used properties different due to income differences, USPAP Standard Rule 6-6 states *"An appraiser should appraise as if in fee-simple and use market rents rather than actual contract rents"*. Long-term rental properties typically are classified as residential non-homesteads, this is consistent throughout the state of Minnesota and follows DOR guidance.

Short-term rental properties in four northern Minnesota counties and four Twin-Cities metro area counties were analyzed by the Cook County Assessor's office, all of the identifiable properties were found to either be Homesteads or Non-homesteads, none were found to be Seasonal Residential Recreational or Commercial.

7) State Statute 273.13 – Classification of Property

Minnesota statute 273.13 defines the classification of property that has passed legislation. The classifications have a title and are followed by a description of the properties which fit that category. Class 3a, Commercial/Industrial/Utility does not provide a definition of what constitutes commercially used properties. The six potential classifications analyzed are listed below along with the definitions of those classifications.

- a. **3a – Commercial/Industrial/Utility:** *Commercial and industrial property and utility real and personal property is class 3a*
- b. **4b(1) – Residential Non-homestead 1-3 Units:** *Residential real estate containing less than four units that does not qualify as class 4bb, other than seasonal residential recreational property;*
- c. **4bb – Residential Non-homestead One Unit(Not Previously SRR):** *nonhomestead residential real estate containing one unit, other than seasonal residential recreational property; Property that has been classified as seasonal residential recreational property at any time during which it has been owned by the current owner or spouse of the current owner does not qualify for class 4bb.*
- d. **4c(1) - Seasonal Residential Recreational Commercial (Resort):** *except as provided in subdivision 22, paragraph (c), real and personal property devoted to commercial temporary and seasonal residential occupancy for recreation purposes, for not more than 250 days in the year preceding the year of assessment. For purposes of this clause, property is devoted to a commercial purpose on a specific day if any portion of the property is used for residential occupancy, and a fee is charged for residential occupancy. Class 4c property under this clause must contain three or more rental units. A "rental unit" is defined as a cabin, condominium, townhouse, sleeping room, or individual camping site equipped with water and electrical hookups for recreational vehicles. A camping pad offered for rent by a property that otherwise qualifies for class 4c under this clause is also class 4c under this clause regardless of the term of the rental agreement, as long as the use of the camping pad does not exceed 250 days. In order for a property to be classified under this clause, either (i) the business located on the property must provide recreational activities, at least 40 percent of the annual gross lodging receipts related to the property must be from business conducted during 90 consecutive days, and either (A) at least 60 percent of all paid bookings by lodging guests during the year must be for periods of at least two consecutive nights; or (B) at least 20 percent of the annual gross receipts must be from charges for providing recreational activities, or (ii) the business must contain 20 or fewer rental units, and must be located in a township or a city with a population of 2,500 or less located outside the metropolitan area, as defined under section [473.121](#), subdivision 2, that contains a portion of a state trail administered by the Department of Natural Resources. For purposes of item (i)(A), a paid booking of five or more nights shall be counted as two bookings. Class 4c property also includes commercial use real property used exclusively for recreational purposes in conjunction with other class 4c property classified under this clause and devoted to temporary and seasonal residential occupancy for recreational purposes, up to a total of two acres, provided the property is not devoted to commercial recreational use for more than 250 days in the year preceding the year of assessment and is located within two miles of the class 4c property with which it is used. In order for a property to qualify for classification under this clause, the owner must submit a declaration to the assessor designating the cabins or units occupied for 250 days or less in the year preceding the year of assessment by January 15 of the assessment year. Those cabins or units and a proportionate share of the land on which they are located must be designated class 4c under this clause as otherwise provided. The remainder of the cabins or units and a proportionate share of the land on which they are located will be designated as class 3a. The owner of property desiring designation as class 4c property under this clause must provide guest registers or other records demonstrating that the units for which class 4c designation is sought were not occupied for more than 250 days in the year preceding the assessment if so requested. The portion of a property operated as a (1) restaurant, (2) bar, (3) gift shop, (4) conference center or meeting room, and (5) other nonresidential facility operated on a commercial basis not directly related to temporary and seasonal residential occupancy for recreation purposes does not qualify for class 4c. For the purposes of this paragraph, "recreational activities" means renting ice fishing houses, boats and motors, snowmobiles, downhill or cross-country ski equipment; providing marina services, launch services, or guide services; or selling bait and fishing tackle;*

- e. **4c(12) - Seasonal Residential Recreational Non-Commercial (Cabin):** *real and personal property devoted to noncommercial temporary and seasonal residential occupancy for recreation purposes.*
- f. **5(2) – All Other Property:** *all other property not otherwise classified.*

Of the six classifications analyzed, four have the verbiage “Residential” in the title and description, class 4c(1) has both Residential and Commercial in the title. Depending on the number of units/bedrooms, some short-term rentals would fit the 4c(1) definition (almost all of Cook County has a DNR administered trail & neither the city of Grand Marais or any of the townships exceed a population of 2,500 so no recreational activities need to be provided in the majority of Cook County). The majority of short-term rental properties fit the definition of class 4b(1), which is 1-3 unit, residential, non-homestead. Few properties which have minimal rental activity and are still used seasonally and recreationally by the owner could be classified as 4c(12), Seasonal Residential Recreational.

Based on the possibility of 3+ unit, short-term rental properties being classified as 4c(1) property, the 250 days of rental use appears to set the threshold for crossing over to 3a Commercial property on all short-term rental properties.

Implications to Property Owners and Government:

The public, rental property owners and management companies have inquired as to what the implications of re-classifying these properties means. A thorough study was done analyzing all of the different potential classifications. The county has a spreadsheet with this information available to the public and a brief description of the implications are laid out below.

- The tax implications to short-term rental property owners and government could be significant. Cook County has 10% of the overall county real estate, or over \$160 million being used as short-term rental property.
- The majority of the short-term rental properties in Cook County are currently classified as 4c(12) Seasonal Residential Recreational. With the amount of value and a 4c(12) classification, over \$290k is collected on these properties by the county and sent to the state general fund each year.
- A 4b(1) classification would have little effect on the taxpayers, most properties would see a slight increase while some would see a decrease on their tax statement, while at the same time would result in additional revenue to Cook County, over \$333k, or over 3% of the 2018 property tax levy would be collected on these properties.
- A commercial classification would result in significant increases to taxpayers, in some cases tripling the tax bill and the majority of the increase would either be sent to the state general fund or would leave Cook County via the fiscal disparities program.

Executive Summary:

The following summarizes a comprehensive study completed in 2018 by the Cook County Assessor's Office, on the property tax classification of short-term rental properties in Minnesota. To receive a full copy of the report please email Assessor@Co.Cook.MN.US and request a copy of the 2018 Short-Term Rental Classification Report.

Cook County is a high tourism area located in the northeast arrowhead of Minnesota. An increasingly emerging trend of renting residential real estate on a short-term basis caught the attention of the County Assessor's office as it was the main driving force of real estate values in a particular area. After determining that roughly 10% of the taxable real estate value was being rented short-term, the Assessor questioned the use classification of these properties.

The majority of the short-term rental properties in Cook County were classified as Seasonal Residential Recreational Non-Commercial (SRR). The SRR class does not fit an income-producing property as it specifically states "Non-Commercial" within the title and description of the class. The SRR classification fits the family cabin with seasonal & recreational use, not producing an income. To classify an income-producing property that is used year-round, upwards of half the year, similar to a seasonally used cabin, did not seem equitable to the taxpayers of Cook County.

Initially, the Assessor searched previous case law and found a case in McLeod County where a short-term residential rental was classified as a commercial use. The tax court upheld the Assessor's commercial classification. A property in Cook County was used very similarly to the McLeod County tax court case, however was classified as a seasonal resort and met all of the criteria for that classification. This caused confusion and resulted in a thorough analysis on classifying residential rentals and commercial use of residential structures.

The Assessor determined that there is a threshold in which a short-term rental is undoubtedly a commercial use. Without crossing 250 days of rental activity applying a commercial classification potentially creates a tax unfairness based on the number of rental units the parcel has.

The Assessor determined that through analyzing all of the DOR Publications, DOR Reports, DOR Info & Ed Opinions, previous case law, state statute and examining other jurisdictions, the appropriate classification is residential non-homestead for the majority of short-term rental properties. All short-term rentals will be examined on a case-by-case basis to determine the number of days rented during the year.

If a property is rented less than 30 days, the rental use would be considered incidental to any other use. If a property is rented short-term over 250 days it will be classified as a commercial use. All properties rented short-term between 30-250 days, unless qualified as a seasonal resort will be classified as one of the residential non-homestead classifications.

The process of identifying short-term rentals by licensing, permitting, contracting, or dedicating an Assessor's office staff to identify these properties, will certainly increase the workload and cost to local government. Due to the current classification on the majority of these properties in Cook County, this change will result in additional revenue to Cook County, equal to about 3% of the 2018 property tax levy.