



ASSOCIATION OF DESTINATION MANAGEMENT EXECUTIVES | DEFINING THE DMC PROFESSION

## Texas DMC Tax Legislation

### **Issue #1: Sales Tax**

The Texas Comptroller's office was preparing a rule which would have effectively reclassified DMCs as resellers and changed the model under which DMCs have worked since their inception. The new rule would have required that DMCs collect sales tax on their profit margin, i.e., their services which are not currently taxable services in Texas. Further, entertainment and transportation are not taxable services, but if the DMC were to package an event including these services with a meal, the whole package would be taxed including the otherwise non-taxable services. Collecting tax on these services (that otherwise would not be taxable) would not be fair to the DMC's client and would discourage them from utilizing a DMC and from bringing their meetings to Texas.

### **Issue #2: Margins Tax (Corporate franchise tax)**

In 2005, the state legislature changed the corporate franchise tax formula for Texas from 4.5% of net income to 1% of gross profit margin. In 2008, the change took effect. However, according to the Texas tax code (and contrary to Federal tax code), a service company should not have cost of goods sold and thus could not deduct those costs to determine taxable margin. However, for a DMC, cost of services sold (or flow through expenses for the DMC's clients) may account for 70-90% of gross revenue leaving a gross profit margin of 10-30%. From this gross profit margin, employee compensation and overhead are deducted such that if a DMC ends up with 3-7% net income, they are said to be doing well. Obviously, the DMC must be able to subtract cost of services sold (i.e. flow through expenses) in order to have anything resembling "margin".

### **The Legislative Process**

In January of 2007, Laurie Sprouse, CITE, CMP, DMCP, President of Ultimate Ventures and Sales & Marketing Chair of The DMC Network, LLC reached out to the Texas DMCs to inform them of the Margins tax issues. In March of that same year, the Texas Comptroller's office rolled out a letter draft of the sales tax rule on which they were working.

Under the auspices of ADME (Association of Destination Management Executives), a Texas Tax Task Force was created which was led by Sprouse. After a year's worth of conversations with the comptroller, it was determined that legislation was the only viable option for resolution of both tax issues.

In November of 2008, Sprouse interviewed multiple lobbyists, ultimately hiring Richard Evans and William Yarnell with Texas Lobby Solutions, Inc. to represent the Texas DMCs. She also worked to gain the support of the National Federation of Independent Business Texas, Texas Travel Industry Association, Texas Hotel & Lodging Association, Texas Restaurant Association, and Texas Association of Convention & Visitor Bureaus.

Senate Bill 818 and Senate Bill 1347 were filed by State Senator Leticia Van de Putte in the Senate, while House Bill 2583 (sales tax) and House Bill 3131 (margins tax) were filed by State Representative Will Hartnett in the House of Representatives. Both HB 2583 and HB 3131 were ultimately passed favorably by the House Ways and Means Committee due in large part to the testimony provided by Sprouse during the committee hearings. But, in a year when a record number of bills were filed, yet a record low number of bills passed, both bills died when time ran out before they could be heard in the House of Representatives. However, Texas Lobby Solutions worked its magic and (long, tumultuous

story made short) both bills ultimately gained passage (in the final hours of the final day of session) as an amendment to Senate Bill 636 thanks to Senator Kel Seliger and Representative Patrick Rose.

### **DMC factors that were communicated to legislators which helped bring passage**

DMCs are different from other meeting or event planning companies in Texas in that at least 80% of a DMC's clients come from outside of Texas as well as the fact that DMCs market and sell Texas as a meetings destination. In fact, no other private industry spends nearly as much of its own marketing budget as DMCs do (typically 1-3% of their gross revenue) actively marketing the destination of Texas all over the country (and the world), thus making DMCs more like a partner and private sales force for their local Convention & Visitor Bureaus.

There are approximately 20 DMCs in Texas, many of which are small, women-owned businesses. While the DMC industry is small, the impact it has on the Texas economy is significant. Texas DMCs provide nearly 1400 jobs and pay an estimated \$9 million in wages annually. DMC clients spend approximately \$500 million each year in Texas on travel, hotel, airfare, food and beverage, transportation, and meetings.

Thus, DMCs collectively spend more than \$500,000 per year marketing the state of Texas to help generate more than \$500 million annually in economic impact for Texas, the net state taxes of which far outweigh the fiscal note of both bills.

### **Outcome**

Due to the tremendous efforts of all involved, in a year when a record low number of state bills were passed, DMCs were the only industry to pass a "flow through" funds bill on the Margins tax although dozens were filed. DMCs are now the only service industry in Texas, other than general contractors, to be able to take the COGS/"flow through" deduction. In addition to avoiding the ongoing struggles and sales tax audits that DMCs in other states are currently facing, passing the Margins tax bill saves each Texas DMC in annual taxes an equivalent of 1% of their COGS (i.e. COGS of \$2.5 Million saves \$25,000 in annual taxes to the state). Further, Texas is now the first state to have a legal definition for a "Qualified Destination Management Company". Legislative precedent is now a possibility for other states.

### **Background Information:**

A Destination Management Company (DMC) is a professional services company possessing extensive local knowledge, expertise and resources specializing in the design and implementation of events, activities, tours, transportation and program logistics.

DMCs are instrumental to the Meetings and Conventions industry in Texas. DMCs regularly market the Texas destination to their Third Party clients (keeping them updated on what is new in the destination) as well as prepare extensive proposals to try to attract their corporate clients to bring their meetings to Texas.

### **About ADME:**

The Association of Destination Management Executives (ADME) is the only global non-profit association dedicated to increasing the professionalism and effectiveness of destination management through education, promotion of ethical practices, and availability of information to the meetings, convention, and incentive travel industries, as well as the general public.

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