

Audit Report Highlights

Lodging Tax

December 2023

Approx. Amount of Lodging Tax Revenue¹ = \$32 million

County Annual Budget² = \$1.4 billion

Why DIA Did This Audit



An audit was conducted to assess the adequacy, completeness, and accuracy of the Hotel/Motel (AKA Lodging) tax processes from registration to disbursal and the usage of funds. The audit was approved as part of the 2023 Audit Plan. Lodging taxes posed an area of higher risk due to frequency of payments, amount of tax collected, and volume of lodging establishments located in the County. The audit period under review was January 1, 2022 through June 30, 2023.

What DIA Found

The County does a good job managing the Lodging tax (AKA Bed Tax) collection process. However, DIA did note internal control weaknesses or areas of potential process improvement related to:

- Incomplete or outdated Policies and Procedures.
- Monitoring to ensure completeness of taxpayer registration.
- Lack of approval of monthly reconciliations performed by the Lodging Tax Office.
- Governance oversight relating to the use of Bed Tax monies.
- Lack of review of journal entries for the transfer of monies.
- Increased compliance assurance through increased audit coverage.

Recommendations have been rated by priority: High, Moderate, Low, or Business Process Improvement.

The report contains 9 recommendations:

0 High – 30 days to complete

5 Moderate – 90 days to complete

2 Low – 180 days to complete

2 Process Improvements- No action required

¹ Based on recorded 2022 Lodging Tax revenue within Lawson.

² The County Annual Budget includes operating appropriations from all County funds.

Audit Report Highlights

Lodging Tax

December 2023

Background

The Lodging Tax Office is charged with the duties of collecting Bed Tax and ensuring those collections are accurate. There is a 6.5% Bed Tax assessed on transient guests (persons occupying a room for dwelling/sleeping for less than 30 consecutive days) staying in Cuyahoga County. This is based on ORC 5739.09 as well as County Code Section 717, 724, & 726. The County's Bed Tax is used for Capital Improvements and funding for Destination Cleveland, The Rock & Roll Hall of Fame, Sports fund, and The Global Center for Health Innovation (Medical Mart).

The Lodging Tax Office uses Gov OS MUNIRevs for taxpayer registration and tax/penalties payments. MUNIRevs has two modules, the Compliance module and the Bed Tax module.

The Lodging Tax Office conducts audits of the registered taxpayers to ensure that their filings and payments are accurate and in compliance with regulations.



What DIA Recommended

DIA provided Lodging Tax Office management with recommendations for improving internal controls. We provided these recommendations during fieldwork to lessen potential risks related to Lodging revenue. Doing so during the course of fieldwork rather than at audit completion allows the department a chance to remedy identified issues immediately and have no surprises when the report is received.

Lodging Tax Office is working to address the issues noted in this report. Based on their responses, we believe corrective action will be taken to mitigate the risks identified. Management responses follow each recommendation in the report. Recommendations we made for management included:

- Continue their plan to use the Compliance module of MUNIRevs to search for establishments that may be subject to the Bed Tax.
- Review and approval of the monthly reconciliations.
- Update and add key procedures in Policies and Procedures Manuals.
- Follow or revise the applicable language in agreements and Policies and Procedures Manuals as it relates to the oversight of reporting and usage of Bed Tax monies.
- Review journal entry support documentations prior to the submission into Lawson by an employee that is not preparing the journal entries to ensure money is being transferred in the correct amount to the correct accounting units.
- Develop plans to increase audit rates.

Internal Audit would like to express our appreciation for the cooperation and assistance received from the Lodging Tax Office during this audit. The strides made help improve the County's efficiency and accountability.

Internal Audit Report

Cuyahoga County, Ohio
Department of Internal Auditing

**Lodging Tax Audit
Fiscal Office
January 1, 2022 – June 30, 2023**

**Director of Internal Auditing: Monica Houston, CPA,
CGMA, CFE, CIDA**

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Release Date 01/12/2024



**CUYAHOGA COUNTY
DEPARTMENT OF INTERNAL AUDITING**

**INTERNAL AUDIT REPORT
Lodging Tax
Cover Letter**

December 14, 2023

To: Fiscal Officer Mike Chambers and current management of the Fiscal Office,

The Department of Internal Auditing (DIA) has conducted an audit of the Lodging Tax Office for the period January 1, 2022 to June 30, 2023. Our main objective was to assess the adequacy, completeness, and accuracy of the Lodging tax (a.k.a. Bed Tax) processes from registration to disbursement and usage of funds. This included processes related to monitoring of tax filings, payments, reconciliations, proper disbursement of monies collected, oversight of monies usage after disbursement, and audits of taxpayers.

To accomplish our objectives DIA conducted interviews with management and staff regarding procedures that the Lodging Tax Office performs relative to the County Bed Tax. The adequacy of tax returns, reconciliations performed, disbursement of monies collected, and audit functions were assessed by a sample of transactions.

Our audit procedures disclosed internal control weaknesses and areas of potential process improvement related to:

- Incomplete or outdated Policies and Procedures.
- Lack of approval on monthly reconciliations.
- Monitoring to ensure completeness of taxpayer registration.
- Governance oversight relating to the use of Bed Tax monies.
- Lack of review of journal entries for the transfer of monies.
- Increased compliance assurance through increased audit coverage.

We are confident corrective action has been taken or will be taken to mitigate the risks identified in this audit report.

We conducted this audit in accordance with the International Standards for the Professional Practice of Internal Auditing. 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.

Because of the inherent limitations of internal controls, errors or irregularities may occur and not be detected. Also, projection of any current evaluation of the internal control structure to future periods is subject to the risk that procedures may become inadequate due to changes in conditions, or that the degree of compliance with the procedures may weaken.

DIA would like to express our appreciation to Fiscal Office staff and management, most notably the Lodging Tax Office, for their courtesy and cooperation during this audit. A draft report was provided to Fiscal Office management for review. Management responses are included within the audit report.

Respectfully,

A handwritten signature in blue ink that reads "Monica Houston". The signature is written in a cursive, flowing style.

Monica Houston, CPA, CGMA, CFE, CIDA
Director of Internal Auditing

Cc: Cuyahoga County Council
Erik Janas, Chief of Staff
Katie Gallagher, Chief of Operations and Innovation
Richard D. Manaloff, Law Director
Michael C. O'Malley, Cuyahoga County Prosecutor

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Glossary

Gov OS-MUNIREvs	Software the County uses for taxpayer registration, tax filing, recording tax payments, audit results, and compliance. It may also be used to search for unregistered vendors. The software is an industry-leading business tax, licensing, and compliance solution for local governments that is developed and owned by a private entity
Transient	Occupying a room or rooms for dwelling, lodging, or sleeping accommodations for less than thirty (30) consecutive days.
Bed Tax/Lodging Tax	6.5 % tax on lodging for transient guests.
Destination Cleveland	The Convention and Visitors Bureau of Greater Cleveland.
Global Center for Health Innovation	Formerly Medical Mart. A showcase for healthcare innovation and products. (It is being developed into an expansion of the Huntington Convention Center).
Lawson	County financial system that records revenues and expenditures.

Report Details

Purpose

The purpose of this audit was to conduct a comprehensive examination of Hotel/Motel (Lodging Tax) processes.

The Audit Committee approved DIA's 2023 audit plan to include an audit of the Lodging Tax processes. Lodging Tax processes were identified as an area of higher risk on the Annual Risk Assessment due to the number of lodging establishments, the self-reporting nature of taxpayer registration, and high amount of tax collected on an annual basis.

The audit included review and evaluation of procedures, practices and controls as deemed necessary.

Audit Objectives

The objective of this audit was to assess the adequacy, completeness, and accuracy of the Hotel/Motel (AKA Lodging) tax processes from registration to disbursal and usage of funds.

Scope

To accomplish our objectives, we focused on processes related to the administration, collection, disbursal, oversight, compliance, and audit of the Bed Tax for the audit period January 1, 2022 – June 30, 2023. Additionally, tests of transactions and controls were performed to determine if controls were operating effectively.

Methodology

DIA made inquiries to gain a general understanding of the processes utilized by Lodging Tax Office in the collection, recording, and disbursal of lodging tax collected, as well as the process used to audit or review tax remittances.

DIA reviewed a sample of the tax returns submitted through the MUNIRevs system to ensure that the system was properly calculating taxes based on inputs. DIA also reviewed a sample of reconciliations performed between MUNIRevs, the bank, and Lawson. DIA performed comparisons to ensure that all registered taxpayers had filed

a tax return or were noted as being a late filer with penalty assessed for the sampled reconciliation.

DIA reviewed a sample of completed audits to ensure that proper supporting documentation existed for the audit findings noted.

DIA reviewed all applicable agreements and laws relating to the Bed Tax to ensure that any noted reporting requirements for the funds were followed and that the County was reasonably ensuring that tax monies were used for intended purposes. This also included a review of the agreement between the County and Airbnb, and comparison of Airbnb remitted amounts to taxpayer monthly tax filings.

Audit Procedures

Although every audit conducted by the DIA is unique, the audit process for most engagements consists of the following three phases:

- Planning
- Fieldwork
- Reporting

The planning phase of an engagement entails gathering sufficient understanding of the area being audited to identify and reduce key audit risks to an appropriate level. The DIA must document and develop a plan for each audit engagement, including the engagement's objectives, scope, timing, and resource allocation.

The fieldwork phase of an engagement entails executing the audit steps. This usually includes testing, reviewing, and analyzing data along with interviewing the appropriate personnel. Each audit has unique aspects and therefore the audit fieldwork and analysis performed on each audit segment should be customized for that assignment. See Methodology for a summary of fieldwork performed.

The DIA prepares written reports to communicate the results of each engagement. The format and nature of the report can vary depending on user needs and the type of engagement. Additionally, the DIA requires all engagements to receive an appropriate level of supervisory review and quality control as required by professional standards. At the time of report release, DIA resources required to complete the audit were as follows:

Stages		Actual Hours
Planning		157
Fieldwork		228
Reporting:		127
Review	28	
Draft Report	99	
Totals		512

Background

The Lodging Tax Office is responsible for the collection and disbursement of the Cuyahoga County excise tax on lodging of transient guests. There are currently 3 FTE's within the Lodging Tax Office. Every establishment (hotel, motel, bed and breakfast, Airbnb rental, house rental, room rental etc.) kept, used, maintained, advertised, or held out to the public to be used as a lodging establishment where sleeping accommodations are offered to transient guests must file bed taxes. The collection of the 6.5% County bed tax (Bed Tax) is disbursed to the Global Center for Health Innovation, Municipalities, Rock and Roll Hall of Fame, Sports fund, and Destination Cleveland.



Audits of the approximately 194 registered establishments are performed by the Lodging Tax Office to ensure the collection and accuracy of the bed tax. Based on the results of the audit, the Lodging Tax Office will file audit assessments, penalties, and interest against any establishments that were found to owe additional tax. The department also answers questions from the establishments about Bed Tax responsibilities.

The following table illustrates the approximate amount of total revenue collected by the Lodging Tax Office (2019-2022). This includes the Bed Tax collected and any audit assessments collected:

Year	Amount Collected
2019	\$26,602,412
2020	\$13,401,776
2021	\$22,607,581
2022	\$31,698,759

Commendable Practices

We commend and thank the Fiscal Office for their cooperation during the audit. DIA especially thanks the Lodging Tax Office employees for their time and effort during the audit. Based upon the results of our audit, we believe Lodging Tax Office processes relating to the administration of the Bed Tax are well managed. Specific commendable practices that DIA noted during the audit include:

- Implementing a new system for managing Bed Tax returns and payments. This will increase efficiency through automation. It also allows for identification of unregistered taxpayers subject to the Bed Tax.
- Audits are not necessarily performed by all counties with a Bed Tax. The Lodging Tax Office conducts audits in order to ensure compliance with tax laws and this can increase revenue to the County.

Priority Level Criteria for Recommendations

High (P1)	Highest-Ranking Officer's immediate attention is required. Corrective action is strongly recommended (<u>30 days</u>).
	<ul style="list-style-type: none"> • Financially material loss or potential loss • Lack of or failure of internal controls requiring considerable time and resources to correct • Non-compliance with laws, regulations, and policies resulting in significant loss of funds, fines, or restrictions • Significantly negative effect on the County's reputation or public perception
Moderate (P2)	Senior Management's attention is required. Corrective action is recommended (<u>90 days</u>).
	<ul style="list-style-type: none"> • Financial loss or potential loss • Internal controls exist but they are not effective, or they are not consistently applied • Non-compliance with laws, regulations, and policies resulting in loss of funds, fines, or restrictions • Negative effect on the County's reputation or public perception
Low (P3)	Management's attention is required. Corrective action is recommended (<u>180 days</u>).
	<ul style="list-style-type: none"> • Financial loss or potential loss is minimal • Internal controls exist, but could be improved • Non-compliance with laws, regulations, and policies is a minimal risk • No effect on the County's reputation or public perception
Business Process Improvement (P4)	Management or supervisory attention recommended but not required
	<ul style="list-style-type: none"> • Process improvement recommendation • Financial loss or potential loss is minimal or not applicable • Non-compliance with laws, regulations, and policies is a minimal risk or not applicable • No effect on County's reputation or public perception

In an effort to assist the auditee in making the best use of their resources, we have prioritized the recommendations according to the table above.

Findings and Recommendations

Lodging Tax Office Findings

FINDING Not Currently Monitoring to Ensure Taxpayer Registration

The Lodging Tax Office is not currently monitoring to ensure all required establishments are registered to file/pay Bed Tax.

The Lodging Tax Office currently uses a Bed Tax system from Gov OS called MUNIRevs. It consists of two modules:

- Bed Tax module- Tracks the monthly tax filings, payments, and audit results of registered taxpayers.
- Compliance module- Uses active agents of Gov OS to search websites for listings of properties that are offering room rentals. The module is designed to assist in the identification of establishments that are potentially subject to remitting Bed Tax but are not registered with the Lodging Tax Office.

The Compliance Module was not being used at the time of the audit. It should be noted that the Lodging Tax Office intends to utilize the Compliance module and has already drafted a form that could be sent out to inform potentially non-compliant establishments of the tax requirements associated with providing lodging.

During the period of the audit, and prior to implementation of MUNIRevs, Lodging Tax Office employees monitored the lodging environment for potential compliance on an event driven basis. They would contact establishments if they happened to note a news article or get a hit from an internet search which was performed occasionally. This practice was never a formalized process or used consistently as compliance monitoring.

The County Lodging Tax Office is responsible for the administration of the County Bed Tax.

ORC 5739.09 (A)(1) allows for a Bed Tax and states in part:

“A board of county commissioners may, by resolution adopted by a majority of the members of the board, levy an excise tax not to exceed three per cent on transactions by which lodging by a hotel is or is to be furnished to transient guests. The board shall establish all regulations necessary to provide for the administration and allocation of the tax. The regulations may prescribe the time for payment of the tax, and may provide for the imposition of a penalty or interest, or both, for late payments, provided that the penalty does not exceed ten per cent of the amount of tax due, and the rate at which interest accrues does not exceed the rate per annum prescribed pursuant to section [5703.47](#) of the Revised Code.”

The actions of taxpayers (whether due to ignorance, carelessness, or deliberate evasion) mean that instances of failure to comply with the law are inevitable. Taxing authorities should have strategies and controls in place to ensure that non-compliance is kept to a minimum. This includes registration with the taxing authority.

The Lodging Tax Office consists of three employees including a manager and two tax examiners. Resources are insufficient to adequately monitor for compliance without some form of automated assistance such as the MUNIREvs system. The MUNIREvs system was not implemented until the start of 2023. The initial focus of implementation was to ensure system functionality for existing registered users within the Bed Tax Module.

Risk to the County if Not Corrected

By not utilizing available software or implementing other procedures for searching for non-registered establishments that may be subject to the Bed Tax, the County may be losing tax revenue.

Recommendations

1. (P2) The Lodging Tax Office should adhere to its plans to use the Compliance module of MUNIREvs and continue efforts to begin utilizing the module to search for other establishments that may be subject to the Bed Tax in the near future.
2. (P2) Policies and Procedures should be created (*See Finding related to Policies & Procedures*) around the usage of the Compliance module. Including but not limited to:
 - How often, when, and how to utilize the module;
 - What Lodging Tax Office staff will utilize the module;
 - Steps for what to do after a potential new taxpayer is identified;
 - Any procedures to search for establishments if the Compliance module is not being used.

Management's Response:

The MUNIREvs bed tax system has a function/feature that searches websites for listings of properties that are offering room rentals. The module is designed to assist in the identification of establishments that are potentially subject to remitting Bed Tax but are not registered with the Lodging Tax Office. However, this feature will not be available for use until the full system implementation has been completed. The expected

completion date for the full system implementation is the end of Q1 2024. New procedures for the compliance module will be created and implemented after the system is fully functional.

Until the full system implementation has occurred and the compliance feature is operational, the Lodging Tax department will continue to use newspapers, google, and other search engines to help locate/identify non-compliant lodging establishments. This will be done on a monthly basis as part of the compliance monitoring process until the system's compliance module becomes fully operational.

Target Date of Completion: 3/31/24

FINDING Reconciliations Lack Review or Approval

Monthly reconciliations lack appropriate review or approval.

Monthly reconciliations are performed by the Lodging Tax Office Manager between the Bed Tax system (MUNIREvs), payment system (Point 'N' Pay), bank statements, and the County's financial system (Lawson). During the audit, DIA noted reconciliations are not sent to, reviewed, or approved by another employee in the Fiscal Office. Additionally, the monthly reconciliation process is not detailed in Lodging's Policies and Procedures Manual (PPM).

During the audit, DIA reperfomed a sample of Bed Tax monthly reconciliations. No discrepancies were noted.

Performing regular monthly reconciliations of transactions and having those reconciliations approved by someone separate from the process of performing the reconciliation is an important control to ensure errors and/or fraud are prevented.

The Lodging Tax Office's PPM detail procedures for the reports used to reconcile payments but does not detail the monthly reconciliation process. It also does not contain provisions that require reviews and approvals for the monthly reconciliations.

The Lodging Tax Office staff is limited to three employees including only one supervisor. The current practice is the supervisor performs the reconciliation. Review and approve of the reconciliation internally within the department is not currently possible.

Risk to the County if Not Corrected

There is an increased risk of errors or fraud going undetected without the review and approval of the reconciliation by a responsible employee that is not performing the reconciliation.

Recommendations

1. (P2) The Lodging Tax Office should require reconciliations to be reviewed and approval documented by an employee that is independent of the tax collection and remittance processes and who does not have any responsibility related to the preparation of the reconciliation.

This review/approval of reconciliations should be incorporated within PPM (*See Finding related to Policies & Procedures*).

Management's Response:

Detailed policies and procedures will be created for the monthly reconciliation process for Lodging Tax payments. The actual monthly reconciliation will be performed by a team member within the Fiscal department who is not involved in the collection of lodging taxes and/or the receipt or remittance of lodging tax revenue. The reconciliation will be reviewed and approved by someone other than the person performing the reconciliation.

Target Date of Completion: 3/31/24

FINDING Incorrect Journal Entry

There was a journal entry error of \$213,124.71 in June 2023 due to a calculation error.

In June of 2023, a \$632,469.82 journal entry transferring May 2023 Bed Tax Collections allocated to the Capital Improvement Fund should have only been \$419,345.11 (variance of \$213,124.71) as total receipts allocated had reached the \$2 million limit as required by the Bed Tax Agreement Amendment of 2017. This portion of the Capital Improvement Fund was agreed to be used for renovations at the Rocket Mortgage Fieldhouse. The journal entry did require and receive approval within Lawson by the Fiscal Office.

It should be noted:

- The Office of Budget Management (OBM), who authorizes the release of funds on a quarterly basis, did not overpay for the Rocket Mortgage Fieldhouse and simply made payment based on the Bed Tax Agreement from 2017 limiting their annual remittance to \$2 million.
- The Lodging Tax Office completed a correcting journal entry to address the error identified during the audit and made corrections to the spreadsheet that calculates the disbursement amounts.

When reliance is placed on information contained within or calculated by a spreadsheet, it is a best practice to have controls built into the spreadsheet that may be used to mitigate errors or irregularities. These controls may include:

- Logic Inspection- Inspecting the logic in critical spreadsheets by someone other than user or developer of the spreadsheet. The review should be formally documented.
- Input Control- Ensuring reconciliations occur to make sure that data is inputted completely and accurately. Data may be inputted into spreadsheets manually or systematically through downloads.
- Security and Integrity of data- Implementing a process to ensure that data embedded in spreadsheets is current and secure. This can be done by protecting cells to prevent inadvertent or intentional changes to standing data.

Accounting journal entries are records of transactions conducted by an organization. The Lodging Tax Office prepares monthly journal entries in the County's financial system (Lawson) for the collected Bed Tax monies remitted during the prior month. These entries record the movement of Bed Tax monies collected to their appropriate recipient funds within Lawson. A PDF derived from a spreadsheet is used to facilitate the journal entry process.

The Bed Tax Agreement Amendment of 2017 established a portion of Destination Cleveland receipts would go towards the Q (later renamed Rocket Mortgage Fieldhouse) Renovations Project from 2017-2034, in accordance with a payment plan schedule. During 2023, the Rocket Mortgage Fieldhouse was to receive a percentage of Bed Tax collections; however, total receipts were to be limited to \$2 million.

OBM authorizes actual payments made after journal entries are recorded.

The supporting documentation used for the journal entry was a PDF derived from an Excel spreadsheet. The spreadsheet included an error in the calculating formula as it did not factor for the \$2 million cap. This was a month in which both Rocket Mortgage Fieldhouse and Destination Cleveland were receiving funds as the agreed upon yearly disbursement amount of \$2 million had been met. The error was unnoticed by the Lodging Tax Office or Fiscal Office. Additionally, there is no formal review of the PDF, or the spreadsheet used to make journal entries prior to the Lodging Tax Office submission into Lawson.

Risk to the County if Not Corrected

The Accounting Unit used for the Rocket Mortgage Fieldhouse disbursements (FS500160-41200) was transferred the incorrect amount. Incorrect journal entries increase the risk that actual payments will be made in error or cause errors in financial reporting.

Recommendations

1. (P2) There should be a review of the spreadsheet used to create the PDF used to make journal entries by someone that is not preparing the spreadsheet or the journal entries to ensure that the appropriate logic, input, and security controls were designed into it, so the correct amount of money is being transferred into the correct accounting units.
2. (P2) The process of making journal entries and their review should be noted in the Policies and Procedures Manual (*See Finding related to Policy and Procedures*).

Management's Response:

A spreadsheet will be created for the Lodging Tax Office that has a control feature(s) to ensure that the data amounts are input completely and accurately and that thresholds aren't exceeded. The supporting documentation to be provided for the journal entry will be the actual excel spreadsheet with calculations instead of a PDF document. We will reinforce with the journal entry reviewers that they need to review and validate the information that has been submitted and that they must ensure the sufficiency of the support for the entry.

Target Date of Completion: 1/31/24

FINDING Policies and Procedures Require Updating

The Lodging Tax Office Policies and Procedures lack key procedures and require updating to reflect current practices.

The following areas need to be reviewed, to ensure current practices are reflected, and the relative policy or procedure documented or updated:

- Procedures surrounding MUNIRevs (GovOS),
- Update forms,
- Reconciliation process including review and approvals,
- Review and approval of Management’s work on payments,
- Guidance on establishing interest rates to be charged to taxpayers in accordance with Ohio Revised Code (ORC) and County practice,
- Processes relating to methodology of audit selection.

Formally documented procedures are best practice. Documented procedures promote compliance with laws and regulations, consistency of work, and serves as a training tool for new employees. Policies and Procedures Manuals (PPM) provides an overview of a process and any relative requirements (such as review signoffs).

The Lodging Tax Office has written procedures on most processes in various stages of completion recorded in numerous documents. MUNIRevs (GovOS), was implemented in early 2023 and there has not been enough time to include all the new policies and procedures needed, as changes are still being implemented.

The Lodging Tax Office is a small department of three employees who have been working in the department for many years. The processes needed for completing work are understood by these employees.

Risk to the County if Not Corrected

Failure to have adequate internal guidance may result in inconsistent operations that lead to financial statement inaccuracies, non-compliance with regulations, and less than expected operational results. There is also increased difficulty training new employees to learn the positions’ responsibilities and the department’s processes.

Recommendations

1. (P3) The Lodging Tax Office should revise their PPM to reflect current practices and desired daily operations. The PPM should be approved by Fiscal Office management. It should also be reviewed and updated on a regular basis. At the minimum it should include:
 - Procedures surrounding MUNIRevs (GovOS);
 - Updated forms;

- Reconciliation review/approval;
- Review and approval of Management's work on payments;
- Penalty and interest rates charged;
- Audit practices.

Management's Response:

The Lodging Tax Office will ensure that all documents related to the processes and procedures of the department are completed and that the documents reflect current practices and operations of the department. Procedures and forms will continue to be reviewed and updated as processes, methods, or systems change. The department will continue to update its' policies and procedures on an ongoing basis, but no less than annually to ensure that all procedure manuals are current.

There are already current procedures and/or a methodology that exist and is used in determining which establishments are selected for audit testing.

Target Date of Completion: 6/30/24

FINDING Bed Tax Recipients May Not Receive Proper Oversight

Entities that receive funding from Bed Tax proceeds may not receive appropriate oversight relative to funds received.

Bed Tax revenue is allocated and distributed to Destination Cleveland, Rock and Roll Hall of Fame, the Global Center for Health Innovation, various Municipalities and sports funds as per ordinance and written agreements. Cuyahoga County also keeps a portion.

Destination Cleveland, which receives the largest portion of the Bed Tax, delivers an annual presentation to County Council that provides a general overview of operations and funds usage. Additionally, the Auditor of State performs an Agreed Upon Procedures (AUP) engagement of Destination Cleveland annually for benefit of Cuyahoga County. The AUP includes a tax proceeds comparison, inquiry, and sampling of disbursements to ensure compliance with ORC 5739.09, the 2014 Agreement Governing the Use of Extended Capital Improvement Bed Tax, and the 2017 Addendum to the 2014 Existing Agreement.

Although this does not strictly meet the requirements noted in the Bed Tax Reallocation Agreement or Code of Regulations, it provides comparative oversight. Oversight of and reporting from entities other than Destination Cleveland is not performed or received.

Oversight is an essential function through which legislators determine whether current laws and appropriations are achieving intended results. There are agreements and procedures that note reporting/oversight responsibilities on the use of Bed Tax Funds; however, this is limited to Destination Cleveland and includes:

- Bed Tax Reallocation Agreement (Addendum to the 2014 Existing Agreement)
 - Deliver to the County, an approved annual operating budget for Destination Cleveland for such fiscal year, in such form as typically prepared for Destination Cleveland's management and board, which shall in no event be in a form with less than reasonable detail and shall include capital and operating projections, solely for the information of the County.
- Code of Regulations for Transient Guests
 - The Convention and Visitors Bureau of Greater Cleveland, Inc./Destination Cleveland shall present quarterly financial and performance reports as well as an annual operations report each showing its use of the funds hereby appropriated, to the County Executive and County Council and the County Fiscal Officer,
 - The Fiscal Officer shall be charged with the duty of inquiry examination of the work of the said Convention and Visitors Bureau of Greater Cleveland, Inc./Destination Cleveland, to the end that the intent and purposes of this Resolution have been and are being satisfied,
- Cuyahoga County Code 717.04
 - Positively Cleveland (Destination Cleveland) shall annually update the County Executive, County Council, the Cuyahoga County Mayors and Managers Association, the Mayor of Cleveland, and Cleveland City Council regarding the use of the Capital Improvement Bed Tax funds.

There was no unified guidance for the level of oversight the County was to provide for Destination Cleveland Bed Tax funds. Except for Destination Cleveland, none of the entities that receive Bed Tax monies have a contractual or legislative requirement of financial or performance reporting and fiscal oversight.

Risk to the County if Not Corrected

Without appropriate County oversight, there is an increased risk of noncompliance with the various agreements, policies, and regulations. Additionally, performance that does not meet County expectations may go undetected.

Recommendations

1. (P3) The County should consider either:
 - a. Following the applicable language as it relates to the oversight of reporting and usage of Bed Tax monies (Quarterly monitoring), or
 - b. Revise language in the agreements and Code of Regulations to reflect the level of oversight they will follow.

2. (P4) The County should consider implementing similar oversight requirements for other entities that receive Bed Tax monies (e.g. Rock and Roll Hall of Fame, Global Center for Health Innovation, and sports funds). The level of oversight should mirror the level of risk incurred by any restrictions imposed in the enabling legislation (i.e. in instances where the risk of misuse of funds is low perform oversight functions every 3-5 years). Policies and Procedures should be appropriately updated with any additional oversight requirements.

Management's Response:

The Fiscal Office will not be performing additional oversight for other entities that receive Bed Tax monies (e.g. Rock and Roll Hall of Fame, Global Center for Health Innovation, and sports funds) although the Global Center for Health Innovation is also subject to an annual audit by the Auditor of State and their financial reports are reviewed by the County and LGS annually. As the County does not perform oversight over every entity that receives County or tax monies to determine whether the entities are achieving intended results, there will be no exception for special oversight for entities receiving bed tax monies.

The County Code of Regulations for Transient Guest and the Cuyahoga County Code 717.04 will be updated to reflect current procedures and/or requirements.

Target Date of Completion: 5/31/24

FINDING Attempt to Increase Audit Coverage

The Lodging Tax Office could increase compliance assurance through increased audit coverage.

Currently, approximately one audit a month is completed. The following table summarizes the number of audits completed, approximate audit percentage completion rate of population, and amount of revenue collected based on audit assessments from 2019-2022:

Year	Completed Audits	Approximate Audit Completion %*	Approximate Population of Taxpayers*	Audit Assessments collected
2019	11	9%	121	\$378,797
2020	9	7%	131	\$346,687
2021	11	7%	153	\$526,343
2022	12	7%	177	\$257,570
Totals	43	-	-	\$1,509,397

**Notes*

- *As establishments are closing and opening throughout the year it is difficult to obtain an exact percentage of completion of eligible taxpayers.*
- *Population may include Airbnb filers who may not be subject to audit based on the agreement between the County and Airbnb.*
- *Population does not include potential establishments that existed in prior years but closed prior to receiving population as of 12/31/2022.*
- *Population only reduced by hotels noted as opened in preceding year.*

It would take approximately 16 years to complete an audit of every eligible taxpayer at the current rate of completion. The rate of completion may increase as the MUNIREvs system implementation creates efficiencies through automation of previously manual processes.

Tax audits are an essential detective control in establishing and maintaining compliance. They ensure that taxpayers are following the rules regarding exemptions and tax remittance. Additionally, audits have direct effects by raising revenue through the assessment of additional taxes, interest, and penalties when appropriate.

The Code of Regulations for the Cuyahoga County Lodging Tax Office grants the authority to perform audits of Bed Tax returns and assess additional tax, interest, and penalties.

A best practice within audit functions is to ensure appropriate audit universe coverage occurs. Many audit functions consider a three to five-year period appropriate to achieve full audit universe coverage, which is often dependent on the universe size. The audit universe of the Lodging Tax Office includes the 194 registered taxpayers as of 12/31/2022. During the audit, the Lodging Tax Office advised that all taxpayers should ideally be audited on a five-year cycle.

Conducting audits is an important detective control to ensure that taxpayers are following the rules regarding exemptions and tax remittance.

The Lodging Tax Office may lack appropriate resources. Their staff is small, consisting of one supervisor and two staff employees. There are other duties that must be performed by Lodging Tax Office employees in addition to audits. Additionally, there were also more manual processes that needed to be performed relating to tax filings and payments prior to the implementation of the MUNIREvs system in early 2023. The audit process takes time to properly plan, complete, review, and issue audit assessments. The audits completed by the Lodging Tax Office are typically for a four-year period of revenues, so audits completed capture more information than the year the audit is completed.

Risk to the County if Not Corrected

Increased frequency of audits may increase the audit assessment revenue received by the County. Increased audits may also increase the accuracy of tax returns if taxpayers are aware there is an increased likelihood of being audited.

Recommendations

1. (P4) The Lodging Tax Office should work with Fiscal Office Management to develop plans to increase audit rates. This may include, but not limited to the following:
 - Increased staffing for the Lodging Tax Office;
 - Leveraging new systems to increase audits completed by automating certain tasks;
 - Possible changes to procedures to shorten the time to complete audits i.e. shorter audit periods.

Management's Response:

The Lodging Tax Office plans to hire at least two additional resources to perform audits. The additional resources will help to ensure that the appropriate audit universe coverage occurs, which will be targeted at a four-to-five-year cycle for full audit universe coverage.

Target Date of Completion: 12/31/24