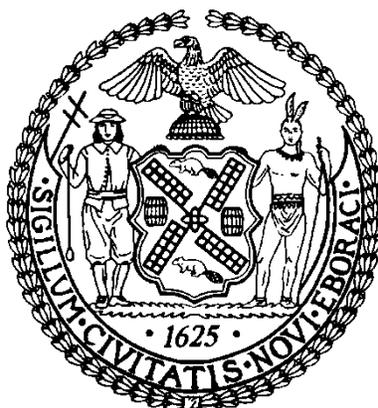


**CITY OF NEW YORK
OFFICE OF THE COMPTROLLER**

**John C. Liu
COMPTROLLER**

FINANCIAL AUDIT

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Deputy Comptroller for Audit**



**Audit Report on the
Department of Finance's
Hotel Room Occupancy Tax
Collection Practices**

FP11-084A

November 28, 2011

<http://comptroller.nyc.gov>



THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

John C. Liu
COMPTROLLER

November 28, 2011

To the Residents of the City of New York:

My office has audited the Department of Finance's (DOF) controls over its tax collection practices to ensure that hotel operators and room remarketers collect and remit the Hotel Room Occupancy tax (HROTX) due to New York City as required. We audit City operations such as this as a means of increasing accountability and ensuring that City resources are used effectively, efficiently, and in the best interest of the public.

The audit found that DOF had significant internal control weaknesses regarding DOF's HROTX collection practices that resulted in 92 hotels owing \$8,894,040 in HROTX. Specifically, DOF did not maintain a complete list of all hotels that are required and authorized to collect the HROTX. Also, DOF did not ensure that all hotel operators and room remarketers commencing business, or opening new hotels, file a Certificate of Registration within three days after the commencement or opening.

The audit makes 16 recommendations to DOF, including that it should conduct audits of the 64 hotels identified in this report as non-filers. The audit also recommends that DOF should conduct further reviews of the 20 room remarketers we identified to determine whether they should be paying the HROTX and pursue actions for those deemed to be non-filers, and conduct audits of the eight hotels mentioned in this report that under-reported the amounts of HROTX due and recoup any additional amounts owed.

The results of the audit have been discussed with DOF officials, and their comments have been considered in preparing this report. Their complete written response is attached to this report.

If you have any questions concerning this report, please e-mail my audit bureau at audit@comptroller.nyc.gov.

Sincerely,

A handwritten signature in black ink, appearing to read "John C. Liu".

John C. Liu

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The City of New York
Office of the Comptroller
Financial Audit

**Audit Report on the
Department of Finance's
Hotel Room Occupancy Tax Collection Practices**

FP11-084A

AUDIT REPORT IN BRIEF

The Department of Finance (DOF) is responsible for collecting City revenues efficiently and encouraging compliance with City tax and other revenue laws. One such revenue DOF collects is the Hotel Room Occupancy tax (HROTX), which is imposed upon the occupancy of a hotel room in the City of New York.¹ DOF collected \$369.1 million in HROTX revenue for Fiscal Year 2010.

All hotel operators are required to file a Certificate of Registration with DOF within three days after the opening of a new hotel. DOF will issue a Certificate of Authority, within five days of registering, to collect the HROTX. Once a hotel is registered, all hotel operators are required to collect the HROTX and remit it to the City. Then all hotel operators are required to file a Hotel Room Occupancy Tax Return quarterly. During the 2010 tax year, the HROTX was and continues to be 5.875 percent of the total room rate of all room types, plus an additional charge per room per day between 50 cents and \$2.00 depending on the room rate.

The objective of this audit was to determine whether DOF had adequate controls over its tax collection practices to ensure that hotel operators and room remarketers² collect and remit the Hotel Room Occupancy tax due to New York City as required.

Audit Findings and Conclusions

DOF collected HROTX from 1,076 hotels totaling \$374 million for the June 1, 2009–May 31, 2010 tax year. However, we noted several internal control weaknesses regarding DOF's HROTX collection practices that resulted in 92 hotels owing an estimated \$8,894,040 in HROTX. Eighty-four of the 92 hotels—64 hotels and 20 room remarketers—in operation did not file HROTX. We estimate that these 64 hotels owe \$1,821,058 for the June 1, 2009–May 31, 2010 tax year. We further estimate that these 64 hotels owe \$7,615,122 from the year the hotel began business through the 2010–2011 tax year.³ Also, while the remaining eight hotels filed

¹ Hotel classifications also include hostels, bed and breakfasts, motels, and room remarketers.

² Hotel rooms are rented from an intermediary and not the hotel itself (e.g., Expedia or Travelocity).

³ This figure includes the \$1,821,058 we estimated for the 2009–2010 hotel tax year.

HROTX returns, we estimate that they under-reported HROTX by \$1,278,918 for the June 1, 2009–May 31, 2010 tax year.⁴ One of these hotels has filed for bankruptcy. We estimated that this hotel under-reported HROTX by \$66,547 for the last month of the 2009– 2010 hotel tax year. DOF officials have not completed an audit assessment for the owners of this hotel, but informed us during the exit conference that this hotel owes over \$2 million in total unpaid HROTX.

We found that DOF did not maintain a complete list of all hotels that are required and authorized to collect the HROTX. Also, DOF did not ensure that all hotel operators and room remarketers commencing business, or opening new hotels, filed a Certificate of Registration within three days after the commencement or opening and did not maintain copies of all the Certificates of Registration received from hotel operators and the returned Certificate of Authority when a hotel ceases business. In addition, DOF did not have a tracking system for all hotels to identify the estimated HROTX amount due from each hotel, did not maintain a tracking system of returned Certificates of Authority when a business was discontinued or sold, and did not link the hotel account identification number with the new number when a hotel changed names. Finally, DOF did not ensure that separate tax returns were always filed for each hotel.

In an effort to reduce the redundancies in government, we believe DOF and the New York State Department of Taxation (the State) could streamline their process by coordinating efforts in collecting HROTX. Currently, hotels operating in New York City must apply for Certificates of Authority on behalf of the City and State, collect the HROTX, and file HROTX returns separately from their New York State Sales Tax return. This is a redundant and arduous practice for hotel operators. Currently, hotel operators report hotel room occupancy “taxable sales” to the State. This is the amount subject to New York State’s Sales and Use Tax that hotel operators pay to the State. Instead of filing separate tax returns, we believe that DOF should coordinate with the State in order to allow the hotel to file one HROTX return on behalf of both the City and the State.

Audit Recommendations

To address these issues, we made 16 recommendations, including that DOF should:

- Conduct audits of the 64 hotels identified in this report as non-filers.
- Conduct further reviews of the 20 room remarketers to determine whether they should be paying the HROTX and pursue actions for those deemed to be non-filers.
- Implement a tracking system that includes, but is not limited to, the following:
 - Hotels that have submitted a Certificate of Registration
 - Hotels that have received a Certificate of Authority
 - Hotel Business Name and Address as well as the name of the Corporation that owns the hotel

⁴ We did not estimate beyond the June 1, 2009–May 31, 2010 tax year for these eight hotels.

- Hotels' HROTX filing status and an estimated HROTX amount due for each hotel required to submit HROTX
- Conduct audits of the eight hotels mentioned in this report that under-reported the amounts of HROTX due and recoup any additional amounts owed.
- Periodically assign staff to research and update the list of active hotels required to collect the HROTX annually and ensure that the list has the name and address of the hotel as it is doing business as.
- Ensure that separate tax returns are filed for each hotel as indicated on the *New York City Department of Finance NYC HTX Hotel Room Occupancy Tax Return for Use by Operators and Room Remarketers*.

Agency Response

In its response, DOF officials agreed with eight recommendations and partially agreed with eight recommendations. DOF did not agree with the audit calculation of \$1.8 million in hotel tax due from the 64 hotels during the audit period. DOF stated that hotels with fewer than 10 rooms have an occupancy rate of approximately 55 percent, significantly below the rate for larger size hotels. By applying the 55 percent rate across the board, DOF determined that the potential hotel tax payable during the audit period is \$1.2 million. DOF stated the 55 percent rate is based on "a review of filings for a recent annual period." However, DOF never indicated which specific year it was referring to and never provided this review to the audit team. Thus, the analysis could not be replicated and the information could not be verified. We, therefore, have no basis to assess whether DOF's estimate is accurate.

Additionally, as DOF is aware, in making the reported estimates, auditors did not include interest and penalties associated with late and non-filers. Based on information provided by the agency, DOF can expect to assess between \$596,000 (based on \$1.2 million) and \$895,000 (based on \$1.8 million) in interest and penalties. When interest and penalties are included, we estimate that, for these 64 hotels, DOF can anticipate additional tax collections between \$1.79 million (using DOF's estimates) and \$2.69 million (using auditors' estimates) during the audit period.

Nonetheless, the important point is that DOF has stated it agrees that outstanding HROTX should be recouped and has begun to perform either a follow-up limited scope audit or a field audit of the entities identified in this audit.

INTRODUCTION

Background

The Department of Finance (DOF) is responsible for collecting City revenues efficiently and encouraging compliance with City tax and other revenue laws, valuing all real property in the City, providing a forum for the public to dispute tax and parking violation liability, and maintaining property records. One such revenue DOF collects is the Hotel Room Occupancy tax (HROTX), which is imposed upon the occupancy of a hotel room in the City of New York. DOF collected \$369.1 million in HROTX revenue for Fiscal Year 2010.

The Hotel Room Occupancy rate is imposed upon the occupancy of any hotel room in the City of New York. The New York City Hotel Room Occupancy tax must be collected for every occupancy of each room in a hotel in the City of New York with the exception of the following:

- Permanent resident (a person who occupies a room for at least 180 consecutive days.)
- New York State, a public corporation, or a political subdivision of the State
- The United States federal government
- The United Nations
- A not-for-profit organization that was formed and operated exclusively for religious, charitable, or educational purposes, or for the prevention of cruelty to children or animals
- Summer camps for children that provide a program of instruction or training
- Campsites, trailer sites, and other like real property
- Rental of individual, privately-owned, summer houses, camps, beach houses, and similar properties
- Bungalows
- Efficiency units in motels

All hotel operators are required to file a *Certificate of Registration* with DOF within three days after the opening of a new hotel. DOF will issue a *Certificate of Authority* within five days authorizing the collection of HROTX.

Once a hotel is registered, all hotel operators are required to collect the HROTX and remit it to the City. Then hotel operators are required to file the appropriate Hotel Room Occupancy Tax Return for their type of business.⁵ Operators must file a separate Hotel Room Occupancy Tax Return for each hotel even if they operate more than one hotel. Combined returns are not allowed. The HROTX is based on the day rate “rent” being charged for a room:

⁵ For our audit period, there were three different forms—one for hotel operators (Form HTX), one for small facility operators only (Form HTXB), and one for room remarketers only (Form HTX-RR).

If the rent for the room is...	The tax will be...
\$10 or more, but less than \$20	50 cents/day + 5.875% of the rent
\$20 or more, but less than \$30	\$1.00/day + 5.875% of the rent
\$30 or more, but less than \$40	\$1.50/day + 5.875% of the rent
\$40 or more	\$2.00 per day + 5.875% of the rent

Objective

The objective of this audit was to determine whether DOF had adequate controls over its tax collection practices to ensure that hotel operators and room remarketers collect and remit the Hotel Room Occupancy tax due to New York City as required.

Scope and Methodology Statement

We conducted this performance audit in accordance with generally accepted government auditing standards. 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. This audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

This audit covered HROTX collection filings for the June 1, 2009–May 31, 2010 tax year. Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with DOF officials during and at the conclusion of this audit. A preliminary draft report was sent to DOF officials and discussed at an exit conference held on October 19, 2011. On November 1, 2011, we submitted a draft report to DOF officials with a request for comments. We received a written response from DOF officials on November 17, 2011. DOF officials agreed that 64 hotels and 20 room remarketers in operation did not file HROTX. DOF officials stated that letters to the 64 entities have been mailed out, and responses are being analyzed as they become available. In addition, DOF officials stated that the 20 entities identified as remarketers will be contacted by DOF to determine whether the entities are required to remit HROTX.

DOF did not agree with the audit calculation of \$1.8 million in hotel tax due from the 64 hotels during the audit period. DOF stated that hotels with fewer than 10 rooms have an occupancy rate of approximately 55 percent, significantly below the rate for larger size hotels. By applying the 55 percent rate across the board, DOF determined that the potential hotel tax

payable during the audit period is \$1.2 million. DOF stated the 55 percent rate is based on “a review of filings for a recent annual period.” However, DOF never indicated which specific year it was referring to and never provided this review to the audit team. As a result, the analysis could not be replicated and the information could not be verified. We, therefore, have no basis to assess DOF’s estimate.

Additionally, as DOF is aware, in making the reported estimates, auditors did not include interest and penalties associated with late and non-filers. Based on information provided by the agency, DOF can expect to assess between \$596,000 (based on \$1.2 million) and \$895,000 (based on \$1.8 million) in interest and penalties. When interest and penalties are included, we estimate that, for these 64 hotels, DOF can anticipate additional tax collections between \$1.79 million (using DOF’s estimates) and \$2.69 million (using auditors’ estimates) during the audit period.

Nevertheless, regardless of the exact figure, the important point is that DOF has stated it agrees that outstanding HROTX should be recouped and has begun to perform either a follow-up limited scope audit or a field audit of the entities identified in this audit.

The full text of DOF’s response is included as an addendum to this report.

FINDINGS AND RECOMMENDATIONS

DOF collected HROTX from 1,076 hotels totaling \$374 million for the June 1, 2009–May 31, 2010 tax year. However, we noted the following significant internal control weaknesses regarding DOF’s HROTX collection practices that, if corrected, could increase collections.

DOF did not maintain a complete list of all hotels that are required and authorized to collect the HROTX. Also, DOF did not ensure that all hotel operators and room remarketers commencing business, or opening new hotels, file a Certificate of Registration within three days after the commencement or opening. We noted several internal control weaknesses regarding DOF’s HROTX collection practices that resulted in 92 hotels owing \$8,894,040 in HROTX. Eighty-four of the 92 hotels—64 hotels and 20 room remarketers—in operation did not file HROTX. The remaining eight hotels filed HROTX returns. However, we estimate that they under-reported HROTX by \$1,278,918 from June 1, 2009, through May 31, 2010.

We estimate that the 64 hotels⁶ owe \$1,821,058 for the June 1, 2009–May 31, 2010 tax year. We further estimate that these 64 hotels owe \$7,615,122 from the year the hotel began business through the 2010–2011 hotel tax year.⁷ We were unable to estimate the amount of uncollected HROTX from 20 room remarketers because the number of rooms and rates for these remarketers was not available.

Additionally, DOF did not maintain copies of all the Certificates of Registration received from hotel operators and the returned Certificates of Authority when a hotel ceases business. Maintaining these documents would facilitate the tracking of new hotels whose operators should be collecting and remitting tax or hotels that may have changed operators (and the new operators that should be collecting and remitting tax).

DOF did not have a tracking system for all hotels to identify the estimated HROTX amount due from each hotel. As a result, DOF did not always identify hotels that reported a significantly lower amount of HROTX collected than we estimate should have been collected. Based on our analysis, we question whether eight of the 92 hotels reported the entire amount of the HROTX collected. As noted above, we estimate that they under-reported HROTX by \$1,278,918 from June 1, 2009, through May 31, 2010.

DOF did not maintain a tracking system of all of the returned Certificates of Authority when a business was discontinued or sold and did not link the hotel account identification number with the new number when a hotel changed names. Furthermore, DOF did not ensure that separate tax returns were filed for each hotel as required. DOF officials confirmed that one tax return was filed for several hotels on more than one occasion. DOF did not know how many locations were included in the tax return and was still researching this information during the course of this audit.

In an effort to reduce the redundancies in government, we believe DOF and the NYS Department of Taxation could streamline their process by coordinating efforts in collecting

⁶ See the Appendix at the end of this report for a list of the 64 hotels cited in this report.

⁷ This figure includes the \$1,821,058 we estimated for the 2009–2010 hotel tax year.

HROTX. Currently, hotels operating in New York City must apply for Certificates of Authority, collect the HROTX, and file tax returns separately from the New York State Sales Tax return. Because these businesses have already filed a Certificate of Authority with the State, DOF could request that the State collect the HROTX on behalf of the City as the State currently does with sales tax. This would not only save the personnel costs needed to monitor the collection for the City, but it would also relieve hotel operators of the extra costs of filing additional tax returns to the City.

These findings are discussed in detail in the following sections of this report.

Eighty-four Hotels Did Not Remit Hotel Tax and Eight Hotels Underreported Hotel Tax

Our review of DOF's procedures for monitoring and collecting HROTX found significant internal control weaknesses that resulted in 84 hotels—64 hotels and 20 room remarketers—in operation that did not file HROTX returns for the June 1, 2009–May 31, 2010 hotel tax year. DOF officials confirmed that these 84 hotels are non-filers and that correspondence audits will be conducted for each of these hotels. We estimate that the 64 hotels that did not collect HROTX owe \$1,821,058 for the 2009–2010 hotel tax year.

We further estimate that these 64 hotels owe \$7,615,122 from the year the hotel began business through the 2010–2011 hotel tax year.⁸ For those hotels that began business prior to the year 2000, the tax rates were not available. Therefore, we were unable to estimate HROTX owed.

DOF did not maintain a computerized tracking system that would have identified hotels that reported a significantly lower amount of HROTX collected when compared to the estimate that should have been collected based on number of rooms available, average rate charged per room, and occupancy rate for the year. Based on the number of rooms available, the room rate, and average occupancy rate of 84.76 percent⁹ for the 2009–2010 hotel tax year, we question whether eight additional hotels reported the entire amount of the HROTX collected. We estimate that these eight hotels under-reported HROTX by \$1,278,918 from June 1, 2009, through May 31, 2010, as shown in Table I. One of these hotels has filed for bankruptcy. We estimated that this hotel under-reported HROTX by \$66,547 for the last month of the 2009–2010 hotel tax year. DOF officials have not completed an audit assessment for this hotel, but informed us during the October 19, 2011, exit conference that this hotel owes over \$2 million in total unpaid HROTX beyond the 2009–2010 hotel tax year.

⁸ This figure includes the \$1,821,058 we estimated for the 2009–2010 hotel tax year.

⁹ NYC & Company reported the monthly occupancy rate.

Table I
Estimated Under-reported Tax for Eight Hotels
June 1, 2009, through May 31, 2010

Hotel Name ¹⁰	Estimated Tax Amount Due	Amount Paid
Hotel Number 1	\$20,869	\$10,920
Hotel Number 2 ¹	\$66,547	\$0
Hotel Number 3	\$307,702	\$55,277
Hotel Number 4	\$388,145	\$58,346
Hotel Number 5	\$74,424	\$0
Hotel Number 6 ²	\$57,156	\$10,974
Hotel Number 7 ²	\$36,434	\$0
Hotel Number 8 ²	\$327,641	\$21,029
Grand Total	\$1,278,918	\$156,546

¹Closed from 3/09-4/10. Our estimate is for May 2010 only. Hotel currently in bankruptcy. DOF officials told us that this hotel owes over \$2 million in HROTX.

²The hotel operator for these three hotels only paid \$5,000 per quarter. There is an outstanding liability of over \$440,000 that is currently being pursued by DOF.

The New York City Administrative Code, Chapter 25 Tax on Occupancy of Hotel Rooms, Section 11-2506 Determination of Tax indicates that if a return required to be filed is not filed, or if a return, when filed, is incorrect or insufficient, the amount of tax due shall be determined by the Commissioner of Finance from information obtained from the hotel operator. Notice of such determination shall be given to the person liable for the collection and/or payment of the tax.

Recommendations

DOF should:

1. Conduct audits of the 64 hotels identified in this report as non-filers.

DOF Response: “Finance agrees. Letters to the 64 entities have been mailed out, and responses are being analyzed as they become available. Depending upon the entity’s size and business complexity, Finance will perform follow-up limited scope audits by mail or a field audit.”

2. Conduct further reviews of the 20 room remarketers to determine whether they should be paying the HROTX and pursue actions for those deemed to be non-filers.

DOF Response: “Finance agrees. The 20 entities identified as remarketers will be contacted by DOF. As we do with all remarketers, Finance will review the responses and

¹⁰ At the request of DOF officials, we have redacted the names of these eight hotels. We are disappointed that DOF officials asked us to redact the names of these eight hotels as they included the name of one of the hotels in their response.

other information sources to determine whether the entities are required to remit HROTX and audit those that are not current with their HROTX obligations.”

3. Ensure that each non-filer completes a Certificate of Registration; DOF can then issue a Certificate of Authority to these businesses.

DOF Response: “Finance agrees. Entities currently operating as a hotel or as a remarketer will be sent a Certificate of Registration. Upon receipt and execution of the Certificate of Registration, Finance will issue a Certificate of Authority to the operator and/or remarketer.”

4. Recoup all outstanding HROTX due from all hotel operators that did not file HROTX.

DOF Response: “Finance agrees that outstanding HROTX due should be recouped. Finance does not agree with the Comptroller’s estimate of the amount of hotel tax at issue.

The Comptroller claims that \$1.8 million in hotel tax is due from the 64 hotels during the audit period, using the advertised room rate and an 84.76% occupancy rate. The 84.76% occupancy rate (based on overall industry statistics) used to estimate tax due does not take into account that smaller hotels, such as bed and breakfasts, generally have a much lower overall occupancy rate. A review of filings for a recent annual period, for example, shows that hotels with fewer than 10 rooms had an occupancy rate of approximately 55%, significantly below the rate for larger-size hotels. Finance’s occupancy rate is derived from occupancies that are subject to the HROTX, which in general is lower than occupancy rates based on industry data. Assuming the occupancy rate across the board is as high as 55% and these are all active hotels, the potential hotel tax payable during the audit period is \$1.2 million. Even when rooms are occupied, the occupancies are not necessarily taxable. The occupancy rate used by the Comptroller does not correct for exempt occupancies, such as those by government representatives or charitable organizations, or long term occupancies, which are not subject to HROTX. By overstating the taxable occupancy rate, the audit report overstates the amount of tax that could be collected from the 64 entities.”

Auditor Comment: DOF did not provide any information to support its analysis. Despite being provided ample opportunity during the course of the audit, DOF did not share a copy of its review nor make auditors aware of its existence until its final response. Auditors, therefore, did not have an opportunity to review and validate DOF’s estimate. As auditors shared their methodology and calculations with DOF throughout the course of the audit, it is unclear why DOF did not reciprocate, particularly if it believed its methodology was more accurate.

Additionally, as DOF is aware, in making the reported estimates, auditors did not include interest and penalties associated with late and non-filers. Based on information provided by the agency, DOF can expect to assess between \$596,000 (based on \$1.2 million) and

\$895,000 (based on \$1.8 million) in interest and penalties. When interest and penalties are included, we estimate that, for these 64 hotels, DOF can anticipate additional tax collections between \$1.79 million (using DOF's estimates) and \$2.69 million (using auditors' estimates) during the audit period.

Nevertheless, regardless of the exact figure, the important point is that DOF has stated it agrees that outstanding HROTX should be recouped and has begun to perform either a follow-up limited scope audit or a field audit of the entities identified in this audit.

5. Implement a tracking system that includes, but is not limited to, the following:

- Hotels that have submitted a Certificate of Registration
- Hotels that have received a Certificate of Authority
- Hotel Business Name and Address as well as the name of the Corporation that owns the hotel
- Hotels' HROTX filing status, and
- An estimated HROTX amount due for each hotel required to submit HROTX.

DOF Response: "Finance partially agrees. Finance already tracks the information in the first four bullets in our database, although we track the corporate operator of the hotel, not the owner of the property if they are different entities. The property owner is not relevant information for hotel tax enforcement. We are reviewing whether we can change procedures to do a better job of ensuring that missing information is routinely captured in our database. Finance recently sent out a mailing to update its list of active hotel operators and to register those that have HROTX filing obligations. We plan to update the HROTX return to better link the facility address with a hotel's corporate name and address and will populate the address in the database to the extent that information is missing.

Concerning identifying audit targets for under-reporting or non-reporting HROTX, our approach is to build models to target likely candidates. Our modelers and audit-selection screening staff generally include an estimated amount of tax due to help the Audit division to prioritize the use of resources. For hotels, key variables in estimating tax due are location, size and amenities provided."

Auditor Comment: We disagree with DOF's response. The tracking system does not identify the total number of Certificates of Registration that are issued or Certificates of Authority that are issued and/or returned.

6. Conduct audits of the eight hotels mentioned in this report that under-reported the amounts of HROTX due and recoup any additional amounts owed.

DOF Response: "Finance partially agrees. Finance had already performed hotel tax audits of four of the eight hotels identified by the Comptroller as under-reporting hotel tax before the audit began. The JFK Plaza Hotel has filed for bankruptcy protection and

the City submitted its claim for additional tax due with the bankruptcy court. We are also performing a follow up audit covering the administrative claim post-bankruptcy filing.

The four remaining hotels on the list will be reviewed and the appropriate audit methodology will be determined. As indicated in our response to recommendation No.4, we believe the estimated tax amount due is overstated.”

The internal control weaknesses are described in the following sub-sections of this report.

DOF Did Not Maintain a Complete List of Hotels

DOF largely relies on hotel operators to notify it that there is a new hotel opening so that DOF can issue the new establishment a Certificate of Authority. As previously mentioned in this report, we independently identified 64 hotels and 20 room remarketers that were not collecting and remitting to DOF the HROTX. Hotel operators do not always send DOF the Certificate of Registration stating a new hotel has opened. Therefore, DOF does not always know when a new hotel opens. As a result, DOF does not establish a new account identification number to track payments for a new hotel.

DOF cannot readily identify all hotel accounts by hotel name or address; therefore, it cannot track outstanding HROTX efficiently and effectively. As a result, DOF did not maintain a complete list of active hotels required to collect the HROTX. We requested a list of hotels that are required to collect the HROTX. In response to that request, DOF provided eight different incomplete lists of hotels. Even after eight different attempts, DOF’s active lists of hotels did not always list the name and address of the hotel as it is doing business as; instead, it listed the hotel by corporate name and address. For example, a hotel doing business in Brooklyn did business under one name and had an address in Brooklyn, but the list and tax return filed were under a different name and had a corporate address in Maryland. Until we were able to obtain copies of the Certificate of Registration and Certificate of Authority, we were unable to link the corporate name with the name the hotel was doing business as. Without that link, it would be impossible to determine that the hotel was paying the HROTX. DOF’s current list of active hotels makes it very difficult to determine if all hotels identified from various internet websites and other publications, including the AAA Tour Book and NYC Visitor Guide, are on DOF’s current list.

Recommendations

DOF should:

7. Utilize computer matches through various internet sources as well as review publications such as the AAA Tour Book and the NYC Visitor Guide annually for new hotels to ensure the list is up-to-date.

DOF Response: “Finance partially agrees. The Internet and guidebooks can be useful tools for uncovering non-filers and Finance has and will continue to explore the possibility of using these tools. In addition, Finance has utilized matches of sales tax, property tax and hotel tax data to detect non-filers.”

8. Periodically assign staff to research and update the list of active hotels required to collect the HROTX annually and ensure that the list has the name and address of the hotel as it is doing business as.

DOF Response: “Finance partially agrees. Finance plans to update the HROTX return to better link the facility address with a hotel’s corporate name and address and will populate the address in our database of active hotels to the extent that information is missing.

The database and Certificate of Authority already contain an entity’s address, corporate name, and additional names of the hotel and operator, such as DBA (‘Doing Business As’). As we identify missing information for any entity, the information will be added to the database.”

DOF Did Not Maintain all Documentation

DOF did not enforce the Local Law¹¹ that all hotel operators and room remarketers commencing business or opening new hotels must file a Certificate of Registration within three days after the commencement or opening. Without a Certificate of Registration, DOF cannot issue a Certificate of Authority empowering the hotel operator and room remarketers to collect the HROTX. As a result, many hotel operators and room remarketers are operating without having the New York City Certificate of Authority to collect HROTX.

Specifically, we identified 642 out of 1,076 hotels from DOF’s lists of hotels that did not have a Certificate of Registration and/or a Certificate of Authority. In addition, 186 of the 1,076 hotels were missing the date on the Certificate of Registration and/or the Certificate of Authority. Our visits to 130 of the hotels not on DOF’s list found that 125 hotels did not have the New York City Certificate of Authority.

The New York State Department of Taxation and Finance requires all businesses that operate in New York to collect and pay sales and use taxes.¹² Each business must have a valid Certificate of Authority from the Tax Department, which must be displayed.¹³ There is a civil penalty of \$50 if a business fails to display the State’s Certificate of Authority. In addition, any business that fails to surrender the State’s Certificate of Authority once a notice of revocation or suspension becomes final is subject to fines up to \$500 for the first day of such failure, plus up to \$200 for each subsequent day the certificate is not returned, not to exceed \$10,000.¹⁴ Currently, there are no penalties in New York City if a hotel does not display the City’s Certificate of Authority, if a hotel does not return the City’s Certificate of Authority when a business is discontinued or sold, or if there is a change in business entity.

¹¹ Local Laws of the City of New York for the Year 2009 No. 43, Section 11-2514, Registration, indicates that every hotel operator and room remarketer is required to file a Certificate of Registration with DOF within three days after commencing business.

¹² Sales tax applies to retail sales of certain tangible personal property and services. Use tax applies if you buy tangible personal property and services outside the State and use it within New York State.

¹³ Tax Law, sec. 1145(a)(4)

¹⁴ Tax Law, sec. 1145(a)(3)(ii)

Recommendations

DOF should:

9. Ensure that each hotel operator files a Certificate of Registration; DOF can then issue a Certificate of Authority to businesses that need it.

DOF Response: “Finance partially agrees. Finance is in the process of updating its database of Certificates of Registration. Finance is requesting the certificate from active hotel operators that have failed to file one. On an ongoing basis, whenever a new hotel files its first HROTX return a Finance Account ID # is assigned and a Certificate of Registration is mailed to the hotel. If a hotel does not complete and return the certificate, we send a reminder letter.”

There is no statutory authority to impose a penalty for noncompliance.”

10. Seek legislative approval that allows DOF the right to impose penalties on hotels for not obtaining, displaying, or returning the Certificate of Authority from New York City.

DOF Response: “Finance supports this recommendation.”

DOF Did Not Maintain a Tracking System of Returned Certificates of Authority

DOF did not maintain a tracking system to monitor returned Certificates of Authority when a business is discontinued or sold, which would facilitate the identification of new hotel operators that would be subject to collecting and remitting hotel occupancy taxes. DOF officials informed us that when a hotel is closed or sold, the hotel operator does not always return the Certificate of Authority to DOF. If a business returns a Certificate of Authority to DOF, then DOF files it in the “Returned Mail HTX/HTXB Certificates of Authority” folder. The hotel account identification numbers are not linked with the new numbers when a hotel changes names.

DOF’s “Returned Mail HTX/HTXB Certificates of Authority” folder only included a total of 17 Certificates of Authority. Eight of these accounts were replaced with new account identification numbers; however, they were not linked to the new hotel operator. For example, information for the following hotels was not linked:

- One hotel in Brooklyn was sold to a new owner, who changed the name of the hotel. DOF was sending letters to the original owner and not to the new owner. DOF did not notify the Hotel Tax Audit unit that the old owner had stopped filing tax returns so that a search could identify that a new hotel was operating. As a result, the new owner did not have a New York City Certificate of Authority and was not filing a tax return or paying the HROTX for two years.

- One hostel in Manhattan changed its name. Then the new name was changed again to a third name. According to DOF officials, the hostel under the third name is owned by an operator that filed tax returns and made tax payments under the third name. However, DOF did not provide the copies of the Certificates of Authority or any other documentation verifying that the third name and the hotel operator were the same.
- Another hotel in Manhattan also changed its name. According to DOF officials, the original hotel name was owned by the same operator we cited in the previous bullet. This operator filed tax returns and made tax payments under the new name. However, DOF did not provide the copies of the Certificates of Authority or any other documentation for the new name to verify that the hotel was the same.

The New York City Department of Finance Certificate of Authority indicates:

“This Certificate of Authority will become void if you sell or discontinue the business or change the business entity. You must complete and submit the following information, along with the original Certificate of Authority to the New York City Department of Finance, Automated Tax Processing Unit, Hotel Tax Section, 59 Maiden Lane, 18th Floor, New York, NY 10038 within 20 days of the change.”

DOF does not impose a penalty for operating a hotel with a Certificate of Authority that was filed by the prior owners under a different hotel name.

Recommendations

DOF should:

11. Include in its tracking system (as mentioned in Recommendation #5):

- a record of returned Certificates of Authority when a business is discontinued or sold
- a link for each hotel account by the hotel address so that when a hotel changes the name, ownership, or other corresponding information, it can be flagged, and
- the ability to flag hotels that stop filing HROTX returns.

DOF Response: “Finance partially agrees. Finance is updating its database to ensure that it includes such information as the issuance date and if applicable the termination date of Certificate of Authority.

A new Certificate of Authority is not required based on a change of name, only on a change of legal identity (change of EIN). Account identification numbers are always linked to the Employer Identification Number (EIN), even when a name has changed.

However, when the hotel changes its name and notifies the Department, our records will be updated to reflect the name change in our database.

Finance already flags hotels that stop filing returns. If a hotel stops filing HROTX for two consecutive quarters, Finance automatically creates a delinquency case for further investigation. When the hotel is out of business, Finance generally receives no response and the account becomes delinquent. Finance staff can be assigned to conduct a field visit to the last known place of business of any taxpayer with HROTX delinquencies to ascertain whether the delinquent taxpayer is still active or has terminated operations, or a new taxpayer is doing business.

Finance plans to update the HROTX return to better link the facility address with a hotel's corporate name and address and will populate the address in the database to the extent that information is missing.”

12. Seek legislative approval that allows DOF the right to impose penalties on hotels that operate with a Certificate of Authority that was filed by the prior owners under a different hotel name.

DOF Response: “Finance supports this recommendation”

Separate Tax Returns Were Not Always Filed for Each Establishment

Contrary to requirements, combined hotel room occupancy tax returns were filed for various establishments. One operator, for example, filed one New York City HTX Hotel Room Occupancy Tax Return for various establishments. Therefore, we were unable to determine which hotels filed a tax return and the total amount of HROTX collected by each establishment. DOF officials informed us that one hotel we could not originally identify was included with this operator. In addition, DOF officials informed us that another *NYC HTX Hotel Room Occupancy Tax Return* was filed for two other hotels that we could not originally identify.

The New York City Department of Finance's *NYC HTX Hotel Room Occupancy Tax Return for Use by Operators and Room Remarketers* indicates that quarterly returns must be filed for each establishment for each three-month period ending on the last days of August, November, February, and May of each tax year and must be filed within 20 days of the end of the period they cover. The legal name, facility address, city and state, zip code, business telephone number, taxpayer's e-mail address, EIN/SSN (Employer Identification Number/Social Security Number), account identification, period beginning, period ending, due date, and federal business code are required on the tax return. DOF officials confirmed that each establishment is required to submit a separate HROTX return.

Recommendations

13. DOF should ensure that separate tax returns are filed for each hotel as indicated on the *New York City Department of Finance NYC HTX Hotel Room Occupancy Tax Return for Use by Operators and Room Remarketers*.

DOF Response: “Finance agrees. Finance already requires hotels to file a separate return. Our records show only one instance in the past when Finance permitted consolidated filing and in that case a hotel was permitted to do consolidated filing by the State Department of Taxation and Finance.”

14. DOF should ensure a single return is filed by each room remarketer as indicated on the *New York City Department of Finance NYC HTX Hotel Room Occupancy Tax Return for Use by Operators and Room Remarketers*.

DOF Response: “Finance agrees. Finance already enforces the requirement of a Room Remarketer to file a single return.”

Other Issue

In an effort to reduce the redundancies in government, we believe DOF and the NYS Department of Taxation (the State) could streamline their process by coordinating efforts in collecting HROTX. Currently, hotels operating in New York City must apply for Certificates of Authority on behalf of the City and State, collect the HROTX, and file HROTX returns separately from their New York State Sales Tax return. This is a redundant and arduous practice for hotel operators. Currently, hotel operators report hotel room occupancy “taxable sales” to the State. This is the amount that is subject to New York State’s Sales and Use Tax that hotel operators pay to the State. Instead of filing separate tax returns, we believe that DOF should coordinate with the State in order to allow the hotel to file one HROTX return on behalf of both the City and the State for those hotels located within the City. This option would relieve hotel operators of the costs of filing multiple tax returns.

Recommendations

DOF should:

15. Share the information from this Audit Report with the State.

DOF Response: “Finance agrees.”

16. Coordinate with the State to jointly enhance the collection process of hotel occupancy taxes by the City and the State.

DOF Response: “Finance and the NYS Department of Taxation & Finance (T&F) have discussed areas where sales tax and NYC HROTX audits can be coordinated, and we will

continue to explore the possibility of conducting joint audits. Finance and T&F staff meet regularly to discuss areas where tax collection procedures can be streamlined, and we will review sales tax-HROTX issues with T&F.

However, the proposal to allow a hotel located in the City ‘to file one HROTX return on behalf of the City and the State’ is presented but not analyzed in the Comptroller’s report. Issues regarding the broader tax base hotels are subject to under the sales tax compared to the HROTX and tax law differences (for example, the criteria for establishing permanent residency) need to be examined as part of the analysis. In addition, if the proposal entails NYS collection of the HROTX on behalf of the City, issues regarding NYS administrative expense charges to the City must also be reviewed. The State has increased the charge for administering the City’s Personal Income Tax from approximately \$30 million to \$80 million over the past decade, even though the number of electronic filers has increased and the work involved has diminished.”

DETAILED SCOPE AND METHODOLOGY

We conducted this performance audit in accordance with generally accepted government auditing standards. 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. This audit was performed in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

This audit covered HROTX collection filings from June 1, 2009, through May 31, 2010. To gain an understanding of the policies, procedures, and the remittance of tax due to New York City governing HROTX collection practices, we reviewed the Tax Policy and Planning Division Office of Tax Audit Policy and Procedure Manual, Local Laws of The City of New York for the Year 2009 No. 43, New York City Administrative Code Chapter 25 Tax on Occupancy of Hotel Rooms, Rules of the City of New York Title 19 Department of Finance Section 12, and various Finance Memorandums. In addition, we interviewed key DOF personnel from the Automated Tax Processing Unit, Payment Operations Division, Audit Division, and Collections Department.

We reviewed and analyzed all Certificates of Registration Pertaining to Hotel Room Occupancy Tax (COR) and Certificates of Authority (COA) from DOF's files. We determined whether CORs and COAs for all hotels included on DOF's list of active hotels were on file with DOF. Then we determined whether the hotel name and address indicated on the CORs and COAs corresponded to the hotel name and hotel address indicated on DOF's list of active hotels. Also, we determined whether the CORs indicated the "Certificate Date." In addition, we determined whether the COAs indicated the "Date Issued."

We attempted to independently develop as complete a list as possible of hotels operating in New York City for the purposes of determining whether DOF was collecting HROTX from all hotels. We obtained the AAA NY Tour Book and the NYC Visitor Guide Spring 2010. We conducted searches of various internet websites including www.booking.com, www.google.com, www.hotelguides.com, and www.bedandbreakfast.com to identify additional hotels. We also obtained a listing of establishments classified as hotels from the Department of Environmental Protection.

In addition, we obtained from the New York State Liquor Authority's website a list of all hotels that were issued hotel liquor and hotel wine licenses.

Using all of the above sources, we compiled a list of 631 hotels in New York City.

DOF provided eight different incomplete lists of hotels. Five of the eight lists included the hotel name, address, and identification number which DOF uses to track hotel information, hotel name or corporate name, and either the hotel address or the corporate address. The remaining three lists contained the amount of HROTX paid by each hotel from June 1, 2009, through May 31, 2010. Using all eight lists, we compiled a list of 1,076 hotels in New York City. Our review of DOF's list of hotels by name and address found 11 hotels were not included on DOF's list of hotels that paid

HROTX during the June 1, 2009– May 31, 2010 hotel tax year. On March 11, 2011, DOF officials told us that two of the hotels were not filing HROTX. The remaining nine hotels paid their HROTX under a different corporate name.

We then compared our list of 631 hotels that we independently developed to DOF's lists of 1,076 hotels to determine whether the 631 hotels were included on any of DOF's lists. Although we found 419 hotels on at least one of DOF's lists, we were unable to match 212 hotels from our list to any of DOF's lists. We then conducted further research and removed 59 shelters and hotels that either were closed or were not in business during our scope period. We submitted the remaining 153 hotels not on DOF's lists and requested that DOF provide an explanation why these hotels were not included on any of DOF's lists. By reviewing DOF files, we also determined whether these hotels had a New York City Department of Finance Certificate of Authority. We then conducted field visits to 130 out of the 153 hotels to verify whether these hotels were open for business. During our field visits, we asked the hotel staff at each location to provide us with the rates and the number of rooms for the hotel for the June 1, 2009–May 31, 2010 hotel tax year.¹⁵ We did not visit 18 of the remaining 23 hotels on our list because they were remarketers that offer rooms through the internet and do not always have an address in New York City. The remaining five hotels were found through additional research after our site visits in May and submitted to DOF on June 27, 2011.

DOF was able to provide our office with supporting documentation for 61 out of the 153 hotels. We accepted DOF's results for these 61 hotels. We estimate that nine hotels under-reported HROTX. At our exit conference, DOF officials provided us with the tax returns for one of the nine hotels, reducing our number to eight hotels that we estimated under-reported HROTX. DOF officials confirmed that the remaining 83 hotels—63 hotels and 20 room remarketers—on our list were non-filers and will be scheduled for DOF correspondence audits, bringing the total to 65 hotels that did not file HROTX for the June 1, 2009–May 31, 2010 hotel tax year. At our exit conference, DOF officials told us one of the hotels on our list did not qualify as a hotel under the definition of a hotel, which thus reduced our number of hotels that did not file HROTX from 65 to 64 hotels.

For the 2009–2010 hotel tax year, we independently determined the estimated amount of uncollected HROTX for the 64 hotels DOF officials confirmed were non-filers. We obtained the rates and the number of rooms from various hotel websites. In addition, we used the rates and the number of rooms obtained from hotel staff during our field visits at each hotel. We used DOF's *NYC HTX Hotel Room Occupancy Tax Return* as a guide to compute the tax rate per room and day and the additional 5.875 percent tax due of the total rents. Then we used the average occupancy rate of 84.76 percent and average daily room rates, which we obtained from NYC & Company, Inc., to calculate the estimated tax due. Our tests did not include an estimate of the amount of uncollected HROTX from the 20 room remarketers because we were unable to verify the number of rooms they rented or the prices they charged for renting rooms acting as intermediaries for hotel operators.

¹⁵ If the rates and the number of rooms for the June 1, 2009–May 31, 2010 tax year were not available, then we obtained the current information from hotel websites.

For the 64 hotels that did not file HROTX, we then determined how far back they should be assessed for not paying HROTX in the previous tax years¹⁶ by determining when the entities established businesses. We reviewed various sources, such as internet websites, earliest reviews, New York City Department of Finance Office of the City Register, and New York State (NYS) Department of State Division of Corporations Entity Information (<http://dos.state.ny.us>). We used the dates that were most reliable for our calculations as follows:

- For *Date Opened* we used the information on an internet website, which indicated the date the hotel opened.
- For *Earliest Review*, we used this date only if the earliest review date (done by an independent reviewer or hotel review website) was prior to our audit scope, which was June 1, 2009. If the earliest review date was earlier than the corporation date, we used the corporation date because it is possible that a different corporation previously ran the establishment. If the earliest review date was after the corporation date, we used the earliest review date because we could not determine whether the hotel was in operation prior to a review date or if the hotel was under construction, not in operation, etc.

We determined whether or not we should estimate beyond the two-year HROTX period of June 1, 2009–May 31, 2011 by reviewing the use of the building. We compared the number of units in each building as indicated on NYCityMap to the number of units rented as a hotel, bed and breakfast, etc. If it appeared that the corporation or individual only used one or two units in a larger building, then *no prior year estimates were calculated*. If it appeared that the corporation or individual used at least 90 percent of the units located at that building, we then calculated estimates as follows:

- For *Corporation Date*, we determined when that corporation took over the deed/mortgage for that location from New York City DOF Office of the City Register website, and we used that date for the date opened for our estimate.
- For *Individual Date*, we determined when that individual took over the deed/mortgage for that location from New York City DOF Office of the City Register website, and we used that date for the date opened for our estimate.

¹⁶ We did not estimate any taxes owed prior to the year 2000 because we did not have the hotel occupancy rate or the room rates prior to January 2000.

List of 64 Hotels that Have Not Filed HROTX

	Name of Lodging	Borough	Estimated HROTX Owed
1	287 Hoyt Street	Brooklyn	\$8,182.26
2	Chelsea Apartments	Manhattan	\$15,062.16
3	Chelsea Central Apartments/ Chelsea West 23rd Street Apartments/ Elite City Stays-Chelsea	Manhattan	\$159,138.16
4	Dream Apartments	Manhattan	\$25,435.07
5	East Village Avenue C Apartments	Manhattan	\$41,345.09
6	Gramercy Studio East	Manhattan	\$5,402.88
7	Greenpoint Guest House/ Dwell 76	Brooklyn	\$9,346.60
8	NYC Hudson Rooms West 48th	Manhattan	\$195,621.82
9	Park View Apartments	Manhattan	\$15,913.82
10	Rivington Apartments-Nolita	Manhattan	\$51,406.27
11	Stay Smart NYC 126 Lexington Avenue	Manhattan	\$5,576.59
12	United Nations Apartments	Manhattan	\$29,239.81
13	Upper West Side 71st Street Apartments	Manhattan	\$49,093.55
14	A & G Bed & Breakfast	Brooklyn	\$146,931.65
15	Auberge St. Marc, St. Marks Inn	Staten Island	\$82,831.94
16	Dekoven Suites	Brooklyn	\$58,131.63
17	Fort Place Bed & Breakfast	Staten Island	\$33,596.75
18	Hartshorne House	Staten Island	\$32,945.22
19	Imhotep Bed & Breakfast	Brooklyn	\$128,272.10
20	Midwood Suites	Brooklyn	\$145,533.94
21	Minetta Suites	Manhattan	\$707,273.11
22	Serenity at Home	Brooklyn	\$21,093.26
23	Soho Bed and Breakfast	Manhattan	\$67,129.02
24	The Harlem Flop House	Manhattan	\$98,275.09
25	The Sofia Inn/ Bed & Breakfast Marisa	Brooklyn	\$163,604.96
26	Tony's Place Upper Westside	Manhattan	\$77,199.03
27	Victorian Bed and Breakfast of Staten Island	Staten Island	\$104,852.39
28	Victorian Villa	Staten Island	\$75,977.21
29	Blue Moon Hotel	Manhattan	\$575,949.48
30	Central Park Hostel/The Central Park Hostel	Manhattan	\$373,202.18
31	Central Park House	Manhattan	\$31,626.40
32	Chelsea Center Hostel/ Chelsea Center Eastside	Manhattan	\$18,477.32
33	Lefferts Manor	Brooklyn	\$39,270.05
34	New York Bed and Breakfast	Manhattan	\$95,856.65
35	Prince Hotel	Brooklyn	\$298,211.73
36	The International Cozy Inn	Manhattan	\$35,010.75
37	East Village Suites	Manhattan	\$178,761.13
38	Elite City Stays Central Park East	Manhattan	\$65,906.95
39	Elite City Stays Financial District/ Financial District Apartments	Manhattan	\$46,279.16
40	Elite City Stays Greenwich Village/ Village Apartments	Manhattan	\$41,492.46
41	Elite City Stays Park Ave. Midtown	Manhattan	\$65,906.95
42	Elite City Stays Theater District	Manhattan	\$23,837.16
43	Elite City Stays Timesquare	Manhattan	\$189,302.11
44	Elite City Stays Turtle Bay	Manhattan	\$23,837.16
45	Elite City Stays United Nations	Manhattan	\$46,279.16
46	Elite City Stays United Nations 307 East	Manhattan	\$32,953.48

	Name of Lodging	Borough	Estimated HROTX Owed
47	Elite City Stays West 69th Street and Central Park West /One Bedroom 69th Street	Manhattan	\$14,841.09
48	Elite City Stays-Midtown	Manhattan	\$92,558.32
49	Glenwood Hostel/ One Henderson Management	Brooklyn	\$233,528.67
50	Gorgeous Apartments	Manhattan	\$74,201.20
51	Hostel 104	Manhattan	\$314,810.51
52	Hotel Name Redacted from Final Report ¹	Brooklyn	\$263,164.41
53	Original Beauty Apartments	Manhattan	\$103,862.52
54	Pink Hostels (Females Only)	Manhattan	\$41,075.75
55	Pink in the City Hostel (Females Only)/ 201 West 87 LLC	Manhattan	\$168,512.06
56	Regent Hotel/ Queens Blossom Corp	Queens	\$370,861.19
57	Studio 75 at Riverside	Manhattan	\$196,154.60
58	Guesthouse	Manhattan	\$74,428.64
59	Honey's Bed and Breakfast	Brooklyn	\$50,936.69
60	New York Hostel 99	Manhattan	\$187,994.15
61	Sylvan Heights Guest House	Manhattan	\$70,647.63
62	The Fort Greene Apartments	Brooklyn	\$71,920.64
63	The Missing Lantern Urban Inn	Brooklyn	\$55,764.44
64	Bowery Grand Hotel	Manhattan	\$493,287.95
			\$7,615,122.12

¹ Number 52, the name of this hotel was redacted for this Final Audit Report the dollar amount listed in the table is an actual audit assessment amount from DOF, not an estimate.



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November 17, 2011

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Sent via e-mail: tkim@comptroller.nyc.gov

**Re: Audit Report on the Department of Finance's Hotel Room
Occupancy Tax Collection Practices (FP11-084A)**

Dear Deputy Comptroller Kim:

Introduction

During the audit period of June 1, 2009 – May 31, 2010, the City collected \$374 million in hotel tax from 1,076 hotels. The Department of Finance's hotel tax audit group audits all large hotels on a multi-year cycle, ensuring that the vast majority of hotel tax revenue owed the City is identified and collected.

The Comptroller's audit team identified 64 entities that did not file hotel tax and advertise rooms to travelers. These are apparently a mix of businesses, including individuals offering stays in their apartments and smaller hotels. While the amount at issue is small (the Comptroller's team estimates that an additional 0.5% of total hotel tax revenue could have been collected during the audit period), the Department of Finance will follow up with these entities. As explained below, the amount that could be collected is approximately \$1.2 million, assuming all the entities are active hotels, and not the \$1.8 million estimated by the audit team.

Finance currently identifies non-filers by matching potential hotels against sales and property tax data and by contacting entities that remitted taxes in the past to determine whether the entity is still active. In order to detect non-compliance by the type of small hotels or individuals offering rooms for rent that were the focus of the audit, Finance is looking at various additional strategies, including the use of models to identify the characteristics of non-filers and periodic reviews of Internet room listings. Our goal is to identify the most efficient method to detect non-compliance without moving audit resources away from higher value audit targets.

Room remarketers are a group that only recently became subject to the hotel tax on the mark-ups charged on hotel room rentals. Given their

importance in the growth of on-line bookings, the Department of Finance is exploring multiple strategies to identify and collect from the remarketers that are not currently registered.

Other suggestions by the audit team are already part of Finance procedures or would require a change in law, as indicated in the responses to the specific findings.

1 - Conduct audits of the 64 Hotels identified in the report as non-filers

Finance agrees.

Letters to the 64 entities have been mailed out, and responses are being analyzed as they become available. Depending upon the entity's size and business complexity, Finance will perform follow-up limited scope audits by mail or a field audit.

2 – Conduct further reviews of the 20 room remarketers to determine whether they should be paying the HROTX and pursue actions on those deemed to be non-filers

Finance agrees.

The 20 entities identified as remarketers will be contacted by DOF. As we do with all remarketers, Finance will review the responses and other information sources to determine whether the entities are required to remit HROTX and audit those that are not current with their HROTX obligations.

3 – Ensure that each non-filer completes a Certificate of Registration; DOF can then issue a Certificate of Authority to those businesses

Finance agrees.

Entities currently operating as a hotel or as a re-marketer will be sent a Certificate of Registration. Upon receipt and execution of the Certificate of Registration, Finance will issue a Certificate of Authority to the operator and/or remarketer.

4 – Recoup all outstanding HROTX due from all hotel operators that did not file HROTX.

Finance agrees that outstanding HROTX due should be recouped. Finance does not agree with the Comptroller's estimate of the amount of hotel tax at issue.

The Comptroller claims that \$1.8 million in hotel tax is due from the 64 hotels during the audit period, using the advertised room rate and an 84.76% occupancy rate. The 84.76% occupancy rate (based on overall industry statistics) used to estimate tax due does not take into account that smaller hotels, such as bed and breakfasts, generally have a much lower overall occupancy rate. A review of filings for a recent annual period, for example, shows that hotels with fewer than 10 rooms had an occupancy rate of approximately 55%, significantly below the rate for larger-size hotels. Finance's occupancy rate is derived from occupancies that are subject to the HROTX, which in general is lower than occupancy rates based on industry data. Assuming the occupancy rate across the board is as high as 55% and these are all active hotels, the potential hotel tax payable during the audit period is \$1.2

million. Even when rooms are occupied, the occupancies are not necessarily taxable. The occupancy rate used by the Comptroller does not correct for exempt occupancies, such as those by government representatives or charitable organizations, or long term occupancies, which are not subject to HROTX. By overstating the taxable occupancy rate, the audit report overstates the amount of tax that could be collected from the 64 entities.

5 – Implement a tracking system that includes, but is not limited to, the following:

- Hotels that have submitted a Certificate of Registration.
- Hotels that have received a Certificate of Authority.
- Hotel business name and address as well as the name of the corporation that owns the hotel.
- Hotels HROTX filing status, and,
- An estimated HROTX amount due for each hotel required to submit HROTX

Finance partially agrees.

Finance already tracks the information in the first four bullets in our database, although we track the corporate operator of the hotel, not the owner of the property if they are different entities. The property owner is not relevant information for hotel tax enforcement. We are reviewing whether we can change procedures to do a better job of ensuring that missing information is routinely captured in our database. Finance recently sent out a mailing to update its list of active hotel operators and to register those that have HROTX filing obligations. We plan to update the HROTX return to better link the facility address with a hotel's corporate name and address and will populate the address in the database to the extent that information is missing.

Concerning identifying audit targets for under-reporting or non-reporting HROTX, our approach is to build models to target likely candidates. Our modelers and audit-selection screening staff generally include an estimated amount of tax due to help the Audit division to prioritize the use of resources. For hotels, key variables in estimating tax due are location, size and amenities provided.

6 – Conduct audits of the eight hotels mentioned in this report that under-reported the amount of HROTX due and recoup any additional amount owed.

Finance partially agrees.

Finance had already performed hotel tax audits of four of the eight hotels identified by the Comptroller as under-reporting hotel tax before the audit began. The JFK Plaza Hotel has filed for bankruptcy protection and the City submitted its claim for additional tax due with the bankruptcy court. We are also performing a follow up audit covering the administrative claim post-bankruptcy filing.

The four remaining hotels on the list will be reviewed and the appropriate audit methodology will be determined. As indicated in our response to recommendation No.4, we believe the estimated tax amount due is overstated.

7 – Utilize computer matches through various internet sources, as well as review publications such as the AAA Tour Book and the NYC Visitor Guide, annually for new hotels to ensure the list is up to date.

Finance partially agrees.

The Internet and guidebooks can be useful tools for uncovering non-filers and Finance has and will continue to explore the possibility of using these tools. In addition, Finance has utilized matches of sales tax, property tax and hotel tax data to detect non-filers.

8 – Periodically assign staff to research and update the list of active hotels required to collect the HROTX annually and ensure that the list has the name and address of the hotel that is doing business as.

Finance partially agrees.

Finance plans to update the HROTX return to better link the facility address with a hotel's corporate name and address and will populate the address in our database of active hotels to the extent that information is missing.

The database and Certificate of Authority already contain an entity's address, corporate name and additional names of the hotel and operator, such as DBA ("Doing Business As"). As we identify missing information for any entity, the information will be added to the database.

9 – Ensure that each hotel operator files a Certificate of Registration; therefore, DOF can then issue a Certificate of Authority from New York City.

Finance partially agrees.

Finance is in the process of updating its database of Certificates of Registration. Finance is requesting the certificate from active hotel operators that have failed to file one. On an ongoing basis, whenever a new hotel files its first HROTX return a Finance Account ID # is assigned and a Certificate of Registration is mailed to the hotel. If a hotel does not complete and return the certificate, we send a reminder letter.

There is no statutory authority to impose a penalty for noncompliance.

10 – Seek Legislative approval that allows DOF the right to impose penalties on hotels for not obtaining, displaying or returning the Certificate of Authority from New York City.

Finance supports this recommendation.

11 – Include in its tracking system (as mentioned in Recommendation # 5):

- A record of returned Certificates of Authority when a business is discontinued or sold
- A link for each hotel account by the hotel address so that when a hotel changes the name, ownership or other corresponding information, it can be flagged.
- The ability to flag hotels that stop filing HROTX returns

Finance partially agrees.

Finance is updating its database to ensure that it includes such information as the issuance date and if applicable the termination date of Certificate of Authority.

A new Certificate of Authority is not required based on a change of name, only on a change of legal identity (change of EIN). Account identification numbers are always linked to the Employer Identification Number (EIN), even when a name has changed. However, when the hotel changes its name and notifies the Department, our records will be updated to reflect the name change in our database.

Finance already flags hotels that stop filing returns. If a hotel stops filing HROTX for two consecutive quarters, Finance automatically creates a delinquency case for further investigation. When the hotel is out of business, Finance generally receives no response and the account becomes delinquent. Finance staff can be assigned to conduct a field visit to the last known place of business of any taxpayer with HROTX delinquencies to ascertain whether the delinquent taxpayer is still active or has terminated operations, or a new taxpayer is doing business.

Finance plans to update the HROTX return to better link the facility address with a hotel's corporate name and address and will populate the address in the database to the extent that information is missing.

12 – Seek Legislative Approval that allows DOF the right to impose penalties on hotels that operate with a Certificate of Authority that was filed by the prior owners under a different hotel name.

Finance supports this recommendation

13 – DOF should ensure that separate tax returns are filed for each hotel as indicated on the NYC Department of Finance NYC Hotel Room Occupancy Tax Return for use by Operators and Room Remarketers.

Finance agrees.

Finance already requires hotels to file a separate return. Our records show only one instance in the past when Finance permitted consolidated filing and in that case a hotel was permitted to do consolidated filing by the State Department of Taxation and Finance.

14 – DOF should ensure a single return is filed by each Room Remarketer as indicated on the New York City Department of Finance NYC HTX Hotel Room Occupancy Tax Return for use by Operators and Room Remarketers

Finance agrees.

Finance already enforces the requirement of a Room Remarketer to file a single return.

15 – Share information from this Audit Report with the State

Finance agrees.

16 – Coordinate with the State to jointly enhance the collection process of hotel occupancy taxes by the City and the State

Finance and the NYS Department of Taxation & Finance (T&F) have discussed areas where sales tax and NYC HROTX audits can be coordinated, and we will continue to explore the possibility of conducting joint audits. Finance and T&F staff meet regularly to discuss areas where tax collection procedures can be streamlined, and we will review sales tax-HROTX issues with T&F.

However, the proposal to allow a hotel located in the City “to file one HROTX return on behalf of the City and the State” is presented but not analyzed in the Comptroller’s report. Issues regarding the broader tax base hotels are subject to under the sales tax compared to the HROTX and tax law differences (for example, the criteria for establishing permanent residency) need to be examined as part of the analysis. In addition, if the proposal entails NYS collection of the HROTX on behalf of the City, issues regarding NYS administrative expense charges to the City must also be reviewed. The State has increased the charge for administering the City’s Personal Income Tax from approximately \$30 million to \$80 million over the past decade, even though the number of electronic filers has increased and the work involved has diminished.

Sincerely,



Elizabeth Botwin

cc: George Davis III, Deputy Director, Mayor's Office of Operations
Michael Hyman, Deputy Commissioner, Tax Policy and Planning
Andrew Salkin, Deputy Commissioner, Operations
Celia Carino, Director, Internal Audit