

The Mayor & City Council Approval
of the City Auditor's Final Report

**City Council of the City of Galveston
Regular Meeting Agenda
Thursday October 24, 2013**

14. Action Items

D. Discuss and consider acceptance by City Council of the Final Audit Report on "**Hotel Occupancy Tax Administrative Audit**" dated January 2013.

CM Robb moved to approve
CM Banks second the motion

The Mayor & City Council **Unanimously Approved**

Office of the City Auditor
Glenn Bulgherini, CPA
City Auditor





**A Report to the Galveston
City Council**

Mayor
Lewis Rosen

Council Members

Cornelia Banks
Rusty Legg
Elizabeth Beeton
Norman Pappous
Terrilyn Tarlton
Marie Robb

Office of the City Auditor

City Auditor
Glenn Bulgherini
CPA
Auditor
Carrie Sumrall

Audit Report

Hotel Occupancy Tax Administrative Audit January 2013



Report Summary

The Office of the City Auditor found that the City of Galveston is in need of administrative procedures for processing Municipal Hotel Occupancy Tax (HOT tax). The City Auditor recommended using an additional database report to search for delinquent Hotels and charging late penalties. The City Auditor also suggested the exemption for municipal hotel occupancy taxes for religious, charitable or educational purposes should be repealed to be in compliance with Chapter 351 of the Texas Tax Code. Currently, the City of Galveston is forgoing approximately \$800,000 annually by allowing this non-compliant exemption.



**HOTEL OCCUPANCY TAX
ADMINISTRATIVE REPORT**

TABLE OF CONTENTS

EXECUTIVE SUMMARY.....	1
SCOPE.....	1
FIELDWORK.....	2
SUMMARY OF RESULTS.....	2
AUDITORS RECOMMENDATIONS.....	3
FINANCE DIRECTOR RESPONSE.....	3
CITY MANAGERS RESPONSE.....	4

AUDIT TEAM

Glenn Bulgherini, CPA, City Auditor
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**City of Galveston
HOT Tax Administrative Report
City Auditor Executive Summary**

The purpose of this report is to improve the City of Galveston's administrative procedures for processing Municipal Hotel Occupancy Tax (HOT tax). A Hotel Occupancy Tax Collection Report is remitted by each hotel within the Galveston city limits to the City of Galveston in the following month after collections (i.e. Collections for the Month of October 2012 are reported and remitted to the City of Galveston in November 2012). Chapter 351 of the Texas Tax Code defines hotels as any building or buildings in which the public may for a consideration of two dollars or more a day obtain sleeping accommodations. The term shall include hotels, motels, tourist homes, houses or courts, lodging houses, inns, rooming houses or other buildings where rooms are furnished for a consideration. The term hotels shall not be defined so as to include hospitals, sanitariums or nursing homes.

Scope

The scope of our procedures included interviews of key personnel in the Finance Department, Planning Department and Texas Hotel & Lodging Association. We interviewed the following:

- City of Galveston Finance Department's - Interim Finance Director, General Fund Accountant, and HOT Tax Clerk.
- City of Galveston Planning Department- Mechanical Inspector.
- President and CEO of the Texas Hotel & Lodging Association.
- The City of Galveston's Legal Department.

The scope of our procedures also included an analysis of the following documents:

- Chapter 351 of the Texas Tax Code: Municipal Hotel Occupancy Taxes.
- The HOT tax database spreadsheet from the Finance Department.
- The Accela database report from the Planning Department.

Our fieldwork was conducted from November 16, 2011 through January 3, 2013.

**City of Galveston
HOT Tax Administrative Report
City Auditor Executive Summary**

Fieldwork Performed

1. We compared the HOT tax database spreadsheet from the Finance Department to the Accela database report from the Planning Department by property addresses.
2. We reviewed the procedures used by the HOT Tax Clerk in the Finance Department to notify hoteliers of underpayment of HOT tax, overpayment of HOT tax, and penalties associated with the late payment of HOT tax or late filing of HOT tax returns.
3. We called the President and CEO of the Texas Hotel and Lodging Association to discuss Administrative fees for the City of Galveston's General Fund so that the City of Galveston may be reimbursed for the time spent on HOT tax collections and processing.
4. We inquired from the City of Galveston's Legal Department if there was any process which allowed the City of Galveston to be reimbursed for HOT tax audits performed by the City Auditor.
5. We reviewed Chapter 351 of the Texas Tax Code: Municipal Hotel Occupancy Taxes to ensure that the City of Galveston is in compliance.

Summary of Results

1. The HOT tax database spreadsheet from the Finance Department identifies 481 properties. The Acela database report identifies an estimated 4,300 properties for rent.
2. There are currently no procedures in place to assess penalties associated with the late payment HOT tax or late filing of HOT tax returns.
3. The President and CEO of Texas Hotel and Lodging Association informed us that Chapter 351 of the Texas Tax Code allows the City of Galveston to pass an ordinance allowing hoteliers to keep 1% of the HOT tax revenue collected. He instructed the City Auditor that if this is done that the Texas Hotel and Lodging Association will support an amendment to Chapter 351 of the Texas Tax Code allowing municipalities such as Galveston to maintain 1% of the HOT tax revenue collected as well.

**City of Galveston
HOT Tax Administrative Report
City Auditor Executive Summary**

4. The City of Galveston's Legal Department researched many hours and made a determination. The Legal Department's determination is that if the City Auditor recommends to the Municipal Court Judge that a HOT tax audit be performed based upon valid reasons then the cost of that HOT tax audit can be charged to the entity being audited for HOT tax.
5. The City Auditor reviewed Chapter 351 of the Texas Tax Code: Municipal Hotel Occupancy Taxes and determined that an exemption for municipal hotel occupancy taxes cannot be granted for religious, charitable, or educational purposes. The City of Galveston was currently allowing this exemption and forgoing approximately \$800,000 annually of HOT tax revenues.

City Auditor's Recommendations

We recommend the following:

1. The Accela database report from the City of Galveston's Planning Department should be used to update the HOT tax database spreadsheet used in the Finance Department.
2. Penalties should be assessed for the late payment of HOT tax or late filing of HOT tax returns and the exemption for municipal hotel occupancy taxes for religious, charitable, or educational purposes should be repealed to be in compliance with Chapter 351 of the Texas Tax Code. Currently, the City of Galveston is forgoing approximately \$800,000 annually by allowing this non-compliant exemption.
3. The City Manager analyzes and determines which method is appropriate for the City of Galveston to receive reimbursement for HOT tax audits performed by the City Auditor.

Finance Director's Response

1. The comparison of rental properties in the City's Accela Database would not necessarily equate to the same number of hotel occupancy taxpayers per se. Rental properties that are for long-term rentals, those longer than 30 days, would not be included in the list of rental units maintained by the finance department. An attempt to identify "apples to apples" would first need to be worked out.
2. While the finance department has historically collected the hotel occupancy tax collections from various entities on the Island, it has not always had the luxury of additional staff time to aggressively search out

**City of Galveston
HOT Tax Administrative Report
City Auditor Executive Summary**

and contact those who have not filed the monthly reports or remitted the tax. Finance staff has usually done a search to compare State filings to those filings with the City. Also, searches of vacation rentals by owner have been done. It frequently occurs that other home owners who do short term rentals report non-filers to the City. Many different efforts have been utilized in the past. Staff has a limited amount of time to devote to this one particular revenue source of the City with our limited resources.

3. The finance director does **not** recommend, to Council, that an ordinance be passed giving 1% of tax to the hoteliers.
4. The finance director believes that legal fees associated with the tax audits should be a reimbursable cost to the City. Further, because the extensive work done by the internal auditor, any costs that are allowable by law, to come back to the City's general fund, should be recouped in full.

City Manager's Response

1. The City is in need of a comprehensive approach to tax & fee collections. Typically the HOT funds collection is a separate and significant function in cities with successful enforcement. A HOT collection program will be created with a multi-departmental team, led by our Finance Director. In the absence of adequate staffing, funds should be budgeted for contracted elements of the strategy in the next fiscal year. City staff have approached the Parks Board for HOT funds to administer these activities for the budget next year.
2. Legislative changes to any Parks Board enabling or HOT legislation are not recommended. The local administrative functions dedicated to HOT at the City was requested of the Parks Board and it is hoped we will get some return to the City for those functions realized in this next or subsequent budget years.
3. Auditing fees should be charged to the worst violators.
4. City Attorney support to the Auditor is needed when the suspected violators bring in their attorneys. This is taking place. Continue high coordination between Auditor, Attorney, Finance Director, and City Manager.