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Phocuswright White Paper

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THE PROFESSIONALIZATION OF U.S. SHORT-TERM RENTALS



In cooperation with

Avalara
Tax compliance done right

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Foreword



As is true in any high-growth industry, one of the biggest constants in the vacation rental industry over the last decade has been change. Change has been rampant as vacation rentals have emerged as a true competitor to the hotel industry, through the quickly shifting COVID-19 travel landscape, and as state, county and city governments have grappled with how to best regulate vacation rentals.

As our industry transitions away from the traditional host-managed property model toward broader adoption of professional management firms, we at Avalara can't help but think about the implications of this professionalization on the future of vacation rental regulations.

Vacation rentals pose a regulatory challenge for several reasons, including that these regulations – and taxes – are imposed at multiple levels of government. Throw in a diverse group of rental hosts, with different rental models and varying understanding of the business requirements expected of them, and one begins to grasp the challenge that state and local officials face: how to best impose and enforce regulations in a consistent manner, in a way that appeals to both hosts and non-host community members.

Given the current enforcement challenges, professionalization may be a tipping point when it comes to the future of vacation rental tax requirements. Just as many states have begun requiring vacation rental marketplaces to collect and remit taxes owed for rentals generated via their platforms, they soon may begin imposing similar requirements among professional property managers. As with marketplaces, it becomes easier for state and local governments to enforce compliance among a small set of business entities than with hundreds of thousands of hosts, thus ensuring jurisdictions recoup lost lodging tax income.

Whether left to hosts or shifted to property managers, an increased rate of compliance in the industry is a goal all stakeholders should work towards. Not only do lodging taxes play a vital role in funding tourism development, but a stronger adherence to state and local requirements increases the likelihood of our industry's longevity.

The continued taxation of the short-term rental industry is a certainty, and jurisdictions will continue to find new ways to enforce compliance and collect lodging taxes owed. As stakeholders within the vacation rental industry, it is up to us to ensure our businesses follow the rules of engagement now to ensure continued growth and success for years to come.

Oliver Hoare

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General Manager - Lodging
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Introduction

The distinction between Host and Property Manager is often ambiguous. Some hosts hire a property manager for limited responsibilities. Others transition to becoming property managers as they grow. To provide a clear demarcation, Phocuswright defines a Host as a person or company managing nine or fewer properties and a PM as a person or company managing 10 or more properties. Hosts who employ a property manager's services are referenced as Managed Hosts.

Short-term rentals (STRs) were already on the path to becoming an integral part of the lodging landscape over the last decade. But pandemic-induced demand thrust them into the limelight and accelerated their growth. STRs are projected to account for 27% of the U.S. lodging market in 2021, a 10-point increase in just two years.

The emergence of STRs as an alternative to hotels has led to the adoption of services that have transformed the industry. Running an STR can be complex and requires implementing and managing technology, day-to-day operations and ensuring regulatory compliance. No surprise then that many hosts are turning to property managers (PMs) for varying degrees of assistance with managing their rentals. This trend towards professionalization has sharply accelerated over the last two years. PMs currently provide many services for hosts but there are still opportunities for growth.

This white paper looks at the changing landscape of STR management, how professional management adds value and offers a way forward as regulatory challenges loom. It is based on key findings from Phocuswright's comprehensive research on the U.S. short-term rental market conducted in 2021. The study included quantitative surveys and interviews with key stakeholders. There were 442 qualified respondents to a survey of U.S. hosts, and 90 qualified respondents to a survey of short-term rental property managers. Phocuswright also conducted 13 in-depth interviews with experts across the STR ecosystem.

The Rise of Professional Property Managers

As the STR segment has grown, so has the reliance that hosts place on PMs, with more and more hosts turning to professional property management companies to help manage their rentals. In some cases, hosts choose to have professional firms partially manage their properties, delegating some responsibilities to PMs while they remain involved in day-to-day operations. Other hosts turn to property management companies to fully manage their rentals and assume all management responsibilities. In 2020, over 60% of hosts elected to employ a property manager to fully manage their rentals, up from fewer than 50% in 2019.

There are many reasons why hosts choose to involve a property manager, but the primary draws are convenience and PMs’ in-depth knowledge of the short-term rental industry. Hosts thoroughly value the ability to step back and know that day-to-day management, customer service, compliance and other details will be handled. Sixty-six percent say they involved a PM for the convenience, and 49% rely on them because they are too far from their properties to oversee operations on their own (see Figure 1). The experience and expertise that managers bring to the table also play a key role; 51% of managed hosts note they use PMs for attracting more bookings, and 44% consider them to be more knowledgeable and efficient in running properties compared to what they could do on their own.

Figure 1:
Hosts – Reasons For Using a Property Manager

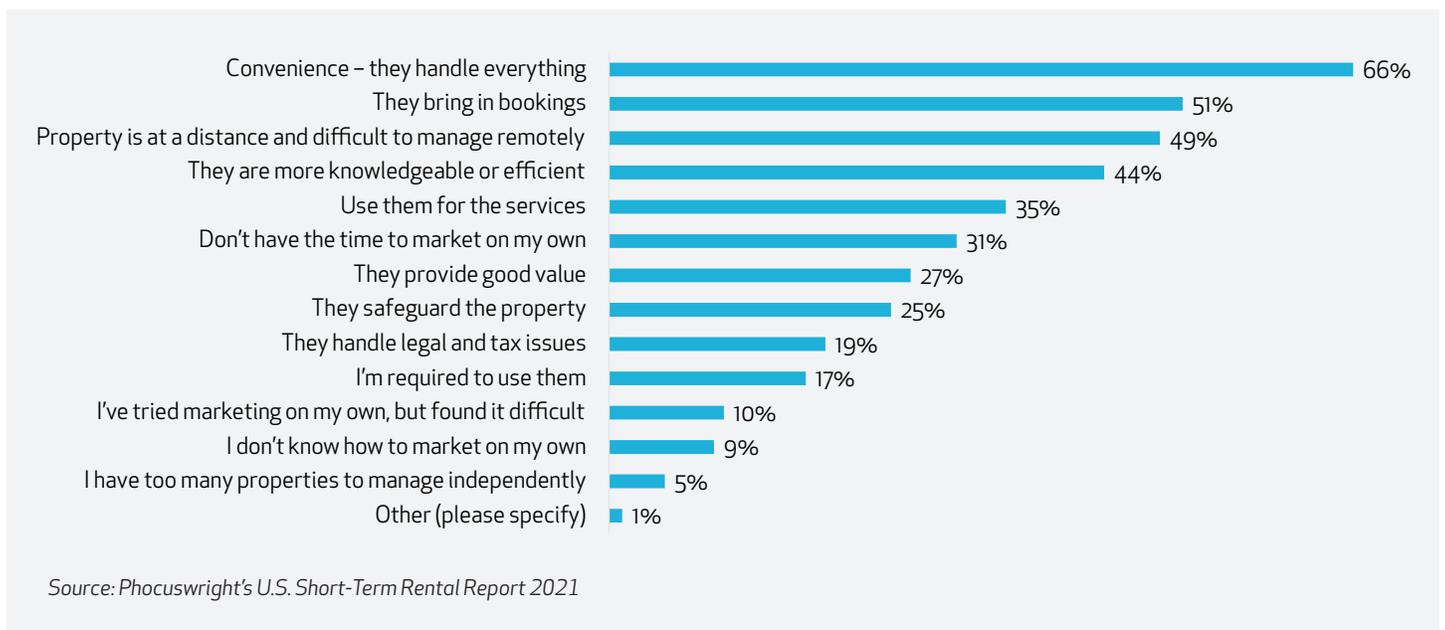
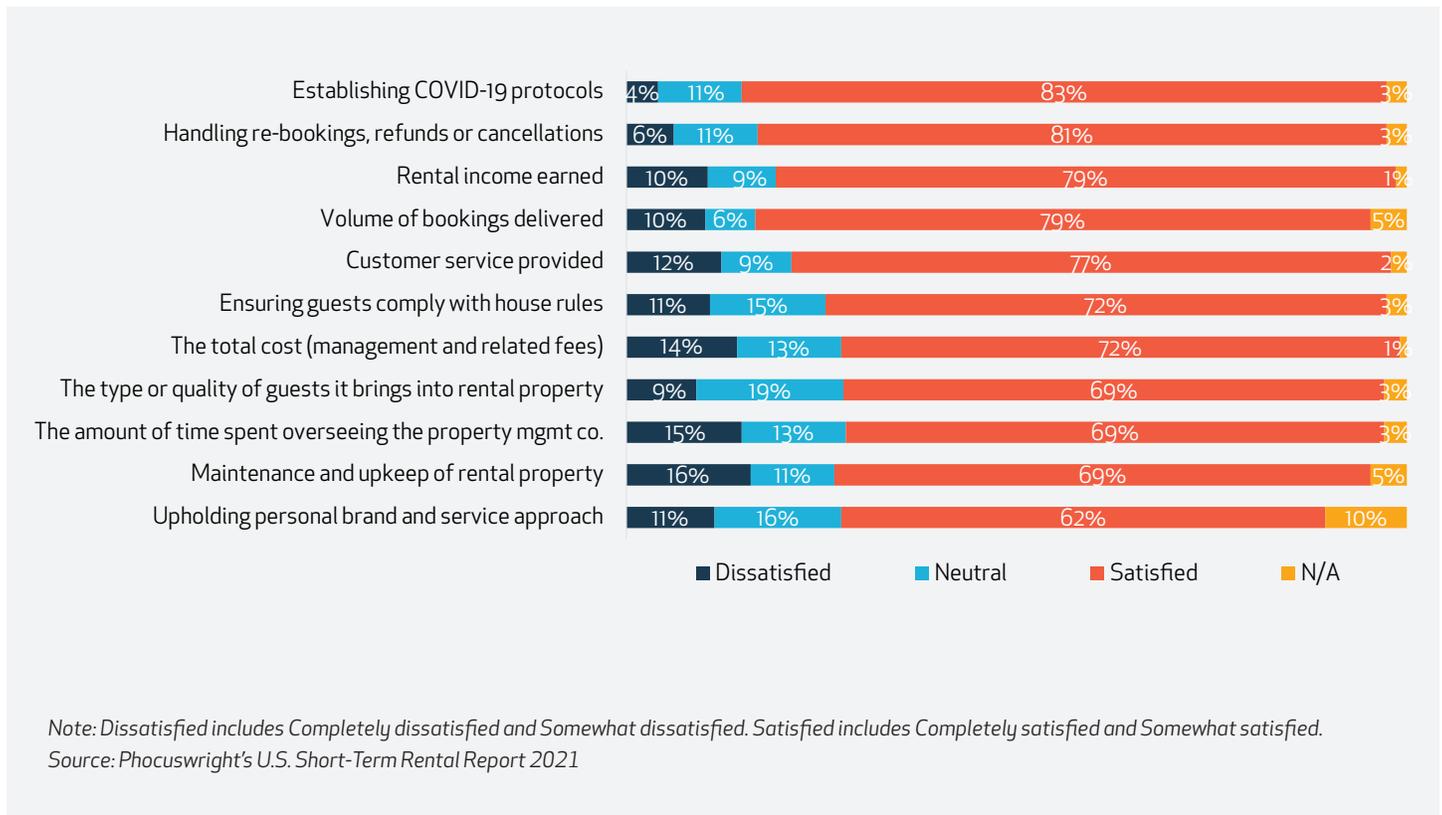


Figure 2:
Hosts – Satisfaction With PM Services

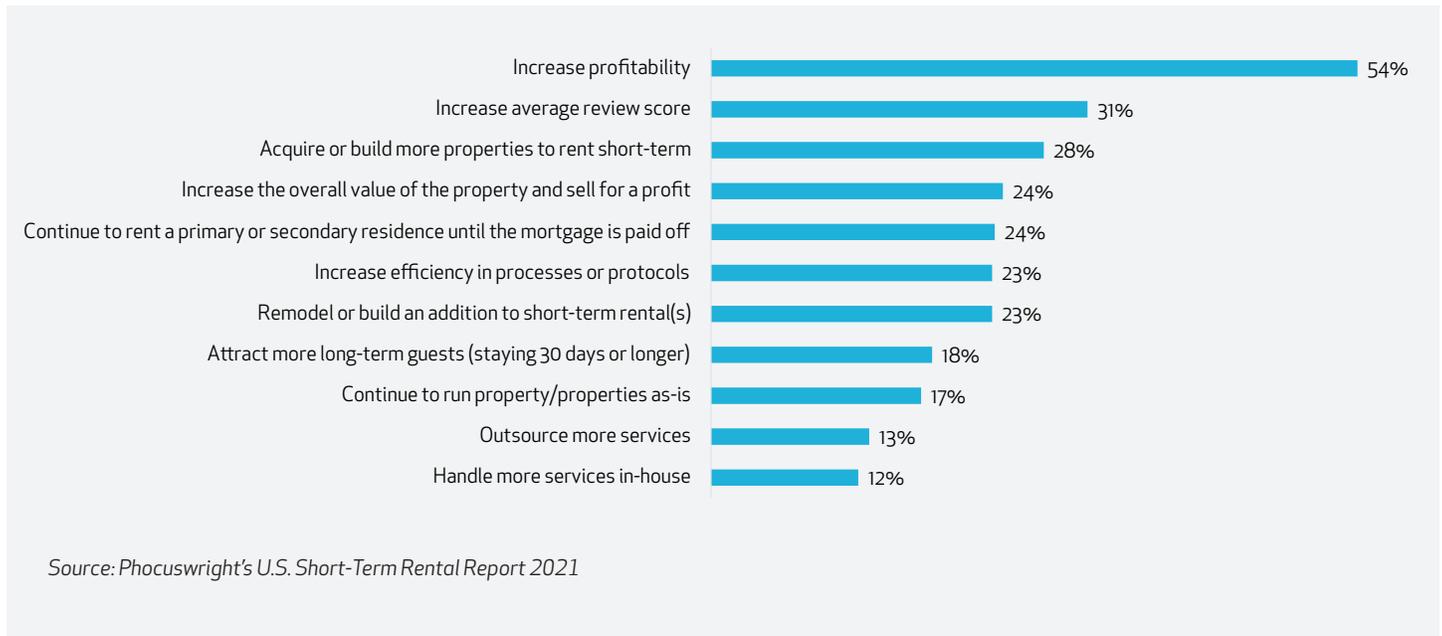
PM performance is generally viewed in a positive light by hosts, regardless of whether a property is fully or partially managed. More than 80% of hosts express satisfaction with how their PMs handle COVID protocols as well as re-bookings, refunds, or cancellations (see Figure 2). And nearly the same proportion say they are happy with the volume of bookings received and income earned.



Hosts who choose a model where some services are managed in-house and some outsourced to PMs are most likely to do so to retain control of the property and its branding. Saving money is usually a secondary factor in the decision to choose a hybrid model. Nearly half of these hosts feel they need to maintain the look and feel of their property themselves. But some management companies may not offer all the services hosts would like to outsource. Twenty-nine percent of hosts who partially outsource their STR management report that their management company does not provide the full spectrum of services they need. This is an opportunity for PMs to fill the gaps in their offerings and provide a wider suite of services.

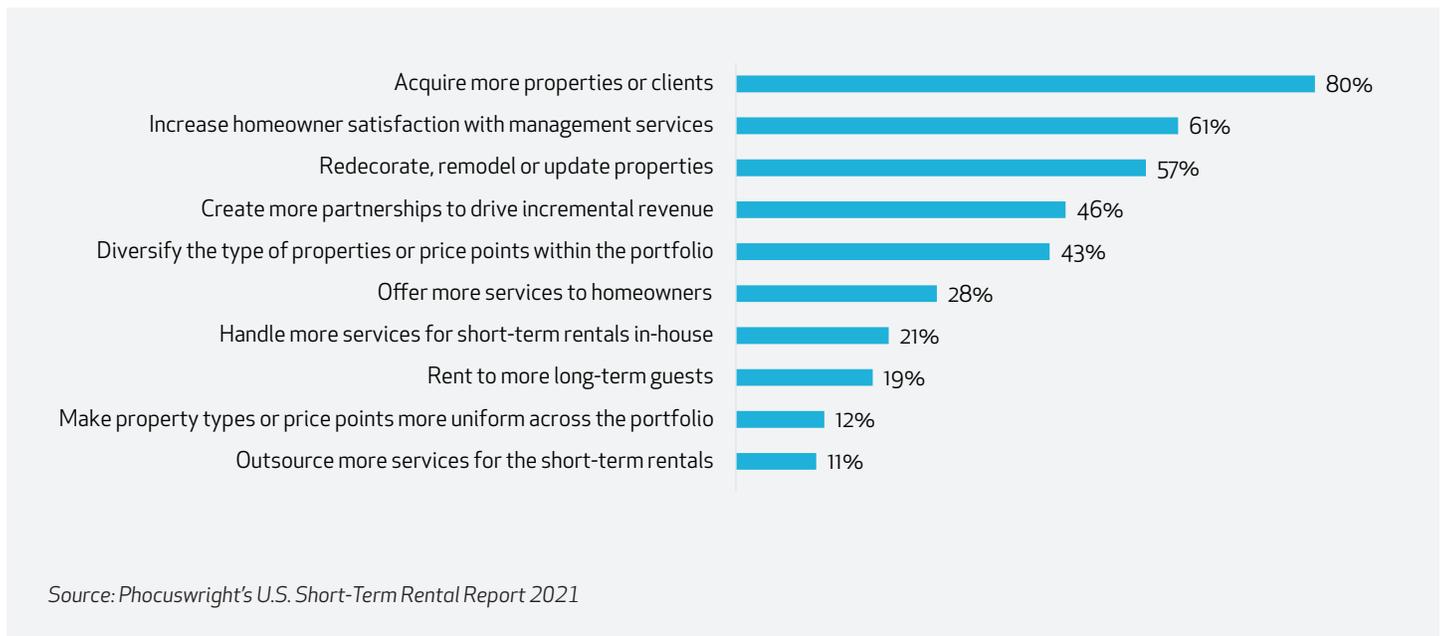
Hosts have a lot of expectations regarding their rental properties, and their goals run the gamut from generating more profit to expanding their portfolio, and even increasing long-term stays. Ultimately, hosts want more from their businesses: more profits, more properties and higher ratings. A majority (54%) want to increase the profitability of their STRs (see Figure 3). Nearly a third aim to improve their ratings while more than a quarter would like to expand their property portfolio. Only a slim minority (17%) are content with the status quo.

Figure 3:
Hosts – Business Goals



Property managers are also highly motivated to grow their businesses. Roughly 80% of survey respondents state that they want to expand their client base and increase the number of properties they manage (see Figure 4). Three in five want to improve their clients' satisfaction with their services. Many also wish to update their managed properties and are actively seeking opportunities to diversify their portfolios with properties of varying types and price ranges.

Figure 4:
Property Managers – Business Goals



Property Managers: Driving and Delivering Value

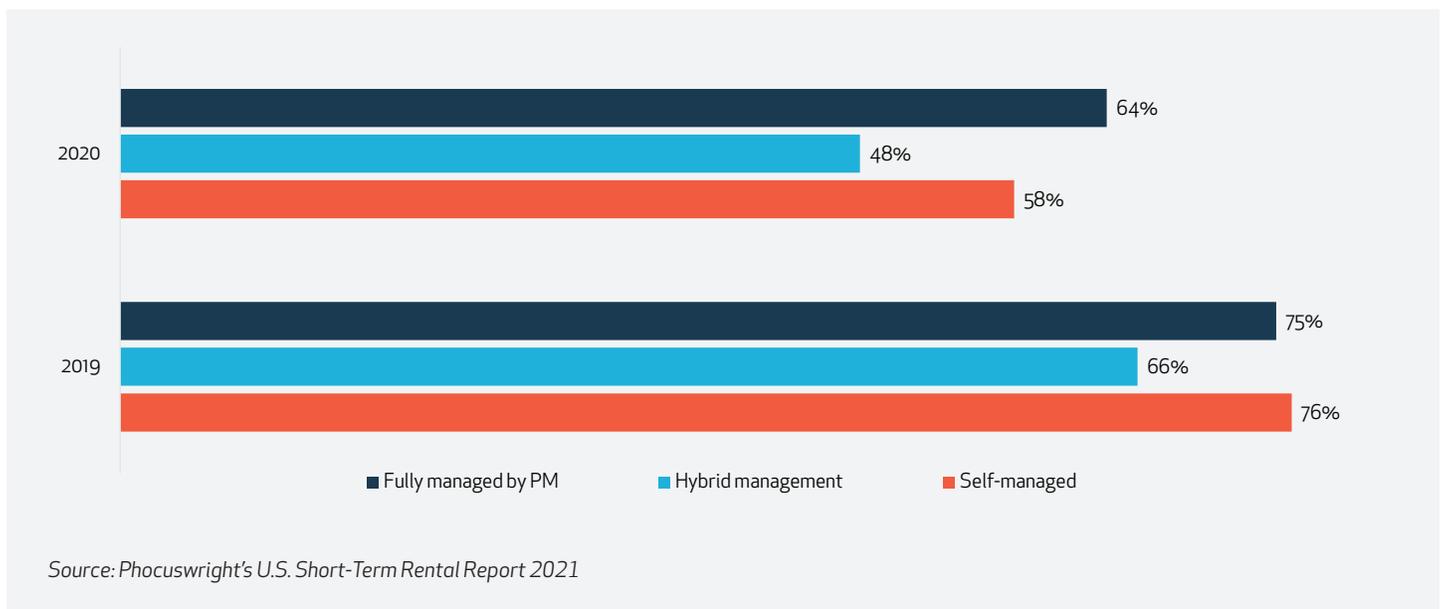
Financial Goals

Property managers offer a variety of modular services to suit different needs. Hosts can choose the degree to which PMs are involved in managing their properties, but when it comes to financial performance, hybrid management falls short. Hosts who used PMs to provide some services but not fully manage their property were the least likely to meet their financial goals in both 2019 and 2020.

Pandemic-related upheaval uncovered important issues around management and profitability. Fully managed and independent hosts had similar likelihoods of meeting their financial goals in 2019, when the landscape was more stable (see Figure 5). However, when uncertainty plagued the markets in 2020, fully managed properties were the most likely to meet their financial goals.

Property managers' expertise makes them adept at dealing with market turbulence. Their professional approach makes them well suited to navigating changes in travel restrictions, pricing protocols, customer expectations and change/cancellation policies. These capabilities lead to a higher likelihood of delivering on financial goals than hosts who stuck to managing their own rentals.

Figure 5:
Hosts Who Met Financial Goals,
by Management Method

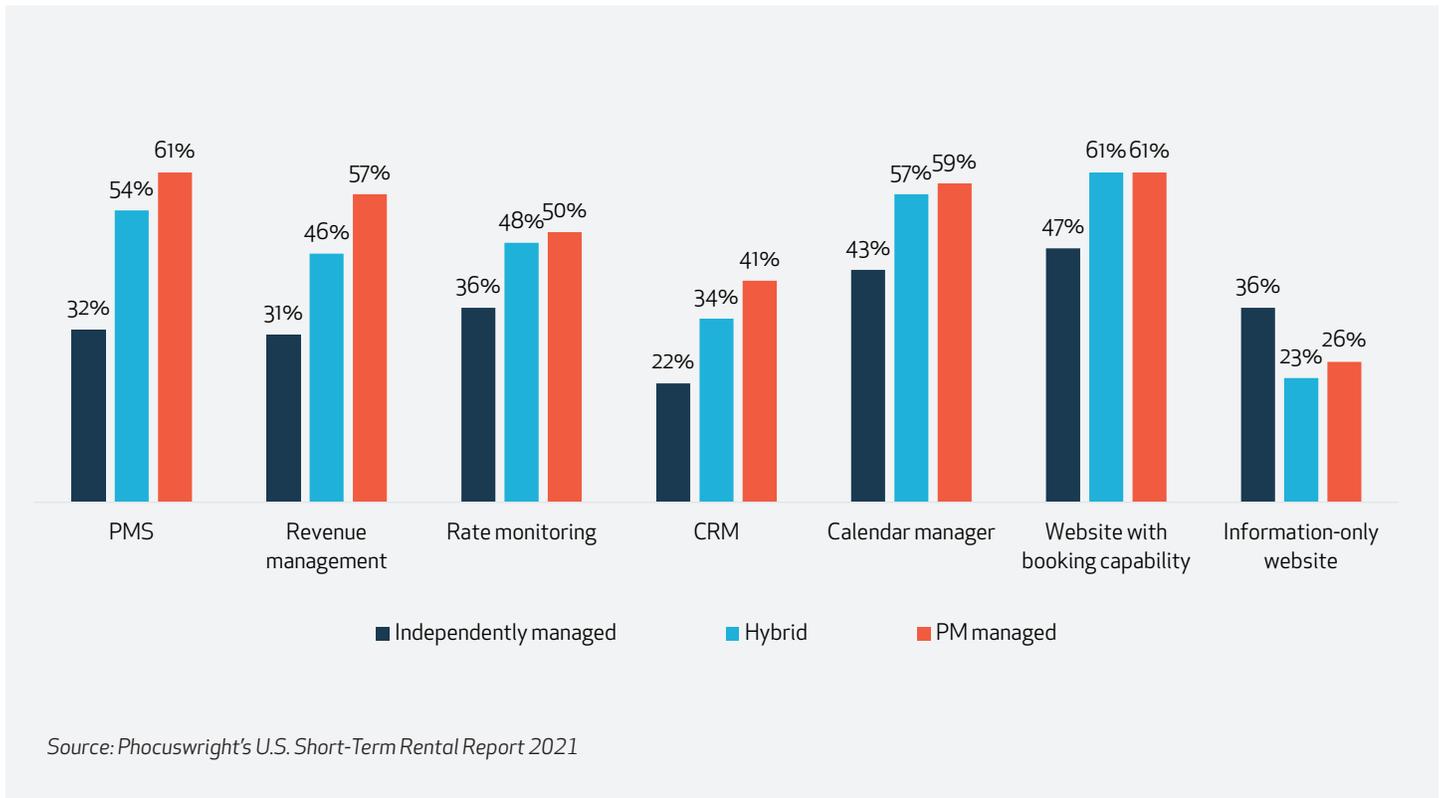


Technology Adoption and Efficiencies

Property managers use a variety of technological tools to drive efficiencies and maintain tight operations across their portfolios. Backend tools like property management systems, rate monitoring tools and revenue management systems are common. But capabilities like booking-enabled websites which allow PMs to establish their own brands and reduce dependence on third parties, and calendar managers which sync availability across channels also have high adoption. Given their relatively larger scale, PMs are far more likely to use technology compared to smaller, independent hosts (see Figure 6).

Technology can assist with strategic pricing and smoother operations in ways that directly contribute to profitability, but independent hosts may not understand the options available or the advantages they confer. Property managers play a vital role in introducing technology to hosts. Their familiarity with the systems and associated benefits makes them a trusted source of information. And while they can encourage hosts to implement more tech-enabled tools, two thirds of PMs also mandate tech usage for properties they manage.

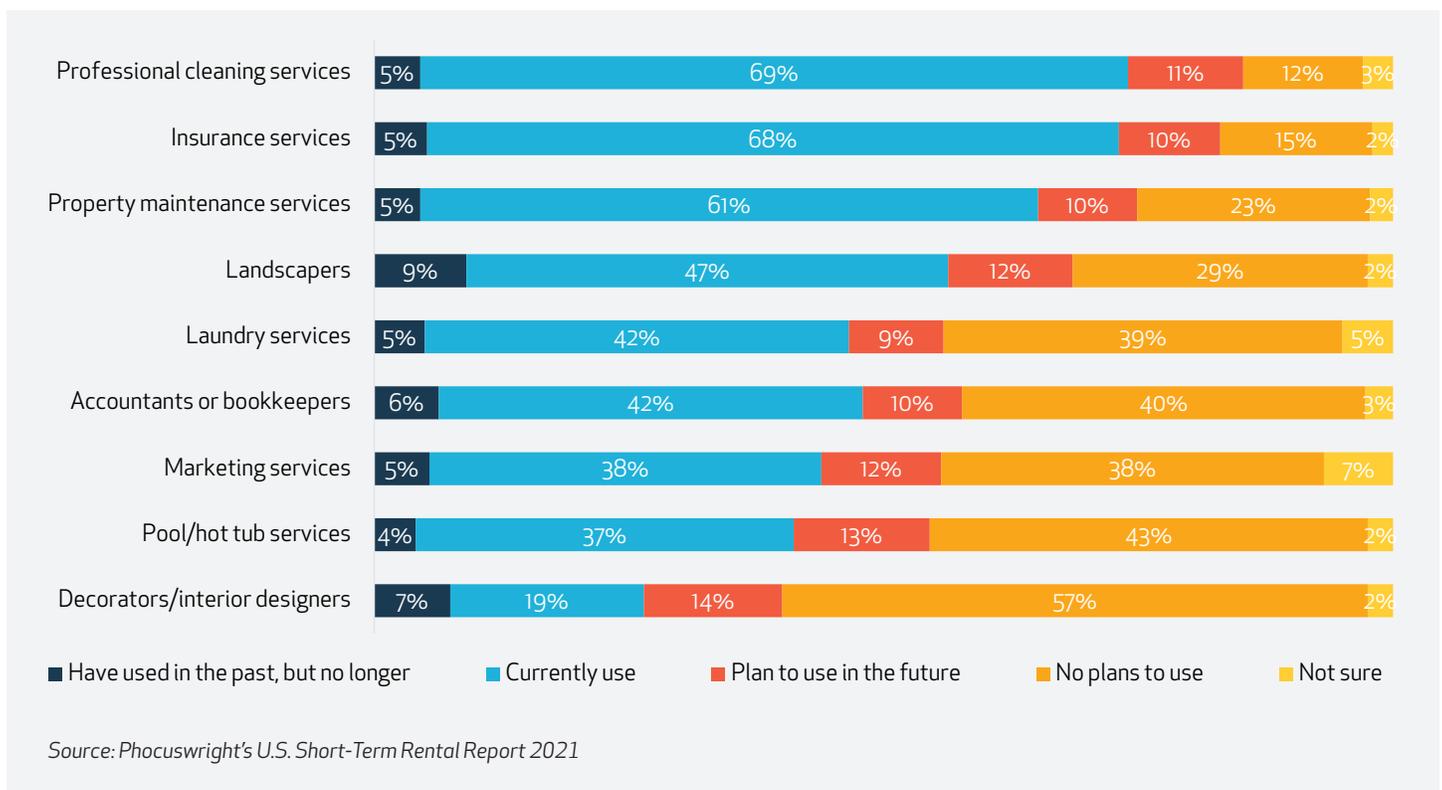
Figure 6:
Technology Systems Adoption,
by Management Model



Professional Services

Hosts' reliance on third parties goes beyond technology to include operational services like cleaning and property maintenance. Hosts with three or more units are the most likely to seek external help for operations and services. Accounting and bookkeeping, marketing and professional decorators are among the professional services hosts utilize. Forty-two percent of all hosts use a third-party to provide financial services related to their STRs, and a further 9% plan to use them in the future (see Figure 7). Property managers are glad to oblige when a host needs help with these services. Ninety-three percent of property managers say they provide accounting services to their clients, and a large majority do so in-house.

Figure 7:
Hosts' Usage of Third-Party Services





A Win-Win Approach to Regulation

Regulation of the short-term rental industry has been a major source of disquiet for hosts and PMs in recent years. There is an inherent tension as destinations try to balance the need for affordable housing with the economics of tourism. The localized nature and changing landscape of regulations contribute to the ongoing uncertainty around STRs.

A large majority of hosts (86%) desire to be good neighbors and work with local authorities to operate their businesses harmoniously and ethically (see Figure 8). Ninety-three percent of PMs indicate that complying with regulations is important to them because they are a part of the local community.

While hosts claim to understand local rules and regulations surrounding rental operations, understanding the intricacies of local and state policies can be daunting, and hosts are more prone to information gaps. PMs may be able to play an assistive role here for their clients. While 92% of PMs are aware of local laws and regulations that concern their rentals, only 78% of independent hosts can say the same. Broadly, PMs are much more likely to stay on top of the regulatory minutiae and keep hosts in compliance, via their services.

Figure 8:
Attitudes Toward Regulation

	Hosts	PMs
Care about complying with local regulations and being viewed as good neighbors	86%	93%
Familiar with local STR laws and regulations	78%	92%
Have adequate resources to understand general STR regulations	74%	80%
Fear that current or future regulations will impact ability to operate	51%	59%
Changes in local regulations have forced a change in business model	39%	49%

Note: Hosts and PMs who agree or strongly agree with these statements.

Source: Phocuswright's U.S. Short-Term Rental Report 2021

However, frustrations arise when guidelines and laws change, or when laws are scripted without input from business owners and hosts. As many as 51% of hosts and 59% of PMs are concerned about the feasibility of operating their businesses in the future. Shifts in what is and is not permitted make running these businesses challenging, forcing alterations to business models.

Industry stakeholders agree that working with governments to create policies that benefit all parties is the way forward. Properly enacted and executed policies must balance income generation for hosts with issues that are important to communities, including affordable housing and other quality of life factors such as noise and parking. Together, hosts and PMs will play a large part in building this thriving future.



Conclusion

The role of property managers in the short-term rental ecosystem is growing as the industry matures. A rising proportion of hosts are choosing to employ full-service property management companies. Their reasons for entrusting their businesses to PMs boil down to the value created through the smooth and profitable operation of their business. Using these professionals enables coherent, consistent and compliant running of short-term rentals.

Independent hosts also have success running their properties. Nonetheless, PMs have gained the confidence of hosts in light of their fluency and success in driving technology adoption, the wealth of services they offer and their ability to deliver financial performance while navigating a challenging environment. As a result, PMs' role in the STR ecosystem is set to grow.

The short-term rental industry has a long runway ahead, but it faces regulatory headwinds. Hosts, property managers and the communities to which they belong stand to benefit from a collaborative approach to policy formulation. A flourishing short-term rental industry will generate jobs and tax revenue for local governments and create shared prosperity for the community.



About Phocuswright

Phocuswright is the travel industry research authority on how travelers, suppliers and intermediaries connect. Independent, rigorous and unbiased, Phocuswright fosters smart strategic planning, tactical decision-making and organizational effectiveness.

To complement its primary research in North and Latin America, Europe and Asia, Phocuswright produces several high-profile conferences in the United States, Europe and Asia Pacific. Industry leaders and company analysts bring this intelligence to life by debating issues, sharing ideas and defining the ever-evolving reality of travel commerce.

Phocuswright also operates PhocusWire, a media service that covers the world of digital travel 365 days a year with a range of news, analysis, commentary and opinion from across the travel, tourism and hospitality sector.

The company is headquartered in the United States with Europe and Asia Pacific operations and local analysts on five continents.

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About Avalara

Avalara is the answer to the unique challenges and frustrations of managing state and local taxes in the lodging and hospitality industry. Our solutions simplify compliance tasks, help reduce risk across the labyrinth of regulations in the hospitality industry and help ensure taxes are collected and remitted accurately. Avalara is a team of tax experts and technologists behind one solution for your business. We live and breathe tax and regulatory compliance, so you don't have to. From independent operators to midsize businesses and Fortune 100 companies, customers choose Avalara for tax compliance tools scaled to their needs. You'll find Avalara around the world helping businesses prepare for growth in the global market.

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