

AUDIT REPORT

Date:	June 16, 2020
Department:	City Manager
Subject:	Transient Lodging Tax (TLT)
Lead Auditor:	Dawn von Epp, Sr Internal Auditor

OBJECTIVE

This audit was conducted to determine whether:

- Transient Lodging Tax (TLT) revenues are used in accordance with applicable laws and contractual agreements.
- Reliable metrics are in place to measure program effectiveness.

SCOPE & METHODOLOGY

We conducted this audit in accordance with Generally Accepted Government Auditing Standards, which 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.

The scope of the audit was fiscal year (FY) 2019 and first quarter 2020. To accomplish our objective, we interviewed City and Visit Mesa staff, reviewed TLT fund distribution and other deliverables to confirm contract compliance, performed detailed tests of TLT funded expenditures, and analyzed Visit Mesa's performance metrics to verify they are supported, reliable, and recognized by the Destination Marketing Organization (DMO)/travel industry.

BACKGROUND & DISCUSSION

The City of Mesa (City) first levied a Transient Lodging Tax (a.k.a. Bed Tax) in November 1983 at a 2% rate, referred to at that time as Transient Occupancy Tax (TOT). The rate has changed over time, most recently in January 2011 to the current 5% rate. The Bed Tax is an added taxation on charges for temporary lodging (29 days or less) including associated charges for services and accommodations. The lodging operators (e.g., motels/hotels, short term vacation rentals, RV parks, etc.) collect the tax from those using their guest rooms and services and remit the money to the Arizona Department of Revenue, who in turn provides the City its portion. Arizona law also restricts the use of TLT; specifically, it requires the money be used exclusively for the promotion of tourism, and prohibits any expenditures used to influence the outcome of elections.

City staff places a portion of collected TLT into City accounts designated to support the operation and improvement of tourism related facilities, specifically, Hohokam and Cubs Spring Training facilities and the Mesa Convention Center. A small portion of TLT collections cover the administration of TLT distributions. The remainder of TLT is provided to Visit Mesa, the DMO the City has contracted with to promote Mesa tourism. The table below shows the TLT amounts collected and retained by the City and distributed to Visit Mesa during FY 2019 and FY 2020 Q1.

Transient Lodging Tax Distribution

FY	Visit Mesa	City	Total Collections
2019	\$2,915,798	\$1,652,199	\$4,567,996
Qtr 1, 2020	\$495,638	\$257,508	\$753,146

Visit Mesa puts extensive effort into advocating Mesa as the premier business and leisure travel destination. Like other DMOs, Visit Mesa uses tourism industry specific performance metrics to capture their efforts towards attracting tourism as well as the economic benefits derived from those efforts. Contractually, Visit Mesa is only required to report certain information to the City but also provides monthly, quarterly, and annual reports containing a multitude of metrics and data that capture the many facets of their efforts.

CONCLUSION

In our opinion, TLT revenues are used in accordance with state statutes; however, a lack of management oversight allowed some minor exceptions and occurrences of noncompliance with contract terms. Also, we determined metrics provided by Visit Mesa are predominantly reliable; however, additional metrics could be used to assist City staff in measuring program effectiveness. Our observations and recommendations are summarized below. For additional details, please see the attached Issue and Action Plan.

SUMMARY OF OBSERVATIONS & RECOMMENDATIONS

- 1. Observation:** The City does not have a monitoring process in place to evaluate Visit Mesa's compliance or performance.

Recommendations:

- 1-1 Monitor Visit Mesa's TLT funded expenses to verify compliance with state statutes and contract terms.
- 1-2 Monitor metrics to evaluate Visit Mesa's performance.
- 1-3 When negotiating contract deliverables, identify those that provide the most value and then monitor for compliance.
- 1-4 Establish a formal communication process including designating individuals who can authorize TLT spending and identifying key activities that should be communicated between both parties.

Issue and Action Plan #1

Issue #1: Monitoring procedures are not in place to evaluate compliance or performance.

Observation:

City staff does not monitor and evaluate Visit Mesa's use of TLT funds, compliance with state statutes and contract terms, or performance.

Had oversight been occurring, the following should have been identified:

- A small amount of TLT funded expenditures were used to help influence the outcome of the November 2018 election by promoting a yes vote on the Mesa Play's ballot questions; and for supporting an out of state scholarship program, a non-Arizona tourism related purpose. The quantity and amounts of these exceptions are considered immaterial; however, they have been identified due to the importance of complying with state statutes. The expenditures were as follows:
 - \$15.81 mileage reimbursement for an employee promoting the Mesa Play's ballot questions.
 - \$26.47 for publishing a coloring page prompting voters to vote yes on the Mesa Play's ballot questions.
 - \$250.00 contribution to a scholarship program for Cal Poly Pomona students sponsored by DMA West, a regional trade association in which Visit Mesa is a member. The scholarship honors a longtime contributor to the tourism industry and the option to contribute is selected and paid in conjunction with annual membership dues.
- The following contract terms were not fulfilled as specified:
 - The Community Relations budget specifies at least 15% of the "3% TLT Collection" will be spent on civic, community, or tourism project/events. Of the 15%, Attachment A of the contract requires that Visit Mesa spend \$129,000 for specific annual events with the remainder determined by Visit Mesa each year with City approval. However, the budgeted amounts did not match fixed organization/event amounts as stipulated in Attachment A.
 - Actual expenditures were not in alignment with the Community Relations budgeted amounts.
 - A deliverable detailing TLT expenditures and the results anticipated and achieved was not provided to the City.

- While not contractually required, Return on Investment (ROI) metrics provided for FY 2019 did not include all applicable investments.

Criteria:

The City's Contract Management Framework, Section 4.h Contract Management Process, stresses the importance of defining vendor performance measures and utilizing a plan to monitor those performance measures.

Arizona Revised Statutes include the following (summarized):

A.R.S. § 9-500.06 requires that TLT be used exclusively for the promotion of tourism.

A.R.S. § 9-500.14 prohibits a city from using its resources for the purpose of influencing the outcomes of elections.

The agreement between the City of Mesa and Visit Mesa contains terms that direct Visit Mesa to spend an established amount of TLT funds on City specified organizations/events, provide an annual Community Relations Budget identifying additional organizations and associated amounts to be spent (and spend those amounts accordingly), and to submit reports twice each year detailing expenditures and how they achieved anticipated results.

Comments:

Monitoring is a basic control to mitigate the risk of noncompliance with statutes and contract terms and ensure that performance expectations are being met. Compliance is imperative as the City is required to follow state statutes. Additionally, City staff would have identified noncompliance and inaccurate metrics if a monitoring process was in place.

A lack of formal communication between the City and the DMO, and multiple City staff providing varying directions, contributed to noncompliance findings. Improved communication between Visit Mesa and the City would help identify effective performance metrics and clarify required deliverables. Visit Mesa staff expressed concern with the difficulty in providing the contract deliverable related to reporting expenditures, as it involves separating TLT revenue from other revenues; yet, they do this for their annual Return on Investment metrics.

Recommendation(s) and Management's Action Plan(s): City staff should perform the following:

Recommendation #1-1: Monitor Visit Mesa's TLT funded expenses to verify compliance with state statutes and contract terms. This should be done in a timely manner so that any exceptions identified can be corrected.

Action Plan #1-1: Create an internal One Drive file to keep all contracts, activity reports and financials available to: City Manager, City Auditor and Tourism Team. In addition, staff will create an internal-only tracking tool to help keep of monitor contract needs and financial reporting milestones.

Individual or Position Responsible: Natalie Lewis and Mike Kennington.

Estimated Completion Date: Administrative tasks listed will be completed by end of Fiscal Year 19/20. As needed, the existing agreement will be continued monthly until new agreement is established. Goal is to complete new agreement Fall 2020.

Recommendation #1-2: Monitor metrics to evaluate Visit Mesa's performance.

Action Plan #1-2: Tourism Team to work with Visit Mesa to identify performance metrics that help the City better understand and share Visit Mesa's value and performance. Some examples to be considered, but not limited to, include: revenue and expenditure actuals vs. budgeted projections; or actualized room nights, tradeshow, numbers of attendees directly booked, secured by Visit Mesa.

Individual or Position Responsible: Natalie Lewis, Jaye O'Donnell, Marc Heirshberg, and Mike Kennington.

Estimated Completion Date: The performance metrics will be included in the updated agreement, when completed. Goal is for Fall 2020 completion, but no later than end of calendar year.

Recommendation #1-3: When negotiating contract deliverables and performance metrics, identify those that provide the most value,

as well as, the frequency in which they are desired. Follow-up with monitoring for compliance.

Action Plan #1-3: Tourism Team to work with Visit Mesa to identify and refine outcome deliverables (rather than task-related outputs) and that are meaningful to the City. One such deliverable may include meetings with City Management and Tourism Team to discuss tourism-related priorities for the City and potential Visit Mesa – City partnerships and action.

Individual or Position Responsible: Natalie Lewis, Jaye O'Donnell, and Marc Heirshberg.

Estimated Completion Date: These outcome-oriented deliverables to be included in agreement, when completed. Goal is for Fall 2020 completion, but no later than end of calendar year.

Recommendation #1-4: Establish a formal communication process, designate the individual(s) who have authority to direct TLT spending, set clear expectations for each party in the contract agreement, and identify key activities that should be communicated between both parties. For example, accepting and/or approving the annual budget, identifying when the allocated budget has not been followed, and requesting the reason for the variance, etc.

Action Plan #1-4: The City will identify roles and responsibilities of the Tourism Team as well as schedule times to meet and coordinate with each other to ensure clear communications to and from Visit Mesa. Also included will be procedures outlined for Visit Mesa's reference if they believe they received conflicting information or guidance from the City via a member of the Tourism Team. Visit Mesa will be fully informed of this strategy and approach.

Individual or Position Responsible: Natalie Lewis and Mike Kennington.

Estimated Completion Date: Fall 2020.