

FREDERICK COUNTY, MARYLAND
Hotel Rental Tax Audit
Frederick, Maryland

PERFORMANCE AUDIT REPORT
For the period July 1, 2014 through June 30, 2016
Report #17-09

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INDEPENDENT AUDITORS' REPORT AND EXECUTIVE SUMMARY

Interagency Internal Audit Authority
Frederick County, Maryland

CliftonLarsonAllen LLP (CLA) was engaged by Frederick County, Maryland (the County) to conduct a performance audit of the hotel rental tax as required by County Ordinance No. 04-11-355, adopted July 2004. The purpose of this report is to provide findings and recommendations regarding this audit. Our audit scope covered the period July 1, 2014 through June 30, 2016. Our audit was conducted in accordance with *Governmental Auditing Standards* issued by the Comptroller General of the United States.

We found that the Frederick County Tourism Council complied with the County Ordinances and Memorandums of Understanding (MOU) with the County. The Tourism Council properly recorded hotel rental tax revenues, administrative expenses and debt service on the outstanding bonds in their general ledger. During our review of the Tourism Reinvestment in Promotion and Product Development (TRIPP) Program, we noted the Tourism Council has policies and procedures in place to evaluate grant applications for the determination of grant awards. Our testing of a sample of TRIPP grants found that all grants were awarded in accordance with internal policies and procedures, expenses associated with those grants were properly approved in accordance with program guidelines, matching funds were properly received, where applicable and grant transactions were properly recorded in the general ledger. In conclusion, there were no exceptions related to the TRIPP program testing.

During our review of the County's financial records, we found that the monthly hotel rental tax revenues received from the hotels were properly recorded in the County's general ledger. We noted several exceptions related to the calculation of the monthly hotel rental tax by the hotels, which are noted below. Our review of the monthly calculations of amounts due to the Tourism Council by the County's Accounting Department appeared accurate based on the revenues received by the County, the administrative rate charged by the County and the debt service requirements of the bonds outstanding.

Out of the nine hotels we visited during our audit, four of the hotels yielded no exceptions in the completion of the hotel rental tax report submitted to the County and our testing indicated that they were properly charging guests the 3% hotel rental tax in accordance with the County Ordinance. We found exceptions at five of the nine hotels, which included incorrectly reporting gross room rental receipts, improperly reporting receipts from non-transients and incorrectly completing the hotel rental tax report using the definition of a transient stay being a maximum 30 days instead of 90 days.

A summary of findings are as follows:

Finding #	Area	Finding
1	Transient Stay	The following hotels were reporting non-transients as those staying more than 30 instead of 90 consecutive nights – Hotel 1, Hotel 2, Hotel 3, and Hotel 4.
2	Hotel 1 – Gross Room Rental Receipts	Gross room rental receipts did not agree to supporting documentation provided by the hotel.
3	Hotel 2 – Receipts from Non-Transients	The hotel reported receipts from non-transients for two months when the amount should have been \$0.
4	Hotel 5 – Hotel Rental Tax Report	The hotel incorrectly completed the hotel rental tax report for February 2016.

The responses from the County's Finance Division are included after each finding in the findings, recommendations, and management's responses section.



CliftonLarsonAllen LLP

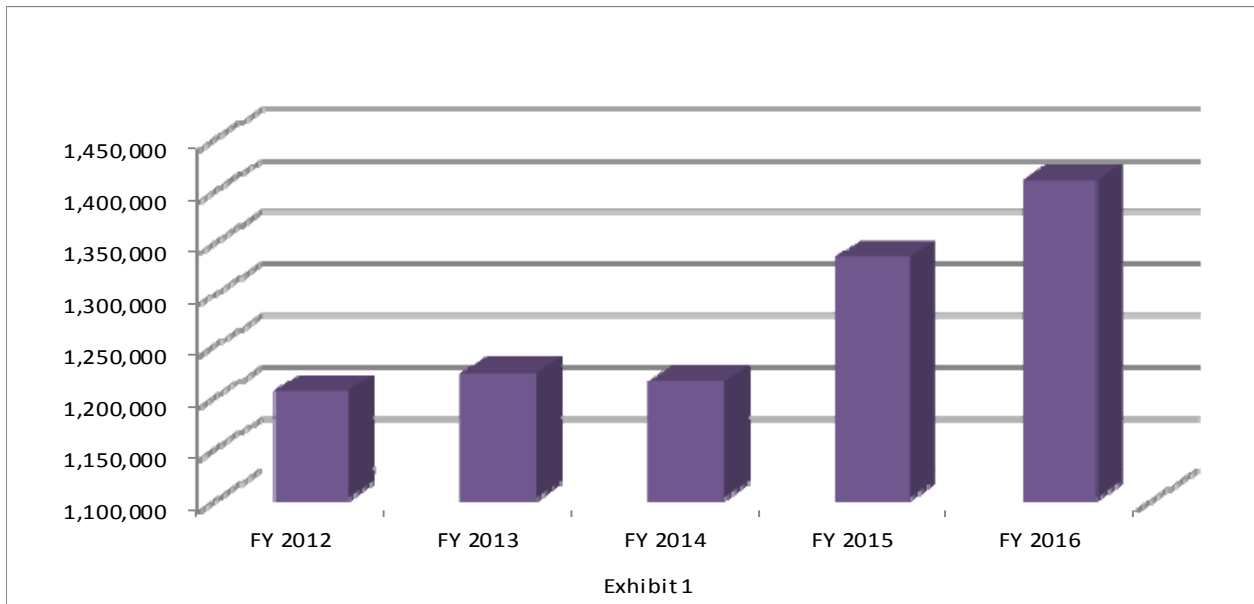
Baltimore, Maryland
October 30, 2017

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BACKGROUND

The Tourism Council of Frederick County, Inc. (Tourism Council) is a non-profit organization created to encourage, foster and stimulate tourism in Frederick County, Maryland (the County). The Tourism Council obtains and distributes information about tourism attractions in the County to promote cooperation and exchanges between business, organizations and tourist attractions both in and out of the County. The Tourism Council's source of funding is a mix of the Hotel Rental Tax, private/government grants, membership dues, advertising cooperatives, sales and miscellaneous income. The Hotel Rental Tax accounted for approximately 78.0% and 68.5% of the Tourism Council's revenue for FY 2016 and FY2015, respectively.

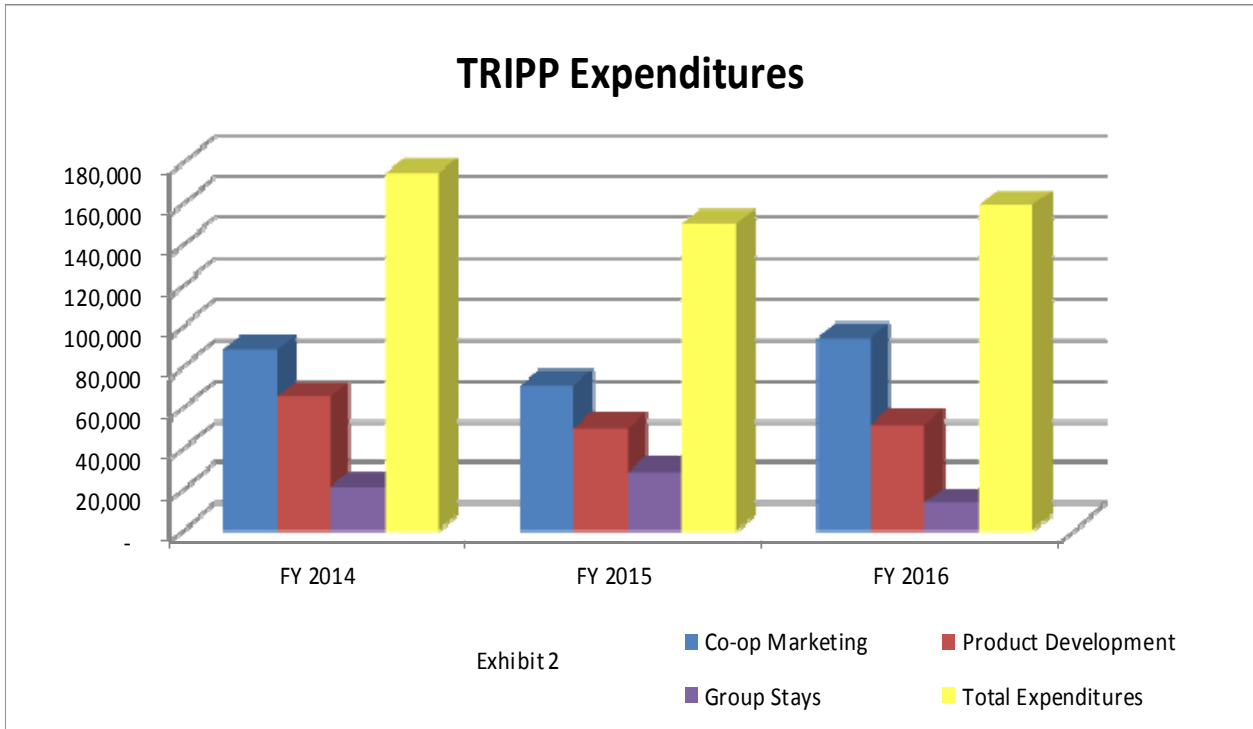
The hotel rental tax was established as a result of the Frederick County Government's Ordinance No. 04-11-355, adopted July 2004, to provide a source of funding to the Tourism Council. Previously, the Council was funded directly from the County's General Fund. The County collects a 3% hotel rental tax on transient stays not exceeding 90 consecutive days from all hotels located in Frederick County. County hotels submit the hotel rental tax collected from guests to the County Treasurer on a monthly basis. Refer to Exhibit 1 for hotel rental tax collected by the County for fiscal years 2012 through 2016. Council Bill No. 16-13 amended the hotel rental tax, effective October 29, 2016 to increase the hotel rental tax from 3% to 5%.



The Ordinance states that the Hotel Rental Tax revenue will first be used to pay for administrative costs incurred by the County in collecting the tax, which was 2.61% for fiscal years 2015 and 2016. The County also deducts debt service payments related to County bond issuances used to construct the Tourism Council's Visitors' Center. There are currently four bond issuances outstanding that are associated with the Tourism Council totaling approximately \$1,866,000 as of June 30, 2016. The balance of the Hotel Rental Tax revenue after administrative and debt service costs are deducted is then paid to the Tourism Council.

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The Tourism Council uses Hotel Tax Revenues forwarded by the County for general operating expenses and the Visitor's Center. Hotel Tax Revenues are also used to fund the Tourism Reinvestment in Promotion and Product Development (TRIPP) program in which non-profit organizations within the County may apply for funding to help promote tourism. These funds are available for advertising, trade show promotion, and development of local non-profit sites, attractions, events, and activities that attract tourists to the County. Refer to Exhibit 2 for TRIPP expenditures for fiscal years 2012 through 2016.



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OBJECTIVES, SCOPE AND METHODOLOGY

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS) established by the U.S. Government Accountability Office (GAO). Those 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 conclusion based on the audit objectives. Because of the inherent limitations, a performance audit made for the limited purposes of our review would not necessarily disclose all weaknesses related to the County's compliance.

The County is required to have an independent audit of the Hotel Rental Tax revenues at least every two years under Frederick County Government's Ordinance No. 04-11-355. The objective of this audit is to ensure that the Tourism Council is in compliance with all laws, regulations, and agreements related to the Hotel Rental Tax revenues and expenditures as well as testing the collection of and appropriate calculation of the hotel rental tax by the County. The scope of the audit covers the period July 1, 2014 through June 30, 2016.

As part of the hotel rental tax audit, we:

- Selected nine out of the twenty-seven hotels that remitted hotel rental tax revenues during the audit period and conducted onsite visits of those hotels. For each hotel that was tested, we:
 - Selected twelve out of the twenty-four months of the audit period and reviewed the supporting documentation used by the hotel to complete the hotel room rental tax report to ensure completeness and accuracy of the report. We also recalculated the hotel rental tax due to the County for accuracy.
 - Selected two guests per month for the twelve months tested and reviewed their hotel bill to ensure the tax was properly calculated and collected from the guest.
- Verified that the monthly tax collections reported by the individual hotels agreed with the amounts utilized by the County to calculate payments due to the Tourism Council.
- Obtained the County's calculation of payments due to the Tourism Council for the twenty-four months of the audit period and:
 - Verified the administrative fees charged by the County were in accordance with the Memorandum of Understanding (MOU) between the County and Tourism Council;
 - Recalculated the administrative fees charged by the County for accuracy; and
 - Verified the debt service amounts charged by the County agreed to the amortization schedules of the bonds issued by the County for the Tourism Council's Visitor's Center.
- Verified that the payments made by the County to the Tourism Council were accurate and agreed with the amounts recorded in the Tourism Council's financial ledgers. We traced payments received by the Tourism Council for twelve out of twenty-four months to the Tourism Council's bank account.

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- Verified that the Tourism Council properly recorded the debt payments and set aside the required minimum for the Visitor's Center each fiscal year in their general ledger.
- Gained an understanding of the Tourism Council's Tourism Reinvestment in Promotion and Product Development (TRIPP) Program and selected 20 out of 40 grants awarded during the audit period for testing to ensure program participants were eligible for the grant and funds were dispersed appropriately to those participants.

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FINDINGS, RECOMMENDATIONS AND MANAGEMENT'S RESPONSES

We identified several areas where exceptions to current policies and procedures were noted or procedures or controls could be improved. These items are discussed below and include our findings and recommendations, together with the County responses to our findings.

1. Transient Charge

Finding:

The County passed Ordinance No. 14-08-663, which amended the hotel rental tax, effective July 1, 2014, to extend the time period for which a transient charge is charged from a maximum of 30 days to a maximum of 90 days. However, we noted the following:

- Hotel 1 - we noted for three out of twelve months tested, the hotel was improperly completing the hotel rental tax report using the definition of a transient stay being a maximum 30 days instead of 90 days. This finding occurred throughout the audit period.
- Hotel 2 - we noted for four out of twelve months tested, the hotel was improperly completing the hotel rental tax report using the definition of a transient stay being a maximum of 30 days instead of 90 days. This finding occurred at the beginning of fiscal year 2015; however, we noted no similar findings after January 2015.
- Hotel 3 – we noted for one out of five months tested, the hotel was improperly completing the hotel rental tax report using the definition of a transient stay being a maximum of 30 days instead of 90 days. This finding occurred at the beginning of fiscal year 2015; however, we noted no similar findings after November 2015.
- Hotel 4 – we noted for seven out of twelve months tested, the hotel was improperly completing the hotel rental tax report using the definition of a transient stay being a maximum of 30 days instead of 90 days. This finding occurred throughout fiscal year 2015; however, we noted no similar findings after July 2015.

Recommendation:

We recommend the County or Tourism conduct training or communicate to all hotels any changes to the hotel rental tax laws and regulations prior to the effective date to ensure the hotels are aware of the changes in order to implement them in a timely manner. We also recommend the County reach out to these particular hotels to ensure they are currently charging taxes properly and make them aware of the error, if they have not already done so.

Management Response:

The County provides all hotels with a copy of the County's Hotel Tax Ordinance No. 14-08-663, which defines the applicable transient charge. The County also provides the hotels the room rental tax report that states the non-transient charge as greater than 90 days. The County and Tourism will review the hotel rental tax form and will include instructions to the form to provide better guidance. The estimated timeframe for completion is one year.

The Tourism Council is very willing to collaborate with the Finance Department on communication to hotels of any future changes to the hotel rental tax laws or regulations. Tourism appreciates the County's efforts to bring hotels into compliance when past changes have been missed by operators.

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2. Hotel 1 – Gross Room Rental Receipts

Finding:

Gross room rental receipts reported by the hotel did not agree to supporting documentation provided by the hotel for the months of December 2014, February 2015, June 2015, December 2015, April 2016 and June 2016. This resulted in an underpayment of the hotel rental tax of \$393.40.

Recommendation:

We recommend the County perform a risk based, cost effective analysis of the hotels in the County, which takes into account the size, the experience and knowledge of management company/owner, the volume of reservations and the average amount of tax paid to the County annually. The County should utilize this analysis to determine if increased oversight by the County would be beneficial to ensure the correct amount of tax is remitted monthly.

Management Response:

The County's Accounting Department does not have adequate resources to perform a risk based cost effective analysis. The County and Tourism will review the hotel rental tax form and will include instructions to the form to provide better guidance. The estimated timeframe for completion is one year.

3. Hotel 2 – Receipts from Non-Transients

Finding:

The hotel incorrectly reported room rental receipts from non-transients for the months of November 2016 and January 2016 when the amount should have been \$0. This resulted in an underpayment of the hotel rental tax of \$26.94.

Recommendation:

We recommend the County perform a risk based, cost effective analysis of the hotels in the County, which takes into account the size, the experience and knowledge of management company/owner, the volume of reservations and the average amount of tax paid to the County annually. The County should utilize this analysis to determine if increased oversight by the County would be beneficial to ensure the correct amount of tax is remitted monthly.

Management Response:

The County's Accounting Department does not have adequate resources to perform a risk based cost effective analysis. The County provides the hotels the room tax report that clearly states the non-transient charge is greater than 90 days. The County and Tourism will review the hotel rental tax form and will include instructions to the form to provide better guidance. The estimated timeframe for completion is one year.

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4. Hotel 5 - Hotel Rental Tax Reports

Finding:

The hotel incorrectly completed the February 2016 hotel rental tax report using the January 2016 gross room rental receipts and room rental receipts from non-transients. This resulted in an underpayment of the hotel rental tax of \$248.22.

Recommendation:

We recommend the County perform a risk based, cost effective analysis of the hotels in the County, which takes into account the size, the experience and knowledge of management company/owner, the volume of reservations and the average amount of tax paid to the County annually. The County should utilize this analysis to determine if increased oversight by the County would be beneficial to ensure the correct amount of tax is remitted monthly.

Management Response:

The County's Accounting Department does not have adequate resources to perform a risk based cost effective analysis. The County and Tourism will review the hotel tax form and include instructions to the form to provide better guidance. The estimated timeframe for completion is one year.

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APPENDIX A: TRANSIENT CHARGE

The County passed Bill No. 16-13 which changed the hotel rental tax rate, effective October 29, 2016, from 3% to 5%. While this amendment became effective after the audit period covered in this report, we were requested by the County and Tourism Council to inquire with the hotels selected for on-site visits and testing the following:

1. Whether the hotel was aware of the change in the hotel rental tax rate,
2. Whether the hotel was properly using the new hotel rental tax report, available on the County's website that reflected the change in the tax rate.

Results:

We noted that all nine of the hotels tested are currently using the 5% hotel tax rate.