



INTERNAL AUDIT REPORT

Municipal Accommodation Tax Audit

January 2024

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CONCLUSION AND SUMMARY

The Property Tax and Assessment division of Financial Services is responsible for administering the Municipal Accommodation Tax (MAT) collected by hotels and short-term rental (STR) operators. Economic Development is the liaison between the hotel operators and the City and stays updated on occupancy trends. By-law and Compliance, Licensing and Permit Services (BCLPS) is responsible for ensuring STR applicants meet all licensing requirements including registering for a MAT account. The audit identified opportunities to improve the administration and oversight of the MAT program by:

- Developing a program to validate operator MAT submissions.
- Ensuring technology is fully leveraged to restrict input errors, improve communication between integrated systems and facilitate management oversight.
- Developing standard operating (SOPs) procedures and service level agreements (SLAs) with departmental stakeholders.
- Ensure staff have resources to provide sufficient administration and oversight over the MAT program.

The collection of MAT is dependent on the occupancy and room rate data submitted by accommodation providers to the City of Vaughan. The City does not have a process in place to validate that the hotel operators' information is accurate, as the operators are not required to submit their reports to the City. In addition, the City has not collected all MAT revenue that was due. Not collecting all outstanding MAT financially impacts the amount of funding available to the Tourism Vaughan Corporation and for other City initiatives. There are opportunities to validate MAT revenue by having operators provide the City with documentation to support their submissions. Other mechanism that could provide further assurance would be through continuous monitoring, spot checks, and audits.

Software was developed to administer the MAT program. However, there are system design issues within the software, such as the system allowing multiple MAT numbers to be assigned to a property and the absence of control features within the free-form fields that have led to data integrity issues. The audit has also identified issues with the design of the process for assigning MAT account numbers to hotel and STR operators. Prospective operators are required to register for a MAT account prior to license approval, rather than having the MAT number assigned to the operator by City staff upon license approval. Both issues have impacted management's ability to manage the program in an efficient and effective manner. Although the MAT system is integrated with the AMANDA system, there are further opportunities to integrate pertinent data, such as license expiry dates. Leveraging technology to provide more complete information in an automated manner may increase the efficiency and effectiveness over the administration of the MAT program.

Properly developed SOPs provide guidance and knowledge transfer to accomplish operational duties. SLAs facilitate communication and expectations between entities. In the case of the MAT program, Financial Services, Economic Development, and BCLPS have interconnected MAT

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activities, yet there is little communication among the departmental stakeholders. Defining staff roles, responsibilities and accountability and developing formal SOPs and SLAs will help facilitate more effective and efficient operations.

Opportunities exist for management to re-evaluate the current resources that are available to ensure the MAT program deliverables and objectives are achievable. This may include analyzing the sufficiency of resources:

- BCLP requires to license operators and enforce the relevant By-Laws.
- Financial Services requires to perform MAT related reconciliation and collection activities.
- For the technology investments required to improve the internal and external stakeholder experience.

Both the City of Toronto (effective May 1st, 2023) and the City of Mississauga (effective January 1st, 2024) increased their Municipal Accommodation Tax rate on transient accommodations from 4% to 6% per cent. Opportunities exist for the City of Vaughan to perform additional analysis to determine whether the City's 4% MAT rate remains effective.

This audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*.

Internal Audit will follow up on the status of outstanding management action plans related to this audit and will report the status to a future Audit Committee meeting.

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BACKGROUND

On November 23, 2017, the Province of Ontario issued the Transient Accommodation Regulation 435/17 which came into force December 1, 2017 and provides the necessary provisions for municipalities across Ontario to implement a Municipal Accommodation Tax (MAT). By-law 029-2019 was approved by Council on March 19, 2019 and came into effect on April 1, 2019. This By-law requires accommodation providers to collect and submit a standard rate of 4 per cent for daily stays to the City. As of April 1, 2020, the MAT was expanded to licensed short-term rentals. Currently in Vaughan, the annual initial licensing fee for STRs is \$360 and up to approximately \$12,000 for an STR broker. During the pandemic, Council approved a temporary suspension of collection and remittance of MAT that lasted from March 2020 until September 1, 2020.

It is estimated that the City could collect more than \$3 Million annually without increasing local residents' taxes through the MAT program. From 2020 through the end of 2022, the City has collected approximately \$4.7 million in MAT. Fifty per cent of the net income collected from MAT is used to fund destination development and marketing in the City. The remaining 50 per cent is to be used at the City's discretion through the budgeting process.

OBJECTIVES AND SCOPE

The objective of the audit was to evaluate the adequacy and effectiveness of the internal controls, processes, and procedures in place to mitigate the business risks associated with the administration and oversight over the Municipal Accommodation Tax program.

The audit scope includes assessing that:

- Strategic plans are appropriately developed, implemented, and monitored, and align with the City's strategic initiatives and priorities.
- There is adequate management oversight, ensuring the proper execution of the Property Tax and Assessment operations.
- Key performance indicators have been developed and management tracks, monitors, and reports on the critical success factors.
- Policies and procedures are regularly reviewed, updated, and applied consistently.
- Information Technology systems are being leveraged and used to their maximum capabilities.

The scope of the audit covered the Municipal Accommodation Tax activities for the period of January 2021 to August 2023.

This audit was conducted in Conformance with the *International Standards for the Professional Practice of Internal Auditing*.

Auditor and Author: Rebecca Burchert, Audit Project Manager

Director: Kevin Shapiro CIA, CFE, CRMA

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DETAILED REPORT

1. *Develop a Program to Validate MAT Submissions*

By-law 029-2019 and By-law 183-2019 outline the authority the Chief Administrative Officer, City Treasurer or designate to administer, enforce and collect MAT. These By-laws also include the requirements of accommodation providers to submit scheduled occupancy data, MAT payment and maintain business records. The By-laws state that hotel and short-term rental operators (STR) can be subject to interest and/or penalties for late or non-payment and for concealing or falsifying information.

The City acquired a new software to administer the MAT program. Phase 1 of the 12 Floor MAT system development for hotels was \$72,772. A second phase was required to accommodate the STRs at a cost of \$87,642.

Hotel and STR operators submit monthly or quarterly occupancy, room rates and MAT collected using the City's website. The MAT system calculates 4% of the revenue the operator received and creates an invoice which is then paid via on-line banking or by cheque.

Currently, the MAT system does not have the functionality for the operators to upload reports to support their submissions, nor does the City require that they be submitted in any manner. The Cities of Toronto, Mississauga and Barrie follow the same process. However, they conduct regular operator audits with the assistance of an external firm. The City of Vaughan has yet to establish such a program. COV By-law 029-2019 section 20 states "The City, or its agent, may inspect and audit all books, documents, transactions, and accounts of the Providers and require the Provider(s) to produce copies of any documents or records required for the purposes of administering and enforcing this By-law". In addition, COV By-law 183-2019 section 10(2) states "The City, or its designate, may inspect and audit all books, documents, transactions, and accounts of Short-Term Rental Owner(s), Short-Term Rental Operator(s), and Short-Term Rental Brokerage(s) and require them to produce copies of any documents or records required for the purposes of administering and enforcing this By-law."

The Tourism Vaughan Corporation (TVC) is a beneficiary of 50% of the net revenues from the MAT collected. KPMG performs annual assurance that the TVC is using the funding to exclusively develop, promote and market Vaughan as a leading destination for tourism, leisure and business travel with the emphasis on promoting overnight stays. But the overall materiality of MAT collected has not made the revenue a priority for the City to include in KPMG's financial audit plan of the City of Vaughan. However, from 2020 through the end of 2022, the City has collected approximately \$4.7 million in MAT, \$2.4 million of which was in 2022.

In addition, the audit identified that not all MAT revenue owing has been collected. Observation #3 provides additional details. Without procedures in place to reconcile revenue received to what is expected and to validate the revenue reported by hotel and STR operators, there is a risk that the City may continue to not identify and collect all the MAT that is owed.

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Enhancing the MAT system with the ability for hotel operators to upload occupancy reports or having the operators email their reports to the City would provide further opportunities for the City to validate operator submissions on an ongoing basis. The MAT program would benefit from complete or periodic audits of the City of Vaughan's accommodation providers. It's important to perform assurance procedures to validate that operators are adhering to the municipal By-laws and the City is receiving all MAT revenue that is owed, to support TVC and other City initiatives.

Recommendations

We recommend that management:

- Ensure operators provide backup to the City to support their MAT submissions.
- Develop a program to conduct audits of operator MAT submissions.

Management Action Plan

Management agrees with these recommendations.

OCIO and Financial Services will engage the software vendor (12th Floor) to confirm the feasibility, cost and the requirements to allow operators to upload the backup to support their MAT submissions. Where feasible and budget permitting, this will be implemented by Q4 2025. Stakeholder consultation will be performed to determine what is possible on the operations side. Any additional resources required for review and analysis will be requested in the 2025 budget.

City staff will explore options for retaining an external auditing company to develop a process for auditing operating MAT submissions in a cost effective manner by Q4 2024.

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2. *Ensure Technology is Fully Leveraged to Restrict Input Errors, Improve Communication Between Integrated Systems and Facilitate Management Oversight*

Submitting occupancy data and remitting payments are similar for both hotel operators and STRs. However, the registration for an STR MAT account is different. By-law 158-2019 places the onus on the prospective STR operator to obtain a MAT account prior to applying for a license to operate as an STR. Registering for an STR MAT number is a two-step process. The prospective STR operator completes an on-line application, then the system sends an email to the applicant with a confirmation link. Once the application is confirmed, the MAT system issues a MAT number. Once the property is licensed, the AMANDA system updates the MAT system and the account changes from pending to licensed. Registration and submission instructions are posted on the City's website. The audit noted several issues with the process and the technology that supports it:

- The process of requiring prospective operators to receive a MAT number before applying for an STR license results in more MAT numbers being issued than necessary. Some applicants are refused a license or abandon the process before being licensed.
- The MAT system issues a unique MAT number upon each request. The result is multiple MAT numbers can be and were assigned to a single property. One scenario where this can occur is when the STR operator has forgotten their login credentials and creates a new MAT account rather than using the 'forgot password' function.
- The MAT application function has free-form fields but does not restrict an applicant from making errors, such as inserting a phone number in the address field. MAT administrators can still run reports by filtering and manually extracting pertinent information, but it is less efficient and input errors are problematic for accurate reporting.
- The STR license expiry date is not available in current MAT reporting making it difficult and time consuming to accurately report the number of actively licensed STR properties at any one point in time.
- The AMANDA STR report does not include the MAT account number which limits BCLPS' ability to effectively communicate or correlate with their Financial Services partners.

Enhancing the system and improving the application process would help improve the experience for both operators and City staff.

Recommendations

We recommend that management:

- Redesign the process so that City staff assign an operator a MAT account/number upon being initially licensed and update the relevant By-law, accordingly.

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- Work with the Office of the Chief Information Officer and software vendor to restrict the risk of input errors and restrict the system's ability to assign multiple MAT numbers to the same property.
- Improve integration between the MAT and AMANDA systems for meaningful reporting to facilitate oversight and decision making.

Management Action Plan

Management agrees with these recommendations.

Financial Services, OCIO and BCLPS will review the STR process to determine if the process can be reworked without disrupting the process for hotel operators by Q4 2025.

Financial Services and OCIO will review and investigate the feasibility with the vendor. Assessment will be made to determine if the cost of adjusting will provide the recommended benefit by Q2 2025. Any additional resources will be requested in the 2025 budget.

Financial Services, and BCLPS will work with OCIO to include required fields and address reporting gaps in both MAT and Amanda systems by Q4 2025.

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3. *Develop Standard Operating Procedures and Service Level Agreements with Departmental Stakeholders*

Standard Operating Procedures (SOPs) are established methods of carrying out operational activities. To be effective they should identify roles and responsibilities, provide expectations and guidance to achieve operational objectives.

Financial Services does not have formalized SOPs. They rely on process maps and the content of relevant By-laws. However, these documents do not provide instruction on operational activities such as how MAT administrators assess MAT submissions for reasonableness, use available data to detect late and non-payments, apply interest to delinquent accounts, collect on arrears and evoke the right to audit.

An SLA provides reciprocal commitments between partners. Although the administration and oversight of the MAT program involves the operations of Financial Services, Economic Development and BCLPS, there is little communication between the departments.

The audit noted two significant findings which may have been prevented if there were properly developed SOPs and SLAs.

A hotel operator had not made a MAT submission to the City since Q2 2020. The MAT system notes indicated that the hotel was closed during the COVID-19 pandemic. Financial Services did not conduct any validation for the closure or follow-up on the status of the hotel. Economic Development has access to third party data which identifies hotel occupancy and industry trends. They also have access to the MAT system but only obtain quarterly financial summaries for budgeting purposes. If there had been communication and sharing of information between Financial Services and Economic Development, Financial Services may have been aware that the hotel reopened in Q4 2022. Upon Internal Audit's discovery, the hotel operator was contacted by Financial Services, and the hotel operator subsequently submitted all the outstanding MAT to the City. However, Financial Services did not charge the hotel operator interest for the late submissions as permitted under the City's By-law.

BCLPS is responsible for licensing STR operators and brokerages. The only STR broker licensed to operate in Vaughan is Air BnB. BCLPS enforcement duties include monitoring the STRs which advertise on Air BnB's platform and ensuring they have current City issued licences. BCLPS's investigative tools include backdoor access to the Air BnB website and the broker's quarterly revenue reporting of STR properties that operated in Vaughan.

During the audit, it was discovered that in 2023, Air BnB began providing the City with a revenue report which contains all Vaughan properties which have earned revenue using their platform. Many of these properties have never made a MAT submission to the City. However, this report had not been shared with Financial Services. There is more than \$13,000 of known revenue from Q1 2023 alone, which remains uncollected.

BCLPS renews STR licences without confirming with Financial Services that STRs are in compliance with the STR MAT By-law, such as ensuring that the property has paid all outstanding MAT owing prior to renewing their license. If Financial Services communicated

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the status of MAT submissions, BCLPS's decision to issue an STR licence renewal would be based upon more complete information.

The audit also determined that there are other STR brokers who are operating in Vaughan without a licence. Only Air BnB is in the scope of BCLPS's investigative STR licensing enforcement.

There are financial, reputational and operational risks when roles, responsibilities and accountability are undefined and programs are administered without appropriate oversight.

Recommendation

We recommend that management:

- Define roles, responsibilities and accountabilities of internal stakeholders from Financial Services, BCLPS and Economic Development with respect to the administration and oversight over the MAT program.
- Develop SOPs for all MAT related processes, including but not limited to, assessing the reasonableness of MAT submissions, detecting late and missing payments, collecting on arrears and evoking the right to audit.
- Establish SLAs between Financial Services, Economic Development and BCLPS to foster communication and facilitate the administration, collection and application of MAT.
- Ensure that Financial Services is provided access to the Air BnB quarterly revenue report.
- Ensure Financial Services develops reconciliation processes for STR MAT revenue received versus what should be expected based on the Air BnB reports and develops collection processes for any unsubmitted STR MAT revenue.
- BCLPS confirms with Financial Services that a property has paid all outstanding MAT owing prior to renewing an STR license.
- BCLPS expand their investigation and enforcement efforts to ensure compliance with the relevant MAT By-laws.

Management Action Plan

Management agrees with these recommendations.

Draft policy and procedure documents have been developed for MAT by Financial Services and will be revised and updated as management action plans are completed in consultation with BCLPS and Economic Development. Roles and responsibilities will be defined in the draft MAT policy and operational activities will be captured in SOPs in Q4 2025.

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Currently there are no handoffs between the departments. Only the MAT registration and the STR application are somewhat dependent on each other. Both processes are initiated by the operator and departments have no control of when the processes are triggered. SLAs may be relevant to the completion of inspections and other tasks leading up to STR license approval. Communication between Financial Services, OCIO, BCLPS and Economic Development could be documented. SLA's will be developed for relevant processes by Q4 2025.

Financial Services staff will review with BCLPS how the City gets the Air BnB revenue report and determine the best way to direct to Financial Services by Q2 2024.

Financial Services will develop a reconciliation process for STR MAT revenue received versus expectations as indicated by the quarterly review of the Air BnB reports. Any additional resources required for review and analysis will be requested in the 2025 budget.

BCLPS and Financial Services will develop an approach to ensure that a property has paid all outstanding MAT owing prior to renewing an STR license. A potential solution would be to develop and grant BCLPS access to the MAT invoice and payment reports and submission reports. This will allow BCLPS access to information required without waiting to engage Financial Services reducing the turnaround time to the STR. Implementation is expected by Q3 2025.

BCLPS will perform a cost/benefit analysis for expanding their enforcement efforts and determine the economic feasibility and make the appropriate funding requests in the 2025 budget.

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4. *Ensure Staff Have Resources to Provide Sufficient Administration and Oversight Over the MAT Program*

In Vaughan, 50 per cent of net income collected from MAT is used to fund destination development and marketing in the City. The remaining 50 per cent is to be used at the City's discretion through the budgeting process.

Based on the issues identified in the previous three observations, it is imperative that management re-evaluate the current funding provided to ensure the MAT program deliverables and objectives are achievable. This may include analyzing the sufficiency of resources:

- BCLP requires to license operators and enforce the relevant By-Laws.
- Financial Services requires to perform MAT related reconciliation and collection activities.
- For the technology investments required to improve the internal and external stakeholder experience.

Both the City of Toronto (effective May 1st, 2023) and the City of Mississauga (effective January 1st, 2024) increased their Municipal Accommodation Tax rate on transient accommodations from 4% to 6% per cent. Opportunities exist for the City of Vaughan to perform additional analysis to determine whether the City's 4% MAT rate remains effective.

Recommendations

We recommend that management:

- Re-evaluate the current funding available to administer and provide oversight over the MAT program to ensure the program is best positioned to achieve its objectives.
- Evaluate the decisions made by other GTA municipalities with respect to their MAT rates and determine whether any changes are recommended for Vaughan.

Management Action Plan

Management agrees with this recommendation.

Financial Services, Economic Development and BCLPS will review the recommended funding requirements with Financial Planning and Development Finance and make the appropriate funding requests in the 2025 budget.

Economic Development and Tourism Vaughan will review recent increases in MAT rates in Mississauga and Toronto. Staff will assess and report the impact on Vaughan and any opportunities. Any change in rates will require Council approval, Q3 2024.