

Internal Audit Report

DEPARTMENT OF FINANCE
ROOM RENTAL TAX
APRIL 2016

Office of the County Auditor





OFFICE OF THE COUNTY AUDITOR

Craig Glendenning, CPA
County Auditor

April 2016

The Honorable Members of the County Council
The Honorable Allan Kittleman, County Executive

Pursuant to Section 212 of the Howard County Charter and Council Resolution 22-1985, we have conducted an audit of the Room Rental Tax collected by the Department of Finance. The body of our report presents our findings and recommendations.

Our audit disclosed that room rental tax collections were not allocated in compliance with the County Code. In addition, we found that procedures and controls were not in place to verify that tax collections were proper and that all hotels subject to the tax were identified. We made recommendations which we believe will improve the internal controls over the program.

Our findings have been reviewed with the Chief Administrative Officer and we have included the Administration's responses. We wish to express our gratitude to the Department of Finance for the cooperation and assistance extended to us during the course of this engagement.

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County Auditor

EXECUTIVE SUMMARY

We conducted a performance audit of the room rental tax collected by the Department of Finance (Finance). The objectives of our audit were to:

1. Determine if adequate controls exist over the collection of room rental taxes.
2. Ensure the completeness and accuracy of tax collections.
3. Ensure that collections are allocated in accordance with the Howard County Code.

Conclusions

Regarding our first objective, we found that Finance had not taken steps to verify the propriety of tax payments, including amounts exempt from taxation as reported by hotels. In addition, Finance had no process in place to ensure that it identified all hotels subject to the tax.

For our second objective, our testing disclosed that Finance received and properly deposited tax receipts. Finance has taken actions to identify and follow up on delinquent taxpayers.

For our third objective, we found that the taxes collected were not allocated in compliance with the County Code.

BACKGROUND

The County Code imposes a room rental tax on hotel rooms. The Code defines a hotel as an establishment with sleeping accommodations for the public and with five or more rooms to rent. Starting in fiscal year 2012, the County raised the tax rate to seven percent with amounts collected over five percent allocated to the Howard County Tourism Council (Tourism) and the Howard County Economic Development Authority (EDA). Under the Code, Tourism receives two-thirds of the collections and EDA receives the remaining one-third.

Finance sends blank tax returns to all hotels (the form is also available on Finance's website) and the hotels submit completed returns and related payments to Finance's Cashier's Office for processing. Collections are deposited as general fund revenue into separate accounts for rental and Tourism/EDA collections. Finance maintains records to track payments and follow ups on delinquent taxpayers. Tourism and EDA receive appropriations as part of the annual budget process.

Table 1 below shows the tax collections from fiscal year 2012 to fiscal year 2015.

Table 1			
Room Rental Tax Collections			
Fiscal Years 2012 to 2015			
Fiscal Year	General Fund Share	Tourism/EDA Share	Total
2012	\$ 3,198,401	\$ 1,023,235	\$ 4,221,636
2013	3,142,271	1,262,293	4,404,564
2014	3,290,239	1,297,596	4,587,836
2015	3,538,424	1,415,351	4,953,775

Totals may not agree due to rounding.

Source: SAP

Note: The County began assessing the Tourism/EDA portion effective September 2011.

FINDINGS AND RECOMMENDATIONS

Finding 1

The County did not allocate the tax collected in compliance with the County Code.

The audit disclosed that the taxes collected were not consistently allocated in compliance with the requirements of the County Code. As noted previously, Tourism should receive two-thirds of all taxes collected over five percent. However, our analysis showed that, for fiscal years 2013 to 2015, Tourism received less than the mandated amount each year (see Table 2). The under allocation totaled \$113,784. Our analysis showed that EDA received general funds in excess of the annual tax allocation each year.

Fiscal Year	Appropriation	Mandated Allocation	Difference (underfunding)
2013	\$ 800,000	\$ 841,529	\$ (41,529)
2014	800,000	865,064	(65,064)
2015	936,376	943,567	(7,191)

Source: SAP, Approved Budget

Note: For fiscal year 2016, Tourism appropriation totaled \$1,075,800.

We recommend that Finance, in conjunction with the Budget Office, ensure that the room rental tax is allocated in compliance with the County Code. We also recommend that Finance reconcile actual tax collections at year-end to the appropriated amount and prepare a supplemental appropriation ordinance, if warranted, to increase Tourism's share of the collections to the amount required by the Code.

Administration's Response:

The Administration concurs with the finding. In FY 2016's Approved Budget, Finance and the Budget Office included an additional contribution to Tourism above the projected two-thirds required in order to start addressing the concern associated with this finding. The Offices are also working to propose a reconciliation contribution in FY 2017 to alleviate any current deficit between the actual room rental taxes received and what was budgeted based on the projection. Finance and the Budget Office will continue to work together to ensure that the room rental tax is allocated in compliance with the Code. Finance will reconcile the actual tax collections at year-end to the appropriation amount and recommend a solution, if necessary.

Finding 2

Finance did not have a formal process to ensure that it identified all hotels subject to the tax.

Finance did not have a formal process to ensure that it had identified all hotels subject to the room rental tax. Finance advised that it uses informal processes such as searching the internet to identify new properties subject to the tax. We obtained a listing of all hotels, motels and bed and breakfast inns licensed by the Department of Inspections, Licenses and Permits (DILP) and compared this list to records maintained by Finance. We found one motel licensed by DILP that was not included in Finance's records. This motel was not paying room rental taxes.

We recommend that Finance periodically compare its records with entities licensed by DILP and research any differences. We recommend that Finance contact the motel which is not paying room rental taxes, inform it of the requirement, and collect all back taxes owed.

Administration's Response:

The Administration concurs with the finding. Finance is in the process of developing an internal control to include a yearly comparison between their records and DILP's records to reconcile all hotels and motels that are subject to the tax. Finance will perform further investigation to determine if there is a cost benefit to expending staff time to calculate and collect the back taxes owed by the motel identified in this report.

Finding 3

Finance did not implement procedures to ensure the accuracy and propriety of amounts reported by taxpayers.

Finance did not ensure that amounts reported by taxpayers, including any exemptions allowed under the Code, were supported by records maintained by the hotels. The Code requires all taxpayers to keep records used to compile the monthly returns for two years. It further gives Finance the right to inspect those records.

We recommend that the Administration periodically review the records maintained by the hotels to support the tax returns and related tax payments.

Administration's Response:

The Administration concurs with this finding. The Administration is currently working internally to determine the most effective way to go about performing periodic reviews of the records maintained by the hotels and motels.

AUDIT SCOPE, OBJECTIVES AND METHODOLOGY

We conducted a performance audit of the room rental tax collected by the Department of Finance (Finance). We included tax collections and related documentation for the period from July 1, 2014 to January 31, 2016.

We conducted our audit in accordance with generally accepted government auditing standards prescribed by the Comptroller General of the United States. Those standards require us to 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 we obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of our audit were to:

1. Determine if adequate controls exist over the collection of room rental taxes.
2. Ensure the completeness and accuracy of tax collections.
3. Ensure that collections are allocated in accordance with the Howard County Code.

To accomplish our objectives, we met with Finance staff to document formal procedures and the internal controls over the tax collection process and related recordkeeping. We tested the propriety and accuracy of tax collections and follow up on delinquent accounts. We compared Finance records to records maintained by DILP to determine the completeness of Finance records. We also reviewed data from SAP. We performed various tests of the relevant data and determined that it was sufficiently reliable for the purposes the data was used for during the audit.

Finance management is responsible for establishing and maintaining effective internal control. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

We conducted our field work from February to March 2016. Finance's responses to our findings and recommendations are included in this report.

AUDIT TEAM

Edward L. Shulder, CPA
Deputy County Auditor

James J. Meyd, CPA
Senior Auditor