



AGENCY: City Council  
MEETING DATE: January 28, 2019  
DEPARTMENT: Finance  
PRESENTED BY: Victor Damiani  
EMAIL ADDRESS: [vdamiani@fortbragg.com](mailto:vdamiani@fortbragg.com)

## AGENDA ITEM SUMMARY

### **TITLE:**

**Receive Report and Finance and Administration Committee Recommendation and Consider Adoption of City Council Resolution to Authorize City Manager to Execute Agreement with Avenu Insights and Analytics (a/k/a Muni Services) to Conduct a Transient Occupancy Tax (TOT ) Audit, Amount Not To Exceed \$30,400 and Approving Budget Amendment No. 2019-05 for Fiscal Year 2018/19 to Reallocate \$30,400 from Measure AA/AB Tax Collections to Account 110-4150-0312**

### **ISSUE:**

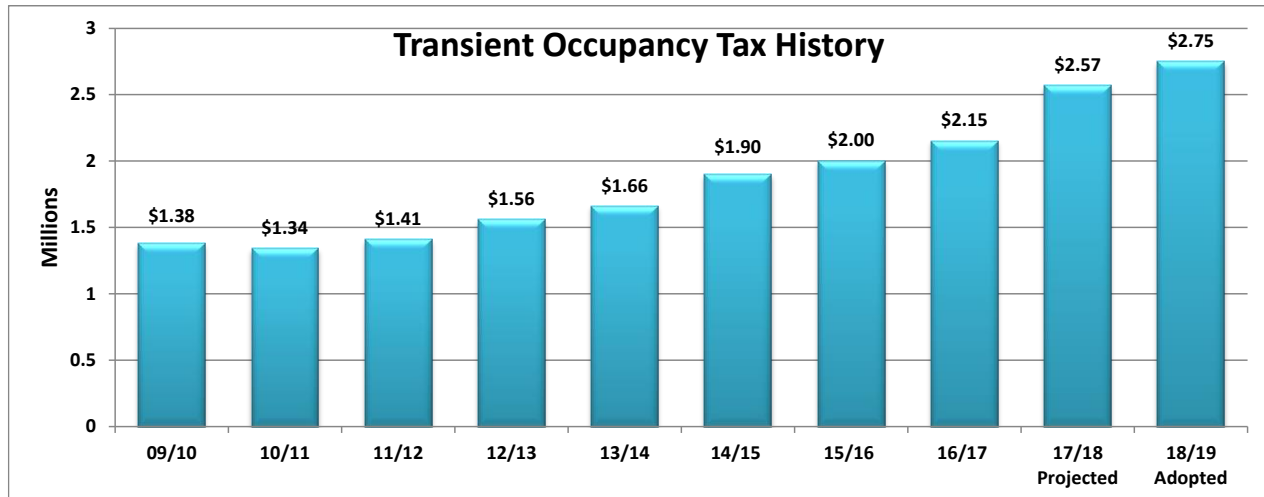
Transient Occupancy Tax (TOT) is a local tax that is applied to the cost of hotel or other lodging stays of less than 30 days. In 2016, with passage of local Measures AA and AB, the City's TOT rate increased from 10% to 12%. This tax is a revenue source solely for the General Fund. TOT is collected by lodging establishments and remitted to the City on a monthly basis. Currently, there are 27 hotels/motels, 3 approved vacation rentals and 1 RV park operating in the City. Factors influencing TOT revenues include vacancy rates, changes in business and leisure travel, new hotels, hotel expansion, and room rate increases.

The City collects Transient Occupancy Taxes in accordance with the City's Municipal Code, Chapter 3.12. Additionally, Chapter 3.12 of the Municipal Code authorizes the City Tax Administrator (currently assigned to the City Finance Director) to audit the financial records of the City's TOT tax payers to determine the accuracy of tax returns filed. The City's Tax Administrator is recommending a TOT audit be conducted.

### **ANALYSIS:**

The Tax Administrator believes it would be prudent to conduct a TOT audit at this time for a few reasons:

First, the City's TOT is the leading revenue source for the City's General Fund. As can be seen in the chart below, TOT has had a strong growth trajectory for several years running. In FY 2018-19, TOT is expected to provide \$2.7 million or 29% of the total General Fund operating revenue.



Secondly, auditing of tax revenues is an important financial tool used to help ensure tax compliance and maximize the City's revenue collection. The City has not conducted a TOT audit in the last five years and it is not known if the City has ever audited this very important revenue stream. It is good practice to periodically conduct an independent TOT audit. Muni Services recommends an audit be conducted every 3 to 5 years.

Thirdly, ongoing review of TOT tax filings and payments indicates the possibility that some lodging operators may be underreporting tax revenue collected. It should be noted that underreporting does not necessarily indicate intent to defraud and may be the result of errors or lack of understanding on the part of lodging operator staff. Of course, intentional underreporting is a possibility as well.

### **VENDOR PROPOSALS:**

Staff solicited proposals from two revenue enhancement firms that operate in California; Muni Services and Hdl. Outside of local CPA firms, these are two of the primary companies operating in this field in California. Each of the two proposals are attached to the agenda item. Each firm provided a cost to conduct a one-time audit and also a proposal for full administration and audit services.

#### **Hdl Pricing:**

Audit Service: \$40,500

Administration Service; \$17,550 annually

#### **Muni Services Pricing:**

Audit Service: \$30,400

Administration Service; \$4,050 annually

Oftentimes TOT audits result in recovery of lost revenue. The Muni Services audit proposal lists the results of several prior audits. Varying amounts of revenue were recovered ranging from \$68,000 to \$608,000. Staff believes it is likely that if the City of Fort Bragg proceeds with a TOT audit, recovered revenue will outpace the cost of conducting the audit.

If the City moves forward with a one-time audit, some anxiety and displeasure is likely to be voiced by some of the local hotel operators. This is a common and natural reaction to being audited. This may be compounded somewhat due to the long period of time since the last audit was conducted. On the other hand, many hotel operators may view the audit as a means of ensuring fair competition in the market. Both firms in consideration have a long history of conducting audits and understand the importance of conducting themselves professionally and unobtrusively.

On November 7, 2018, the City's Finance and Administration Committee reviewed both vendor proposals presented tonight. On December 5, 2018 the City's Finance and Administration Committee

directed staff to bring the TOT Audit item to the full City Council with a Committee recommendation to move forward immediately with the audit. The Committee further recommended awarding the TOT Audit contract to Muni Services.

**RECOMMENDED ACTION:**

Authorize City Manager to Execute Agreement with Avenu Insights and Analytics (a/k/a Muni Services) to Conduct a Transient Occupancy Tax (TOT) Audit, Amount Not To Exceed \$30,400 and Adopt City Council Resolution Approving Budget Amendment No. 2019-05 for Fiscal Year 2018/19 to Reallocate \$30,400 From Measure AA/AB Tax Collections to Account 110-4150-0312.

**ALTERNATIVE ACTION(S):**

1. Authorize City Manager to Execute Agreement with Avenu Insights and Analytics (a/k/a Muni Services) to conduct a Transient Occupancy Tax (TOT) Audit and provide TOT Administrative Services.
2. Award contract to Hdl.
3. Do not award a contract for TOT Audit or Administration services.

**FISCAL IMPACT:**

The cost of the audit is \$30,400 to be paid from Measure AA/AB tax collections. Staff believes that on the low end revenue recovery will be equal to the cost to conduct the audit making the action revenue neutral. On the upper end of the spectrum revenue recovery is likely to be approximately \$150,000, making the action revenue enhancing. Regular audits also ensure and encourage tax compliance going forward.

**CONSISTENCY:**

The recommended action is consistent with the City's Fiscal Policy 4.(d).

**IMPLEMENTATION/TIMEFRAMES:**

From the time of contract execution to completed audit typically takes 10 to 12 months. If approved, staff intends to begin the process early in February 2018 with the goal of completing the audit prior to the end of calendar year 2019.

**ATTACHMENTS:**

1. Resolution to Approve Budget Amendment 2019-05 and Authorize City Manager to Execute Agreement with Avenu Insights and Analytics (aka Muni Services)
2. Muni Services proposal
3. Hdl proposal
4. Proposed contract with Muni Services

**NOTIFICATION:**

None.