DECEMBER 2013

AUDIT OF THE HOTEL OCCUPANCY TAX FOR THE PERIOD MARCH 1, 2012 TO MAY 31, 2013

STEFAN I. MYCHAJLIW
ERIE COUNTY COMPTROLLER

COUNTY OF ERIE
STEFAN I. MYCHAJLIW
COMPTROLLER

December 2013

Honorable Members
Erie County Legislature
92 Franklin Street, 4th Floor
Buffalo, New York 14202

Dear Honorable Members:

The Erie County Comptroller's Office has completed an audit of the Erie County (the "County") Hotel Room Occupancy Tax for the period March 1, 2012, through May 31, 2013.

The objectives of the audit were to evaluate the Hotel Tax Division's procedures and administration of the tax; determine that tax revenue is being maximized; and perform compliance testing on a sample of hotels/motels to verify the propriety of quarterly reports and occupancy tax remitted to the County.

This audit, performed in accordance with Generally Accepted Government Auditing Standards included such tests of records, inquiries, and analyses as considered necessary under the circumstances. No significant matters adversely affecting compliance with applicable laws, rules, and procedures came to our attention except as disclosed in this report.

Background

Pursuant to Erie County Local Law No. 12-1974, and Chapter 614 of the Laws of the State of New York, the "Erie County Hotel Room Occupancy Tax Law" took effect on December 1, 1974. Originally a 2% tax, amendments to the law in 1983 and 1987 raised the rate to 3% for establishments with 30 or fewer rooms; and 5% on establishments with more than 30 rooms. Lodging establishments must register with the County; obtain and prominently display a Certificate of Authority; and collect the tax from occupants. The Hotel Occupancy Tax is a liability of the business, as well as a personal liability of the operator of the establishment (including corporate officers).

Background, Continued:

Two types of occupants are exempt from the tax:

1) Permanent Residents. These are persons (broadly defined) that rent a room for 30 or more consecutive days.

2) Tax Exempt Organizations. These include governments and governmental agencies; religious and charitable organizations; and educational entities.

Returns are filed for fiscal quarters ending on the last day of February, May, August, and November; and are due within 20 days of the close of the quarter. If a return is filed late, or a payment is remitted after the due date, a 5% penalty is assessed immediately; plus interest of 1% per month commencing with the second month of the delinquency. A copy of a sample "Return of Tax on Occupancy of Hotel Rooms" is attached as Appendix A.

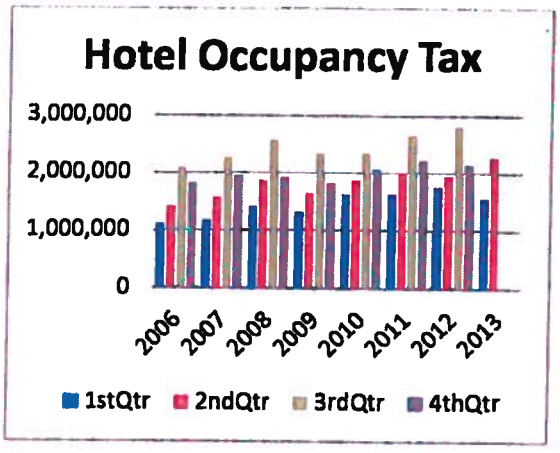
Completed returns in the custody of the County are required to remain secret. Local Law No. 12-1974, Section 2, Paragraph 21, Subdivision (a) states "... it shall be unlawful... to divulge in any manner the rents or other information related to the business of a taxpayer contained in any return." Because of this provision, this audit report does not disclose the revenue or exemptions of specific establishments.

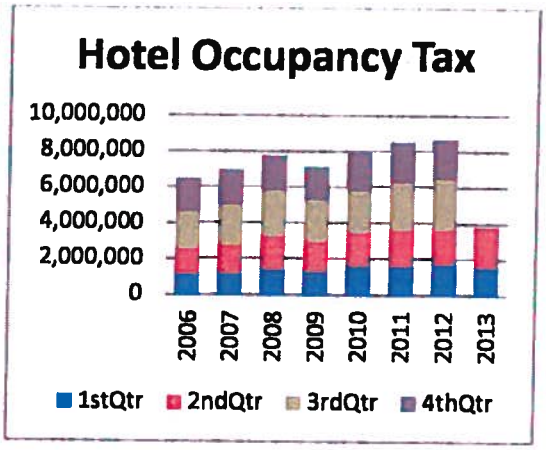
Nonetheless, it should be noted that Local Law No. 4-2007 amended this rule to allow the County to identify any establishment (including its principals) that fails to comply with the law and fails to timely remit their collected Hotel Occupancy Taxes to the County.

Overall, based upon the accrual basis of accounting, revenues to the County from the Hotel Occupancy Tax have been the following for recent calendar years:

2012	$8,861,557
2011	$8,556,982

Therefore, revenues for 2012 exceeded those of 2011 by 3.56%.





The first graph displays the seasonality of the hotel business in Erie County.
The second graph displays the total revenue figures since 2006.

FINDINGS RELATED TO ADMINISTRATION OF THE TAX

FINDING #1; COMPLETENESS OF DATABASE OF HOTEL/MOTEL OPERATORS:

The Hotel Tax Division monitors the media for announcements of new lodging establishments opening for business within the County. A letter will oftentimes be sent to a new business reminding them of the Hotel Occupancy Tax Law; and the requirement that they submit a Certificate of Registration.

We compared establishments listed in the Yellow Pages; listed at the Buffalo Niagara Convention and Visitors' Bureau; and those found online, to the "active" list maintained by the Hotel Tax Division.

The "active" list of hotel/motel operators proved to be complete. We did not discover any establishments advertising in the County that had failed to register with the County.

Currently, there are 136 active establishments in the County's database. Of these, 134 file tax returns quarterly; and 2 file annually (since their tax liability for twelve months doesn't exceed $250).

FINDING #2; CERTIFICATE OF REGISTRATION FORM:

In many instances, the legal name of an establishment is different than the "Doing Business As" name. Information for each establishment is first obtained by the County from the owner via a Certificate of Registration (see Appendix B). We found that this Certificate needs to be updated, since it currently:

1) Does not have separate lines differentiating the establishment's legal name from its DBA.
2) Does not ask for the number of rooms in the establishment, even though this information is necessary in assigning the proper tax rate of 3% or 5%.
3) Does not require the person completing the Certificate to sign it; only print their name.

Also, we found that the Registration form and its instructions are not readily accessible on the County's website.

RECOMMENDATION:

The Certificate of Registration form should be enhanced to include:

a) Separate lines for the legal name of the establishment, and the DBA of the business.
b) A line asking for the number of rooms.
c) A signature line for the person certifying that the information is true and complete.

RECOMMENDATION, Continued:

The business community needs easier access to the hotel occupancy tax forms and instructions. Online access should be supported by the Hotel Tax Division. We found that at www.erie.gov the Comptroller's Office webpage already has a tab for "Forms". The contents of this tab should be updated to include:

a) A blank Certificate of Registration
b) A blank Hotel Occupancy Tax Return for the current quarter
c) Appropriate instructions

FINDING #3; TIMELINESS OF ISSUANCE OF NEW CERTIFICATES OF AUTHORITY:

New hotel/motel operators commencing business in the County are timely submitting Certificates of Registration. Certificates of Authority (see Appendix C) are then being issued to the establishment by the Hotel Tax Division, but *not necessarily* in a timely fashion. Local Law No. 12-1974 Section 2, Paragraph (6) states that Certificates of Authority are to be issued by the County within 5 business days of receiving a completed Certificate of Registration. In several instances, we found that it took more than three weeks for a new registrant's information to be processed, including the preparation and mailing of a Certificate of Authority to the establishment. We found a lack of formal procedures for these steps.

RECOMMENDATION:

To better facilitate the entire process of recording new registrants, including the updating of files and the issuance of Certificates of Authority, a concise procedural checklist should be developed and utilized by the staff of the Hotel Tax Division. A completed checklist, specific to each establishment, should be included in the manila file of each new registrant; and should indicate the date that each procedure was executed, and by whom. At the time of the audit it was noted that a checklist was created and procedures were updated to reflect its use.

FINDING #4; THE TRACKING OF FILED RETURNS, AND THE FOLLOW-UP OF DELINQUENCIES:

To ensure that all active establishments are reminded to file their tax returns timely, blank tax forms along with pre-addressed remittance envelopes are mailed out by the Hotel Tax Division to every active establishment 10 days before the end of the fiscal quarter.

We found proper tracking of timely filed returns. These returns are reviewed for mathematical accuracy; the amount of the remittance is cross-referenced to the calculated tax; the discovery of any differences/discrepancies result in a letter being issued to the establishment; and, the appropriate line of a control list of the active establishments is checked off as "filed".

FINDING #4; THE TRACKING OF FILED RETURNS, AND THE FOLLOW-UP UP OF DELINQUENCIES Continued:

We found only one instance of an establishment (an annual filer) that had failed to file a tax return for the period being audited. All other registered establishments filed their tax returns in a timely fashion.

However, we found that six establishments (sometimes regularly) remitted less than 100% of the tax owed to the County. All of these instances were attributed to the respective establishment experiencing cash flow problems; and, in every instance, a series of installment payments were made. We found that the Hotel Tax Division properly assessed penalties and interest, month by month, on each of these delinquencies. In five of these six cases, we found that the establishment had paid-in-full the entire balance owed to the County as of September 19, 2013. Therefore, only one establishment is still in arrears; with an outstanding balance owed the County of approximately $42,000.

RECOMMENDATION:

The Hotel Tax Division should assess this last delinquency after payments postmarked through September 20, 2013 have been processed; and, if warranted, alert the County's Law Department that legal action may be necessary.

FINDINGS RELATED TO FIELD AUDITS

Our audit examined a sample of twelve establishments ranging in size from large hotels to small motels and Bed and Breakfast inns. Eight of these establishments have more than thirty rooms and, therefore, are subject to the 5% tax rate. The smaller establishments are subject to the 3% tax rate. Our examination included the verification of a sample of daily receipts to daily or monthly journal summaries; and the agreement of those summaries to one or more quarterly tax returns in the audit period. We tested exemptions reported to the supporting documentation. Also, we verified that Certificates of Authority were prominently displayed.

FINDING #1, PROPERLY POSTED CERTIFICATES OF AUTHORITY:

Of our sample, nine establishments had their Certificate of Authority properly posted, either near the front desk or in in a public hallway.

For one establishment, the Certificate was found to be framed, but kept inside a manager's office. The manager promptly relocated the Certificate so that it was prominently displayed.

Two establishments claimed that they had never received through the mail a validated Certificate of Authority. One establishment agreed to immediately complete and submit to the field auditors a new Certificate of Registration so that a new Certificate of Authority could be issued as soon as possible.

FINDINGS RELATED TO FIELD AUDITS, Continued

We found that the establishments examined in this audit have accurately reported their gross and net taxable room revenues, except for the following:

FINDING #2; UNDERPAYING OR OVERPAYING QUARTERLY TAXES:

For eight establishments, remittances to the County were *slightly* more than what had been charged to their customers. These occurrences were attributed to minor math errors; rounding of figures; and, in limited cases, the decision to remit a tax that *should have* been charged to a customer, but inadvertently wasn't. These were fairly small amounts, totaling less than $100.

For one establishment, a tax accountant for a Franchisor was blatantly careless in preparing one recently filed quarterly return, and consequently overpaid the County $3,223. The establishment has not filed an amended return as of this writing.

For another establishment, remittances to the County were incorrectly reduced for twelve consecutive quarters because the preparer of the tax return (the owner) mistakenly reported exempt revenues for permanent residents in two places; line 2 "Non-Taxable Room Rentals supported by an Exemption Certificate", and line 3 "Non-Taxable Room Rentals for Stays of 30 Days or More by a Guest". The total tax underpaid the County is $2,678.

Pursuant to Erie County Local Law No. 12-1974, confidentiality of hotels' financial information prevents the Comptroller's Office from naming the establishment in question in this report.

RECOMMENDATION:

The Hotel Tax Division should immediately issue an assessment of additional tax due, plus penalty and interest, to the establishment that filed inaccurate returns.

FINDING #3; CHARGING GUESTS THE WRONG RATE OF TAX:

One establishment had been allowed to lower its tax rate from 5% to 3% on March 1, 2009, due to a downsizing of the establishment's accommodations. It had converted rooms and suites into residential living spaces (ie. studio and one bedroom apartments). The establishment *never* updated its software, and consequently, has continued to charge its guests a 5% occupancy tax, even though the establishment was remitting to the County the appropriate 3%. The 2% difference, which was retained by the establishment over the course of 17 quarters, amounted to $13,358.

Because of the Comptroller's Office identifying this item, this hotel operator has updated their software to reflect the proper tax rate and customers will no longer be improperly charged.

AUDITORS' NOTES: ISSUES THAT WE ENCOUNTERED THAT MAY BE CAUSING DIMINISHED TAX REVENUES

ISSUE #1, CORPORATE CUSTOMERS GRANTED "PERMANENT RESIDENT" STATUS:

Local Law No. 12-1974 Section 2, Paragraph (1), Subdivisions (a) – (e) define a "person" (for sake of who an "occupant" is) to include a corporation that pays for the right to use a room.

"Persons" that pay for the right to a room for 30 consecutive days (or more) are deemed "permanent residents", and are, by law, not subject to the tax. The only exception is when such a "person" is a corporation and gets *reimbursed* by its employees, clients, or customers (any portion of) the cost of the room; in which case, the room rental is subject to the hotel occupancy tax.

Certain companies in the transportation industry (airlines, passenger trains, touring buses, etc.) oftentimes contract out a base number of rooms at a specific establishment for an extended period of time to accommodate their pilots, crews, or drivers, who may need to stay overnight during the course of their job assignments. Even though any one such employee might stay overnight in a given establishment only a handful of times per month, by virtue of their employer being treated as the person renting the room, the stay is treated as exempt from the hotel occupancy tax.

Only if "permanent resident" status were more narrowly defined by the law to apply *solely* to individuals would certain corporations that are currently (to some degree) escaping the hotel occupancy tax be held liable for the tax to a greater degree.

ISSUE #2, TAXES CHARGED BY THIRD-PARTY ONLINE BOOKING AGENCIES:

The hotel occupancy tax charged to customers booking their reservation online *may not* get remitted in its entirety to the County.

This finding is not applicable when a customer uses Franchisor websites such as HolidayInn.com, RedRoof.com, Hyatt.com, and ComfortInn.com.

Third-party online booking agencies are sometimes referred to as room remarketers ("RR"). These include Expedia.com, Priceline.com, Hotels.com and the like, which enter into agreements with specific establishments (or their brand) that allow the RR to pay the hotel a lower rate than the rate the RR charges the retail customer.

We found instances in which the hotel treats the RR as the "customer" and, accordingly, charges the RR the occupancy tax (and NYS sales tax) on the discounted/contracted price. It is this discounted tax that gets remitted by the hotel to the County with its quarterly tax return. Nonetheless, on the day the reservation is booked online, the retail customer is charged the hotel occupancy tax based on the higher price that they are paying the RR.

ISSUE #2, TAXES CHARGED BY THIRD-PARTY ONLINE BOOKING AGENCIES, Continued:

For example, a customer is charged online by an RR a $5 occupancy tax on a $100 room rental. At the conclusion of the customer's stay, the RR is charged a $4 occupancy tax based upon a discounted room charge of, say, $80. Only the $4 gets remitted to the County.

As more and more customers use online booking agencies, the financial implication of this issue will, accordingly, increase.

Presently, such room remarketers are not filing quarterly tax returns with the County. They appear to be charging the hotel occupancy tax *even though* they have not applied for, nor been issued, a Certificate of Authority.

This is a nationwide issue, and has been litigated extensively. Resolved cases, for the most part, have favored the RR, finding that they cannot be considered "operators" of hotels/motels; and that bed tax liabilities cannot be broadly extended to include the commissions they charge. Washington D.C., New York City, and municipalities in Illinois, South Carolina, and Texas have had some success in collecting bed taxes from such RRs. The status of local government litigation (state by state) against online travel companies as of March, 2012, (per the Tax Foundation) is attached (Appendix F).

RECOMMENDATION:

Depending on the outcome of pending litigation, the County could receive additional revenue, we recommend that the County's Law Department continue to monitor these matters and their outcomes, and notify the Legislature should any viable legal options become available to the County.

EXIT CONFERENCE:

An exit conference was held on December 9, 2013, with the staff the Hotel Occupancy Tax Division. They concurred with the findings and recommendations within this report, and have taken all appropriate corrective actions.

Sincerely,

Stefan I. Mychajliw
ERIE COUNTY COMPTROLLER

cc: Hon. Mark C. Poloncarz, Erie County Executive
Robert Keating, Director of Budget, Management and Finance
Michael A. Siragusa, Erie County Attorney
James A. Sampson, Chairman, Erie County Fiscal Stability Authority

APPENDIX A

County of Erie – State of New York

RETURN OF TAX ON OCCUPANCY OF HOTEL ROOMS

(Pursuant to Chapter 614 of the Laws of the State of New York)

Due by SEPTEMBER 20, 2013
For the Period JUNE 1, 2013 – AUGUST 31, 2013

EIN _____

Hotel/Motel Address:

Type of Establishment:

Hotel ____
Motel ____
Apartment Hotel ____
Lodging House ____
Other (describe) _____

(Please correct any errors on the above)

Business Activity:
Number of rooms_____
If Final Return, check here ____

Date Business Started _____
Reason for Final _____
Sold To _____
Other _____

Computation of Tax:

1 Gross Room Rentals ..... $ _____

2 Less: Non-Taxable Room Rentals supported by an Exemption Certificate $ _____

3 Less: Rental for Stays of 30 Days or More by a Guest ..... $ _____

4 Net Taxable Room Rentals (Line 1 Minus Line 2 Minus Line 3) ..... $ _____

5 Tax Due _____ % of (Line 4) ..... $ _____

6 Penalty (5% of Line 5 due the first month of delay after the due date) ..... $ _____

7 Interest (1% of line 5 for each month of delay excepting the first month of delay after the due date) ... $ _____

8 Total Due ..... $ _____

This return must be filed with your remittance in full for the amount of the tax within 20 days after the period covered by the return to avoid imposition of penalties. Make remittance payable to "Erie County Comptroller". Please mail your return to ERIE COUNTY COMPTROLLER, 95 FRANKLIN ST, ROOM 1100,BUFFALO NY, 14202.

Certificate of Taxpayer:
I hereby certify that this report, including any schedules, is to the best of my knowledge and belief a true and complete return.

FOR OFFICE USE ONLY

_____
Signature (Agent, Officer of Corp., Etc.)

_____
Print Name *Date*

_____
Print Title *Telephone No.*

APPENDIX B

ERIE COUNTY COMPTROLLER'S OFFICE
HOTEL TAX DIVISION

Erie County Office Building•95 Franklin Street• Room 1100•Buffalo, NY 14202•(716)858-8330

CERTIFICATE OF REGISTRATION
and Application for Certificate of Authority to Collect Hotel Room Occupancy Tax

Federal Employer Identification No.

ALL QUESTIONS MUST BE ANSWERED
PLEASE PRINT OR TYPE

1. Business Name: _____ Phone: _____
(Individual, Trade Name or Corporate Name)

2. Mailing Address: _____
(Street) (City) (State) (Zip)

3. Location of Business: _____
(Street) (City) (State) (Zip)

4. List Below Name and Home Address of Individual, Partners or Principal Officers (If Corp.)

NAME	HOME ADDRESS	TITLE

5. Type of Establishment Hotel ☐ Motel ☐ Other _____

6. Type of Ownership Individual ☐ Partnership ☐ Corporation ☐

7. Date started in business in Erie County: _____

8. If acquired from former owner:
Name under which operated _____
Registration number _____

9. How many places of business (or branches) does the applicant conduct in Erie County? _____
(List each Location and Certificate Number on Reverse Side)

I hereby certify that the statements made herein have been examined by me, and are to the best of my knowledge and belief, true and complete.

Date _____, _____ Name: _____
Title: _____
Owner, Partner, Corporate Officer

OFFICE USE ONLY

(See reverse side)

CF 39(7/95)

REGISTRATION

The Legislature of the County of Erie has provided by local law as follows:

Every hotel operator shall file with the Commissioner of Finance a certificate of registration in a form prescribed by him. The Commissioner shall promptly thereafter issue without charge to each hotel operator a certificate evidencing the authority of such operator to collect the tax from the occupants and duplicates thereof for each additional place of business of such operator. Each certificate or duplicate shall state the place of business to which it is applicable.

PENALTIES

Any hotel operator willfully failing to file a registration certificate or surrender the certificate of authority as required**** or assigning or transferring such certificate of authority, shall be liable to the penalties provided by law.

SCHEDULE OF LOCATIONS

Trade Name	Location	Certificate Number

APPENDIX C

CERTIFICATE OF AUTHORITY

COUNTY OF ERIE – COMPTROLLER'S OFFICE – HOTEL TAX DIVISION

Identification Number

(Use this number on all returns and correspondence)

Validation

MAY 31, 2013

Business Name

DBA

Address **MAIN STREET**

BUFFALO, NEW YORK 14202

is authorized to collect Hotel Occupancy Tax under Local Law Number 12 pursuant to Chapter Number 614 of the Laws of 1974 of the State of New York. This certificate must be prominently displayed in your place of business.

APPENDIX D

Status of Local Government Litigation Against Online Travel Companies as of March 2012

State	Litigation?	Disposition
Alabama	X	OTC Services not taxable under hotel tax
Alaska		
Arizona		
Arkansas	X	Government failed to exhaust administrative remedies
California	X	OTC Services not taxable under hotel tax
Colorado		
Connecticut		
Delaware		
Florida	X	OTC Services not taxable under hotel tax
Georgia	X	OTC Services not taxable under hotel tax
Hawaii	X	Case Pending
Idaho		
Illinois	X	OTC Services not taxable under hotel tax
Indiana	X	Government failed to exhaust administrative remedies
Iowa		
Kansas		
Kentucky	X	OTC Services not taxable under hotel tax
Louisiana		
Maine		
Maryland	X	Case Pending
Massachusetts		
Michigan	X	Case Pending
Minnesota		
Mississippi		
Missouri	X	OTC Services not taxable under hotel tax
Montana	X	Case Pending
Nebraska		
Nevada		
New Hampshire		
New Jersey	X	Government lacked standing to pursue claim
New Mexico	X	OTC Services not taxable under hotel tax
New York	X	OTC Services not taxable under hotel tax
North Carolina	X	OTC Services not taxable under hotel tax
North Dakota		
Ohio	X	OTC Services not taxable under hotel tax
Oklahoma	X	OTC Services not taxable under hotel tax
Oregon		
Pennsylvania	X	OTC Services not taxable under hotel tax. Another case pending
Rhode Island		
South Carolina	X	OTC Services not taxable under hotel tax
South Dakota		
Tennessee	X	OTC Services not taxable under hotel tax
Texas	X	In two cases, OTC Services not taxable under hotel tax. In one case, OTC Services taxable
Utah		

APPENDIX D

Vermont		
Viginia		
Washington	X	Case voluntarily dismissed
West Virginia		
Wisconsin	X	Case dismissed
Wyoming		
District of Columbia	X	OTC Services taxable
Source: Tax Foundation Review of Litigation		