

Sonoma County

Auditor-Controller-Treasurer-Tax Collector

Internal Audit Report

# Compliance Audit: Transient Occupancy Tax Operator Collections & Remittances

For the Calendar Year Ended  
December 31, 2017

Engagement No: 3565  
Report Date: November 20, 2019



**Erick Roeser**  
Auditor-Controller-Treasurer-Tax Collector

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Audit No. 3565**

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## **Executive Summary**

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The Audit Division of the Sonoma County Auditor-Controller-Treasurer-Tax Collector's Office (Internal Audit) has completed a compliance audit of collections and remittances of certain operator entities subject to the Sonoma County (County) Transient Occupancy Tax (TOT) Ordinance.

### **Current Year Operator Audits**

For the period January 1, 2017 to December 31, 2017, twenty (20) operators selected for audit reported a total of \$9.11 million in taxable receipts and paid \$1,104,141 in TOT. All twenty (20) operators generally remitted TOT owed to the County in a timely manner and complied with the TOT ordinance, as summarized on Table 1 of Appendix A.

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## **Introduction and Background**

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### **Introduction**

Internal Audit has completed a compliance audit of the collections and remittances of certain operator entities, (operators), subject to the County TOT Ordinance. The audit was conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing (Standards)*. These Standards require that we identify, analyze, evaluate, and document sufficient information and evidence to achieve audit objectives. We believe that the evidence obtained provides a reasonable basis for the results and recommendations contained in our audit report.

The purpose of this audit report is to furnish management independent and objective analyses, recommendations, and other information concerning the activities reviewed. The audit report is a tool to help management identify and implement improvements.

Occasionally, to fulfill its risk management responsibilities, management requests Internal Audit to perform studies, analysis or audits. In responding to these requests we ensure that we do not take on any responsibilities for designing, implementing or operating any part of internal control systems so that our independence in regards to those systems is not impaired.

At the request of TOT Administration, we have performed audits of entities subject to TOT and plan on providing such assistance in the future. We do not believe that performing these audits constitute assuming responsibility for the design, implementation, or operation of any part of TOT Administration's internal control system. The TOT Administration selects the entities and agrees to the audit scope proposed by Internal Audit.

### **Background**

#### **Overview**

The assessment and collection of TOT is authorized under California State Revenue and Taxation Code Section 7280, as an additional source of non-property tax revenue to local governments. TOT is assessed by operators on transients who occupy lodging facilities (e.g. hotels, motels, campgrounds, or vacation rental homes) in the unincorporated areas of the County for fewer than 30 consecutive calendar days. In Sonoma County, this tax was levied at a rate of 12%, for this audit period. TOT funds are discretionary, in that the Board of Supervisors may direct use of these funds for any legitimate county expense. The tax code does not require any specific use of TOT funds.

Beginning January 1, 2017 the County entered into an agreement with Airbnb for the collection, reporting, and remittance of TOT for booking transactions completed by hosts and guests on the Airbnb internet-based platform for the unincorporated areas of Sonoma County. Airbnb will report aggregate information reported on the County's TOT return form.

As of December 31, 2017, there were approximately 2,332 operators, registered with the County, including hotels, motels, bed & breakfasts, inns, recreational parks, campgrounds, vacation rentals, and property management firms. The total collection of TOT for the calendar year 2017 was \$21,156,705, as compared to 2016 which had revenue of approximately \$16.56 million. The TOT Administration is

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## **Introduction and Background**

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responsible for the administration and enforcement of TOT and works closely with the Permit and Resource Management Department to ensure that all vacation rentals registered by them obtain a TOT certificate.

### **Policies & Procedures**

Each operator is required to report and remit TOT on a quarterly basis. TOT Administration sends the TOT return form to all active operators two weeks prior to the end of each calendar quarter, and they request the gross rent receipts for the reporting period, less qualified exemptions, in order to calculate the 12% tax due. A qualified exemption is the rents received from a tenant who is a federal, state, or foreign government officer or employee on official business.

Penalties and interest are applied if the returns are not filed timely or the tax is unpaid. For late filings, a penalty of 10% of the base tax is calculated for failure to file on or before the last day of the month following the close of the calendar quarter, an additional 10% penalty is assessed for the second month of delinquency. For late payments, interest of 1.5% per month on the base tax is charged from the delinquent date to the date of payment. If payment is not received in full by the first working day of the second month of delinquency, the account is transferred to the Central Collections section of the Auditor-Controller-Treasurer-Tax Collector's Office. Central Collections assists the TOT Administration with collection. A Certificate of Delinquent TOT Lien is filed with the Sonoma County Recorder's Office by the Revenue Accounting Division when payments from an operator become two quarters late.

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## **Objective, Scope and Procedures**

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### **Objective**

The primary objectives of this audit were to determine:

1. Whether selected entities remitted TOT owed to the County in a timely manner and materially complied with the applicable ordinance.

### **Scope**

#### **Current Year Operator Audits**

We audited one year of TOT returns for twenty (20) entities selected by the TOT Administration. TOT Administration agreed in advance to the scope of the audits. The audit covered the period January 1, 2017 to December 31, 2017. The scope of our work encompassed reviewing records of transactions subject to the TOT as well as interviewing the management and staff of operators responsible for the maintenance of financial and guest management systems (Operators).

### **Procedures**

The overall objective of the audits was to determine if the Operators' financial records supported their filed quarterly TOT returns. To accomplish this, we performed a review of the Operators' internal controls over the collection and remittance of TOT, including the entering of guest information in reservation systems, processing and recording of financial transactions and summarizing of financial transactions for the purpose of preparing TOT returns.

Operators are required to maintain records necessary to determine the amount of TOT owed to the County. At a minimum the records deemed necessary for this determination shall be a chronological cash journal showing tax and room rate separately, or other means acceptable to the TOT Administration of summarizing the Operator's monthly or quarterly revenue, supported by room registrations (including the name and address of the transient), a calendar of advance registrations, copies of forms used to claim exemption from the tax, and pre-numbered payment receipts showing payment for occupancy which state the room rate separate from the amount of tax paid and which may, with reasonable effort, be identified with the revenue summary. In instances where the Operator did not maintain records as stated above, all guest transactions within the period under audit were selected and tested. If the Operator maintained records as stated above, a sample of transactions within a specific time period was selected and tested.

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## Results

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For the period January 1, 2017 to December 31, 2017, twenty (20) operators audited reported a total of \$9.11 million in taxable receipts and paid \$1,104,141 in TOT. Thirteen (13) of the twenty (20) generally remitted TOT owed to the County in a timely manner and complied with the TOT ordinance, as summarized on Table 1 of Appendix A. Six (6) of the entities underpaid TOT tax by a total amount of \$5,111 and one entity overpaid by an amount of \$213.

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## **Recommendations & Staff Acknowledgment**

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### **Recommendation No. 1:**

Over and under payments, as identified in Appendix A should be settled with respective Operators as appropriate.

### **Management Response:**

Management agrees and will follow standard policies and procedures to refund/collect amounts as identified.

### **Recommendation No. 2:**

TOT Administration should take steps as outlined in the TOT ordinance to determine and assess the tax, interest and penalties for all Operators that failed to cooperate with the audits.

### **Management Response:**

Management agrees and will follow standard policies and procedures to determine, assess and collect any liabilities due.

### **Staff Acknowledgement**

We would like to thank management and staff for their time, information, and cooperation throughout the audit.

## Appendix A: Schedule of Operators Reviewed

The following table details the Operators that provided sufficient records to complete their audit:

**Table 1: Schedule of Audited Operators Providing Sufficient Records**

County of Sonoma Transient Occupancy Tax For the period of January 1, 2017 to December 31, 2017					
<u>Entity</u>	Taxable Receipts Reported	Taxable Receipts Per Review	Tax Paid	Tax Per Review	Over (Under) Paid
Creekside Inn & Resort	\$ 467,241	\$ 467,241	\$ 56,069	\$ 56,069	\$ -
Healdsburg Estate	143,779	143,779	17,253	17,253	-
Gustafson Family Vineyard	131,090	131,090	15,516	15,516	-
Riverlane Resort	263,985	263,985	27,633	29,046	(1,413)
2300 Mill Creek LLC	42,285	42,285	4,728	4,728	-
The Radford Inn, Inc.	274,984	274,984	30,751	30,751	-
Russian River RV Campground	179,506	179,506	21,541	21,541	-
Sea Ranch Escapes	1,903,321	1,929,596	216,639	217,899	(1,260)
Bodega Bay & Beyond	2,430,521	2,430,521	326,842	326,842	-
Speedway Sonoma LLC	796,804	796,804	95,616	95,616	-
Westerbeke Ranch Conf. Center	428,081	428,081	50,527	50,527	-
Salt Point Lodge	370,599	370,605	44,473	44,494	(21)
Redwood Inn	562,570	567,320	67,508	68,078	(570)
Wellington House	147,267	147,267	17,497	17,497	-
Santa Nella House B & B	143,044	142,745	16,916	16,916	-
1015 Westside Road LLC	121,194	121,194	14,543	14,543	-
3217 Lovall Valley Road	168,109	168,109	16,436	16,436	-
A Breath of Heaven	110,777	109,205	12,214	12,001	213
Crossroads Vineyard LLC	112,517	124,070	13,502	14,888	(1,386)
Duggan Ranch LLC	316,146	352,247	37,937	38,398	(461)
<b>Total</b>	<b>\$ 9,113,820</b>	<b>\$ 9,190,634</b>	<b>\$ 1,104,141</b>	<b>\$ 1,109,039</b>	<b>\$ (4,898)</b>

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## **Appendix B: Prior Year Results and Recommendations**

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### **Recommendation No. 1:**

Over and under payments, as identified in Appendix A, should be settled with respective operators as appropriate.

**Status: Implemented**

### **Recommendation No. 2:**

TOT Administration should take steps as outlined in the TOT ordinance to determine and assess the tax, interest and penalties for all operators that failed to cooperate with the audits.

**Status: Implemented**