

Audit Report

HOTEL OCCUPANCY TAX FOLLOW-UP AUDIT

April 22, 2008

Office of the City Auditor
Austin, Texas

BACKGROUND

The City collects a hotel occupancy tax of nine percent on overnight stays costing more than \$2 in hotels, motels, tourist homes, tourist courts, lodging houses, inns, rooming houses, and bed and breakfasts. As of fiscal year (FY) 2007, there were 175 establishments collecting the tax within Austin's city limits. Hotel occupancy taxes have been steadily increasing over the past few years and in FY 2007 yielded over \$40 million in revenue. The recipients of these revenues include the Convention Center Department, the Venue Project, the Austin Convention and Visitors Bureau, and the Cultural Arts Program.

The Office of the City Auditor (OCA) conducted 75 hotel audits between FY 2005 and FY 2007. These audits were conducted in three different phases. Each of the three phases yielded significant revenue to the City of Austin. As shown in Exhibit 1 below, a total of \$875,746 in deficient hotel taxes was identified over a period of three fiscal years. Of this amount, \$795,272 has been collected as of March 2008.

EXHIBIT 1
Deficiencies Identified and Remitted for Previous Hotel Audits

Audit Year	Deficiency Identified	Amount Paid to City	Percentage Paid
2005	\$ 508,339	\$ 467,391	92%
2006	\$ 263,531	\$ 227,005	86%
2007	\$ 103,876	\$ 103,876	100%
Total	\$ 875,746	\$ 798,272	91%

SOURCE: Summary of prior audits (FY05 to FY07) by OCA.

Issues identified in previous audits conducted by our office include:

- Misapplication of 30-day exclusions;
- Misapplication of exemptions;
- Records retention issues;
- Reporting issues;
- Registration system control weaknesses; and
- Calculation mistakes.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

The purpose of this follow-up audit was to determine whether selected hotels audited between FY 2005 and FY 2007 have implemented changes that result in compliance with applicable regulations and accurate collection and remittance of hotel taxes.

Scope

The time period under review was FY 2005 to FY 2007. Within this time frame, 75 hotels were audited. Out of these 75 hotels, 60 (or 80 percent of hotels) did not remit accurate hotel taxes to the City of Austin. Our scope for this follow-up audit included 12 hotels, which corresponds to 20 percent of the 60 non-compliant hotels between FY 2005 and FY 2007. The scope of review for each hotel covered the time period from the last quarter reviewed in our prior audit through the last quarter of calendar year 2007.

Methodology

We selected hotels for follow-up review using the following criteria:

- the amount of hotel tax owed in prior audits;
- the extent of compliance issues identified in prior audits; and
- past and current revenue and exemption reporting.

In order to perform our work we used various methods including:

- Reviewing applicable laws and regulations to identify criteria for hotel taxes;
- Conducting interviews of selected hotel staff members to determine progress in implementing changes that result in compliance with applicable regulations; and
- Extracting and analyzing data from the selected hotels to determine if accurate exclusions and exemptions and gross sales/taxable income were reported and whether accurate hotel taxes were remitted to the City of Austin.

As part of our follow-up process, we sent advance notification to hotels, conducted on-site entrance and exit conferences with hotel management, and sent letters of compliance or deficiency to each hotel.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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 conclusions based on our audit objectives.

AUDIT RESULTS

When we conducted our follow-up work, many hotels still had compliance issues that resulted in deficiencies; however, system improvements by hotels resulted in lower deficiencies on average than in our original audits.

We completed follow-up audits of eleven hotels. We found that two hotels were fully compliant and had no tax deficiency, while the remaining nine hotels still had compliance issues that resulted in tax deficiencies totaling over \$200,000. However, several of the hotels reviewed had significantly improved their systems resulting in more appropriate collection and remittance of hotel taxes to the City.

While two hotels reviewed in follow-up were in full compliance with hotel tax requirements, nine hotels had recurring compliance issues resulting in at least \$212,000 due the City. We began twelve hotel follow-up audits and completed eleven of these. For the remaining audit, we required additional time to review documentation and expect to complete this audit in the next 30 days. From the eleven hotel audits completed, we identified two hotels that were fully in compliance with City ordinance and had no tax deficiency. The remaining nine hotels had deficiencies ranging from 3 percent to 60 percent of claimed tax exemptions not supported that resulted in \$212,530 in tax due the City, not including penalty and interest. Upon request, the Controller’s Office will review the hotel’s past payment and compliance history and may grant a waiver of penalty and interest if the deficiency is paid promptly.

**EXHIBIT 2
Deficiency and Tax Due By Hotel**

ID	Average Deficiency	Tax Due	Penalty & Interest	TOTAL
Hotel A	36%	\$ 105,653	\$ 20,732	\$ 126,385
Hotel B*	60%	\$ 76,932	\$ 13,588	\$ 90,520
Hotel C*	7%	\$ 8,821	\$ 1,971	\$ 10,792
Hotel D	11%	\$ 7,659	\$ 2,412	\$ 10,071
Hotel E	17%	\$ 5,451	\$ 730	\$ 6,181
Hotel F	4%	\$ 4,437	\$ 815	\$ 5,252
Hotel G	9%	\$ 2,335	\$ 364	\$ 2,700
Hotel H	6%	\$ 729	\$ 91	\$ 820
Hotel I	3%	\$ 513	\$ 83	\$ 596
Hotel J	0%		In full compliance	
Hotel K	0%		In full compliance	
Total	14%	\$ 212,530	\$ 40,786	\$ 253,317

* Hotel is still within the 10 day appeal period allowed by our audit process and may provide additional support to reduce their deficiency.

SOURCE: Summary of follow-up audits completed.

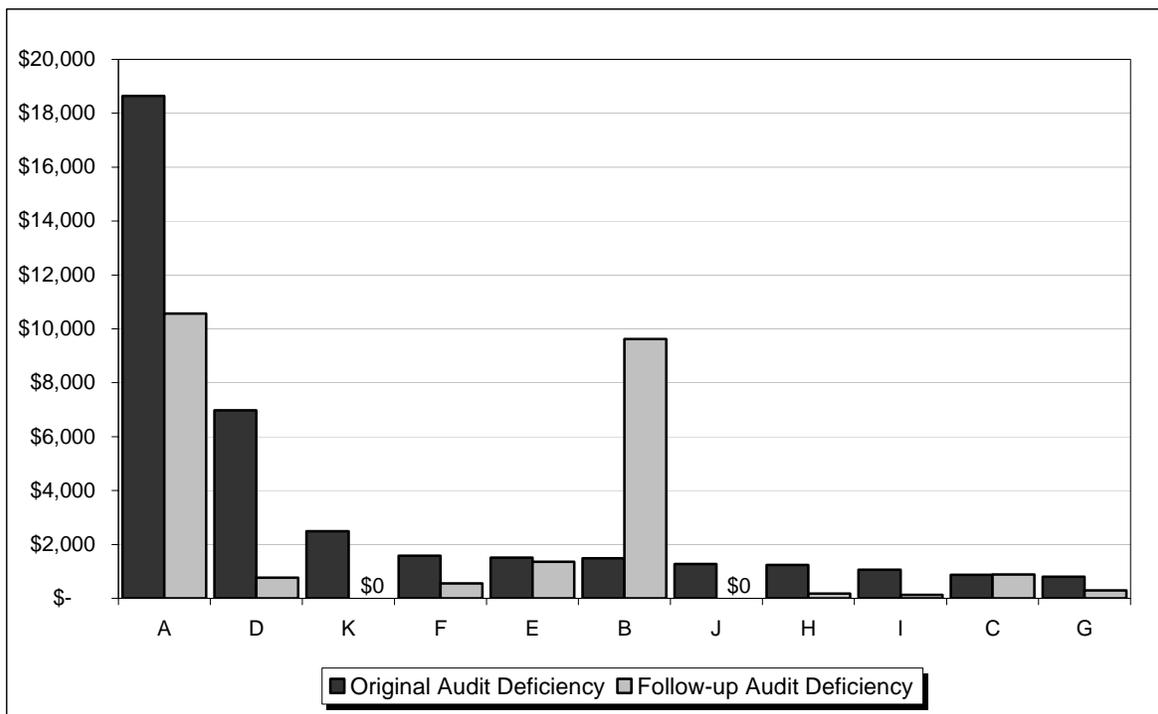
Recurrent compliance issues identified include:

- Misapplication of 30-day exclusions;
- Misapplication of exemptions; and
- Records retention issues.

In addition, we identified calculation mistakes in the quarterly reports submitted to the City at two hotels. These mistakes will result in the hotels submitting amended tax returns and remitting additional tax revenue to the City.

Though many hotels were not fully compliant during our follow-up audits, most hotels had improved their systems for supporting hotel tax exemptions which resulted in lower deficiencies than in our original audits. During the original audits the eleven hotels we reviewed had an average quarterly deficiency of \$3,449, while in our follow-up audits their average quarterly deficiency was \$2,214. Exhibit 2 compares the quarterly deficiencies identified in the original audits to the quarterly deficiencies found in our follow-up audits.

**EXHIBIT 3
Comparison of Average Quarterly Deficiencies
(Original Audit to Follow-up Audit)**



SOURCE: OCA analysis of original (FY05-FY07) and follow-up (FY08) average quarterly deficiencies.

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