FREDERICK COUNTY
INTERAGENCY INTERNAL AUDIT AUTHORITY

FREDERICK COUNTY
HOTEL RENTAL TAX EXAMINATION
FOR THE PERIOD
JULY 1, 2007 THROUGH JUNE 30, 2009

Report# 10-06
June 16, 2010

TABLE OF CONTENTS

I. Introduction

Internal Audit (IA) conducted this attestation examination in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the examination to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our examination objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our examination objectives.

This report is intended to provide information to management; however, it is also a matter of public record, and with the exception of any applicable disclosure exemptions, distribution should not be limited. Information extracted from this report may also serve as a method to disseminate information to the public as a reporting tool to help citizens assess government operations. Management responsible for the functional area reviews the report, and their formal written responses are incorporated into the final report per IIAA policy and generally accepted government auditing standards.

It is management's responsibility to design and implement an adequate system of internal control, and it is the Internal Audit Division's responsibility to determine if management's system of internal control is functioning properly in relation to the audit objectives. It is also management's responsibility to decide if action should be taken in response to any reported recommendations, taking into consideration related costs and benefits. Management, therefore, assumes the risk of making the decision not to implement any reported recommendations.

II. Background

The Hotel Rental Tax was established as a result of the Frederick County Government's Ordinance No. 04-11-355. The ordinance was approved and adopted on July 15, 2004, with an effective date of August 2, 2004. This tax was enacted to provide a source of funding to the Tourism Council of Frederick County, Inc. (Tourism Council). Prior to the tax, the Tourism Council was largely funded directly from Frederick County's General Fund. Specifically, the ordinance states that the Hotel Rental Tax revenue will first be used to pay for administrative costs incurred by the County in collecting the tax. The balance is then to be paid to the Tourism Council, with a portion of the balance to be used for a visitor center.

Prior to the establishment of Ordinance No. 04-11-355, the Tourism Council entered into a Memorandum of Understanding (MOU) with the Board of County Commissioners (BoCC), dated June 15, 2004. This MOU provided guidelines that the Tourism Council would be required to follow, if a Hotel Rental Tax were to be established. One such requirement was that 5% of the net tax collections for fiscal years 2005 and 2006 would be designated for the Tourism Council's new visitor center. This requirement increased to 10% of the net tax collections for all subsequent fiscal years.

The MOU also stipulated that the Tourism Council would be required to create a program by which non-profit organizations within Frederick County may apply for funding from the Hotel Rental Tax in order to help promote tourism. The Tourism Council established the Tourism Resources Invested in Promotion and Product (TRIPP) program, whereby organizations can apply for such funding on an annual basis. The Tourism Council Board approves the annual amount to be used for the TRIPP program and the percentage of allocated funds used for advertising and development. The Tourism Council entered into another MOU with the BoCC on June 28, 2007. This MOU outlined the amount of debt service for the construction of the new visitor center and stated the County will deduct an amount equal to one-twelfth of the annual debt service each month from the Hotel Rental Tax collections.

On a monthly basis, hotels within the County are required to pay the Treasurer of Frederick County their balance of the Hotel Rental Tax collected from patrons. Once the revenue is received, the Accounting Department records the revenue and calculates the administrative fee to be retained by the County. Administrative fees are estimated at the beginning of the fiscal year. At the end of each fiscal year, beginning with FY09, actual administrative costs are calculated and any adjustments are made to the next fiscal year collections. For the period of this examination, the administrative fee rate was 2.46% of gross collections which totaled $2,214,299 ($1,112,564 for FY08 and $1,101,735 for FY09). From the net collections, Accounting records the visitor center allocation, the debt service allocation, and the balance of Hotel Rental Tax revenue to be paid to the Tourism Council in the County's PeopleSoft financial system. A check along with a spreadsheet explaining how the monthly amount was derived is sent to the Tourism Council for their share of the monthly receipts.

In addition to expenditures resulting from the construction and renovation of the new visitor center, as well as everyday operations, the Tourism Council uses the revenue generated from the Hotel Rental Tax to fund its TRIPP program. Non-profit organizations may apply for two types of awards provided by this program: advertising and development. The applicant must submit a complete application by the deadline, as well as a marketing plan for the project that they want to fund through the TRIPP program. The Tourism Council's selection committee chooses applicants that are most deserving and meet the overall guidelines of promoting tourism within Frederick County. Once funding is approved for an organization, the type of award stipulates how the funding is distributed. The organization must contribute a match of funds in order to receive an award from the Tourism Council, as stipulated by their award agreement.

III. Objective, Scope, and Methodology

The objective of this examination was to issue a conclusion on the Tourism Council's compliance with all laws, regulations, agreements and procedures related to Hotel Rental Tax revenues and expenditures. This examination was focused on areas specifically mentioned either by the June 15, 2004 Memorandum of Understanding, namely the TRIPP program and visitor center funds, or by Ordinance No. 04-11-355.

Specifically we determined:

- Whether Hotel Rental Tax revenues were recorded properly.
- If operating and TRIPP expenses were properly approved, appropriate, and allowable in accordance with applicable laws and/or regulations, agreements, and Tourism Council procedures.
- If the appropriate amounts of Hotel Rental Tax revenue were being set aside for the visitor center and related expenditures were approved, appropriate, and allowable in accordance with applicable laws and/or regulations, agreements, and Tourism Council procedures.

The scope of this examination covers Hotel Rental Tax revenues, the Tourism Council's operating, TRIPP, and Visitor Center expenditures for the period July 1, 2007 through June 30, 2009.

During the planning phase of this examination, we analyzed Hotel Rental Tax revenues, associated fees, and allocations for fiscal years 2006, 2007, 2008, and 2009. The results showed an increase between fiscal years 2006 and 2007 as the economy was still thriving. After that, each year revenues gradually declined due to a downturn in economic events.

Our methodology also included:

- Verifying that tax collections from individual hotels as reported on County summary reports agreed with amounts used to calculate payments due to the Tourism Council.
- Verifying that the amounts paid by the County to the Tourism Council agreed with the amounts recorded in PeopleSoft and were accurately deposited in their bank account.
- Recalculating each month's withholding of the administrative fees and visitor center allocations.
- Verifying that the Tourism Council set aside the proper amount for the visitor center.
- Testing a sample of 30 operating expenses, 15 TRIPP expenses (including both advertising and program development expenses), and 5 visitor center construction expenses to ensure that the expenses were properly approved, appropriate and allowable. Additionally, for the TRIPP expenditure sample, we verified that the appropriate amount of awardees' match was received and that the funding amount did not exceed the fiscal year's maximum allowable amount.

IV. Audit Results

Based on our examination of Hotel Rental Tax revenues and expenditures for fiscal years 2008 and 2009, we conclude that the Hotel Rental Tax revenues are being recorded properly. Also, our testing showed that expenditures of the Hotel Rental Tax revenues for operating, TRIPP program, and visitor center purposes were approved, appropriate and allowable in accordance with applicable laws and/or regulations, agreements, and Tourism Council procedures. Our testing also showed that the Tourism Council set aside appropriate amounts of Hotel Rental Tax revenue for the visitor center. Our sample testing yielded no exceptions.

However, in reviewing the Tourism Council's policies and procedures, we found that their document retention policy is not sufficient to meet Hotel Tax examination requirements. Although all documents were available for the examination period, should the Tourism Council follow their current document retention policy and procedures (Policy Section 2d), adequate supporting documentation may not be available to conduct the required Hotel Rental Tax examination. The examination is required every two years, and the Tourism Council's policies allow for the destruction of some documents, such as bank statements, after one year.

We recommend that the Tourism Council research recommended document retention procedures and consult with their accounting firm to review the policy/procedures. We also recommend the Tourism Council change the current policy/procedures to coincide with recommended practices and maintain records long enough to meet examination requirements.

V. Summary of Response

On May 18, 2010, the Tourism Council's Executive Director provided a written response (see attached) to our May 10, 2010 draft report. He agreed with our recommendation to review and revise the data retention policy and procedures and informed us that the Tourism Council's Board of Directors has already taken action. A new policy was adopted on May 14, 2010 to ensure that records continue to be maintained long enough to meet examination requirements. Specifically, accounting documentation now has to be retained for four years. This action is responsive to our recommendation. No further action is needed.

Interagency Internal Audit Authority

June 16, 2010 Interagency Internal Audit Authority

ATTACHMENT

Tourism Council of
Frederick County, Inc.
MARYLAND

May 18, 2010

Kelly Hammond, CICA
Audit Manager
Internal Audit Division
Frederick County Government
30 N. Market St.
Frederick, MD 21701

Dear Ms. Hammond:

Thank you for the opportunity to respond to the Discussion Draft of the Frederick County Hotel Rental Tax Examination for the period of July 1, 2007 through June 30, 2009.

The Tourism Council of Frederick County (TCFC), Inc. has no issue with the audit results.

We do concur with Internal Audit's recommendation about document retention. TCFC adopted its first formal document retention policy in November 2008 in anticipation of then pending IRS Form 990 standards. The policy was one of several that were researched at the time by examining what other nonprofit organizations were doing. We missed the obvious issue of needing retention guidelines to ensure that records that are needed biannually by Internal Audit would be retained long enough to be available when the examination begins. As the IA recommendation noted, all documents needed for this examination were available.

The TCFC Board of Directors has already taken action on this recommendation, adopting a revised Document Retention and Destruction Policy on May 14, 2010, using guidelines suggested by local CPA firms which call for some longer retention periods. The new policy will ensure that records continue to be maintained long enough to meet examination requirements.

Sincerely,

John J. Fieseler
Executive Director

Enc.

Cc: George Wunderlich, TCFC Board President
Mike Irons, TCFC Board Treasurer
Barbara Lindberg, TCFC Accountant

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Document Retention and Destruction Policy

This Document Retention and Destruction Policy of The Tourism Council of Frederick County identifies the record retention responsibilities of staff, volunteers, members of the Board of Directors, and outsiders for maintaining and documenting the storage and destruction of the Organization's documents and records.

1. **Rules.** The Organization's staff, volunteers, members of the Board of Directors and outsides (i.e., independent contractors via agreements with them) are required to honor these rules: (a) paper or electronic documents indicated under the terms for retention below will be transferred and maintained by the Human Resources, Legal or Administrative staffs/departments or their equivalents; (b) all other paper documents will be destroyed after three years; (c) all other electronic documents will be deleted from all individual computers, data bases, networks, and back-up storage after one year; and (d) **no paper or electronic documents will be destroyed or deleted if pertinent to any ongoing or anticipated government investigation or proceeding or private litigation.**

2. Terms for Retention.

a. Retain permanently:

Governance records – Charter and amendments, Bylaws, other organizational documents, governing board and board committee minutes.
Tax records – Filed state and federal tax returns/reports and supporting records, tax exemption determination letter and related correspondence, files related to tax audits.
Intellectual property records – Copyright and trademark registrations and samples of protected works.
Financial records – Audited financial statements, attorney contingent liability letters.

b. Retain for ten years:

Pension and benefit records – Pension (ERISA) plan participant/beneficiary records, actuarial reports, related correspondence with government agencies, and supporting records.
Government relations records – State and federal lobbying and political contribution reports and supporting records.

c. Retain for seven years:

Accounting - Accounts payable and receivable ledges and schedules, cancelled checks, (with exception of important payments), contracts, mortgages, notes and leases which have expired, garnishments, inventories, invoices, notes receivable ledges and schedules, payroll records and summaries, terminated personnel files, purchase orders, sales records, cancelled stock and bond certificates, subsidiary ledgers, time books/cards, withholding tax statements and vouches for payments to vendors, employees, etc. (includes allowances and reimbursements of employees, officers, etc., for travel and entertainment expenses.)
Insurance - Accident reports/claims (settled cases)

d. Retain for four years:

Accounting - Bank reconciliations and statements, duplicate deposit slips, expired insurance policies, petty cash vouchers, and sales commission reports

e. Retain for three years:

Employee/employment records – Employee names, addresses, social security numbers, dates of birth, INS Form I-9, resume/application materials, job descriptions, dates of hire and termination/separation, evaluations, compensation information, promotions, transfers, disciplinary matters, leave/comp time/FMLA, engagement and discharge correspondence, documentation of basis for independent contractor status (retain for all current employees and independent contractors and for three years after departure of each individual).

Lease, insurance, and contract/license records – Software license agreements, vendor, hotel, and service agreements, independent contractor agreements, employment agreements, consultant agreements, and all other agreements (retain during the term of the agreement and for three years after the termination, expiration, non-renewal of each agreement).

f. Retain for two years:

All other electronic records, documents and files – Correspondence files (other than legal and important matters), past budgets, publications, and survey information.

3. **Exceptions**. Exceptions to these rules and terms for retention may be granted only by the Organization's chief staff executive or President of the Board.

4. **Destruction Policy**

Boxes prepared and sent to records storage have a description of the contents in the box, delivered with each box. This description is also stored in an electronic file. Similar documents with the same retention periods are grouped together in boxes. Every two years these are reviewed and those which need to be destroyed are shredded.

Revised May 11, 2010
Adopted by Board of Directors May 14, 2010