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Accountability \* Integrity \* Reliability

United States Government Accountability Office  
Washington, DC 20548

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November 5, 2004

The Honorable Kenneth M. Mead  
Inspector General  
Department of Transportation

Subject: *Applying Agreed-Upon Procedures: Highway Trust Fund Excise Taxes*

Dear Mr. Mead:

We have performed the procedures contained in the enclosure to this report, which we agreed to perform and with which you concurred, solely to assist your office in ascertaining whether the net excise tax revenue distributed to the Highway Trust Fund (HTF) for the fiscal year ended September 30, 2004, is supported by the underlying records. As agreed with your office, we evaluated fiscal year 2004 activity affecting distributions to the HTF.

In performing the agreed-upon procedures, we conducted our work in accordance with U.S. generally accepted government auditing standards, which incorporate financial audit and attestation standards established by the American Institute of Certified Public Accountants. These standards also provide guidance for performing and reporting the results of agreed-upon procedures.

The adequacy of the procedures to meet your objectives is your responsibility, and we make no representation in that respect. The procedures we agreed to perform were (1) detailed tests of transactions that represent the underlying basis of amounts distributed to the HTF, (2) review of the Internal Revenue Service's (IRS) quarterly HTF certifications, (3) review of the Department of the Treasury's Financial Management Service adjustments to the HTF for fiscal year 2004, (4) review of IRS's precertification<sup>1</sup> of receipts for the second and third quarters of fiscal year 2004, (5) review of certain procedures of the Department of the Treasury's Office of Tax Analysis' (OTA) process for estimating amounts to be distributed to the HTF for the fourth quarter of fiscal year 2004, and other procedures including (6) compiling and reporting the net amount of fiscal year 2004 excise taxes distributed to the HTF, (7) detailed tests of transactions that represent total IRS tax revenue receipts and refunds, and (8) review of key reconciliations of IRS records to Treasury records.

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<sup>1</sup>To accommodate the Department of Transportation's accelerated reporting date for fiscal year 2004, IRS performed precertifications of excise tax collections. The data are for information purposes only and the precertification does not constitute an official certification.

The enclosure contains the agreed-upon procedures and our findings from performing each of the procedures.

We were not engaged to perform, and did not perform, an audit, the objective of which would have been the expression of an opinion on the amount of net excise taxes distributed to the HTF. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.<sup>2</sup> We completed the agreed-upon procedures on October 27, 2004.

We provided a draft of this report to IRS and OTA officials for review and comment. IRS agreed with the results and findings presented in this report. OTA's review of the report only covered the procedures related to the estimation process for the quarter ended September 30, 2004. OTA agreed with the results and findings presented in this report relating to procedures performed on the estimation process for the quarter ended September 30, 2004.

This report is intended solely for the use of the Office of Inspector General of the Department of Transportation and should not be used by those who have not agreed to the procedures and have not taken responsibility for the sufficiency of the procedures for their purpose. However, this report is a matter of public record, and its distribution is not limited. Copies are available to others upon request. This report is also available at no charge on GAO's Web site at <http://www.gao.gov>. If you have any questions, please call me at (202) 512-3406.

Sincerely yours,



Steven J. Sebastian  
Director  
Financial Management and Assurance

Enclosure

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<sup>2</sup>In our report on the results of our audit of IRS's fiscal year 2003 financial statements, we noted a material weakness in IRS's financial reporting process (GAO, *Financial Audit: IRS's Fiscal Years 2003 and 2002 Financial Statements*, GAO-04-126, Nov. 13, 2003). A component of this process includes IRS's ability to allocate excise tax collections to the appropriate trust funds at the time deposits are made. This condition affects the adequacy of the distributions of federal excise tax revenue to recipient trust funds and is a continuation of an issue that we have reported on in prior years.

## Highway Trust Fund Excise Tax Procedures and Results

### I. Detailed tests of transactions that represent the underlying basis of amounts distributed to the Highway Trust Fund (HTF) in fiscal year 2004

#### A. Nonrepresentative selection of tax returns from the quarters ended June 30, 2003, and September 30, 2003<sup>3</sup>

1. For each of the quarters ending June 30, 2003, and September 30, 2003, select the 30 largest excise tax returns containing excise taxes related primarily to the HTF and the Airport and Airway Trust Fund (AATF) on the basis of total tax liability amount<sup>4</sup> from the Internal Revenue Service's (IRS) master file.<sup>5</sup>

#### Description of findings and results

We selected the 30 largest excise tax returns related primarily to the HTF and the AATF from each of the two quarters for testing. The selection was based on the total tax liability amount and type of taxes owed for each return from IRS's master file.

The total tax liability amount related to the 30 returns from the quarter ended June 30, 2003, was approximately \$8.8 billion, or 68 percent of the total excise tax liability amount of \$13 billion for all excise tax types for the quarter. Of these 30 returns, 21 contained primarily HTF-related taxes and 9 contained primarily AATF taxes.

The total tax liability amount related to the 30 returns from the quarter ended September 30, 2003, was approximately \$8.9 billion, or 67 percent of the total excise tax liability amount of \$13.3 billion for all excise tax types for the quarter. Of these 30 returns, 21 contained primarily HTF-related taxes and 9 contained primarily AATF taxes.

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<sup>3</sup>Since certifications are not completed until 6 months after the end of the quarter, the certification and corresponding adjustment by the Department of the Treasury's Financial Management Service for the quarters ended June 30, 2003, and September 30, 2003, were completed in December 2003 and March 2004, respectively, and thus affected fiscal year 2004 distributions to the HTF.

<sup>4</sup>Although the certifications are based on amounts collected, we used the tax liability amounts to identify the taxpayers paying the largest amounts of excise taxes. Our review shows that these taxpayers generally pay their excise taxes in full each quarter.

<sup>5</sup>The master file is a detailed database containing taxpayer information.

2. For each of the 42 returns related primarily to the HTF from the quarters ended June 30, 2003, and September 30, 2003, we performed the following procedures, which resulted in our testing approximately \$13.3 billion in prorated collections<sup>6</sup> affecting fiscal year 2004 distributions to the HTF:

- (a) Trace the liability amount for abstracts<sup>7</sup> 59, 60, and 62 from the tax return to IRS's master file.

Description of findings and results

The liability amount for abstracts 59, 60, and 62 on the tax return agreed with the master file for all 42 returns.

- (b) Check the mathematical accuracy of taxpayers' calculations on the tax return for the selected abstracts.

Description of findings and results

The taxpayers' calculations on all 42 returns were mathematically correct.

- (c) Recompute the prorated collection amount for the selected abstracts based on information from the master file and compare this amount to the amount from the Collection Certification System audit files.<sup>8</sup>

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<sup>6</sup>IRS certifies to trust funds the amount of excise taxes collected. Because taxpayers have sometimes not fully paid their tax liability, IRS must allocate the amount of payments actually received among the different excise taxes reported on the taxpayer's return. IRS's Collection Certification System prorates a taxpayer's payments proportionately among all taxes reported as owed on the tax return. For example, if a corporation reports that it owes \$4 million for gasoline tax, \$2 million for diesel fuel tax, and \$1 million for gasohol tax on its Form 720, Quarterly Federal Excise Tax Return, but has paid IRS only \$3.5 million at the time IRS performs its certification, the program prorates the \$3.5 million in the following manner: \$2 million to gasoline tax, \$1 million to diesel fuel tax, and \$500,000 to gasohol tax.

<sup>7</sup>The abstract numbers identify the tax type (e.g., gasoline and ticket tax) and are used as the basis for determining the distribution of the excise taxes to the various trust funds. Abstract numbers are preprinted on Form 720, Quarterly Federal Excise Tax Return, and are used by the taxpayer to report excise tax assessments. If the return was related to the HTF, we selected (1) tax on 10 percent gasohol (abstract 59), (2) diesel fuel tax (abstract 60), and (3) gasoline tax (abstract 62). If the return was related to the AATF, we selected (1) tax on transportation of persons by air (abstract 26), (2) tax on the use of international air facilities (abstract 27), and (3) tax on transportation of property by air (abstract 28). The tax amounts related to the selected abstracts for each trust fund are the largest tax amounts reported on the taxpayer's excise tax return and made up over 82 percent of the total amount certified to the HTF and over 89 percent of the total amount certified to the AATF each quarter.

<sup>8</sup>The Collection Certification System produces what IRS refers to as audit files. These audit files contain the individual prorated collections, by abstract and taxpayer identification number, that make up the certified total amounts for each abstract.

Description of findings and results

The recomputed prorated collection amounts for the three selected abstracts agreed with amounts in IRS's Collection Certification System for 39 of the 42 returns. Of the remaining 3 returns, 1 was from the quarter ended June 30, 2003, and 2 were from the quarter ended September 30, 2003.

On the one return from the quarter ended June 30, 2003, the taxpayer reported a credit on Part I of Form 720 under abstract 62. IRS allowed this credit and offset the amount against the taxpayer's reported abstract 62 assessment. IRS should have disallowed the credit because taxpayers filing Form 720 can report credits only on Schedule C of the form. As a result, IRS understated the prorated collections for the selected abstracts by an aggregate amount of \$14,549. IRS corrected this error on the trust fund certification for the quarter ended September 30, 2003. Consequently, there was no net effect on fiscal year 2004 distributions to the HTF resulting from this error.

On the two returns from the quarter ended September 30, 2003, IRS recorded a credit reported by the taxpayers on Schedule C of Form 720, which IRS had previously denied. As a result, IRS overstated the prorated collections for the selected abstracts by an aggregate amount of \$126,465. On one return, IRS received the information from the taxpayer to allow the credit. On the other return, IRS corrected the error on the trust fund certification for the quarter ended December 31, 2003. Consequently, there was no net effect on fiscal year 2004 distributions to the HTF resulting from these errors.

B. Dollar unit sample (DUS) of transactions from the quarters ended December 31, 2003, and March 31, 2004

1. Sampling

- (a) Obtain excise tax collection data from the master file for the first two quarters of fiscal year 2004. Determine if excise tax collection data from the master file agree with data from IRS's general ledger. Reconcile total excise tax collections from the master file to total excise tax collections from the Collection Certification System audit files to determine if they materially<sup>9</sup> agree.

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<sup>9</sup>For the purpose of this reconciliation, "material" is defined as 1 percent of the Form 720-related excise tax collections for the quarters ended December 31, 2003, and March 31, 2004. For fiscal year 2004, the materiality amount was \$226 million for the two quarters combined.

Description of findings and results

Excise tax collections for the first two quarters of fiscal year 2004 from the master file materially agreed with IRS's general ledger and with excise tax collections from the Collection Certification System.

- (b) Select a random attribute sample of 78 excise tax assessments from the master file.<sup>10</sup> Compare assessment and receipt information for each sample item from the master file to the assessment and receipt information in the Collection Certification System to determine if assessments and receipts from the master file are contained in the Collection Certification System.

Description of findings and results

For each sample item, assessments and receipts from the master file were contained in the Collection Certification System.

- (c) To determine if the Collection Certification System properly summarized the prorated collections, total the prorated collections for selected abstracts<sup>11</sup> from the audit files and compare these amounts to amounts in the *Report of Excise Tax Collection*.<sup>12</sup>

Description of findings and results

The Collection Certification System properly summarized the prorated collections for all of the selected abstracts. Prorated collections from the audit files for the selected abstracts agreed with the corresponding amounts in the *Report of Excise Tax Collection*.

- (d) Separate the total population of prorated collections from the audit files into the following distinct populations: (1) HTF, (2) AATF, and (3) other excise tax abstracts. Use DUS to select a sample of prorated excise tax collections from the HTF population.

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<sup>10</sup>For this sample, if one or no errors were found in testing the 78 items, we would be 90 percent confident that the error rate in the population would not exceed 5 percent.

<sup>11</sup>The selected abstracts are (1) tax on 10 percent gasohol (abstract 59), (2) diesel fuel tax (abstract 60), (3) gasoline tax (abstract 62), (4) tax on transportation of persons by air (abstract 26), (5) tax on the use of international air facilities (abstract 27), (6) tax on transportation of property by air (abstract 28), and (7) tax on aviation fuel for commercial use (abstract 77). The tax amounts for the three HTF-related abstracts made up over 82 percent of the total amount certified to the HTF, and the tax amounts for the four AATF-related abstracts made up over 95 percent of the total amounts certified to the AATF each quarter.

<sup>12</sup>The *Report of Excise Tax Collection* contains prorated collections, classified by abstracts, that serve as the basis for IRS's quarterly trust fund certifications.

Description of findings and results

Use of DUS with a confidence level of 80 percent, a test materiality of \$341 million, and an expected aggregate error amount of \$102.3 million resulted in a sample of 102<sup>13</sup> prorated collections for the HTF for the first two quarters of fiscal year 2004.

- (e) Select samples of prorated excise tax collections from the two non-HTF populations.

Description of findings and results

Use of DUS with a confidence level of 80 percent, a test materiality of \$88 million, and an expected aggregate error amount of \$26.4 million resulted in a sample of 73<sup>14</sup> prorated collections for the AATF for the first two quarters of fiscal year 2004.

A random attribute sample of 45 items from the population of prorated tax collections, related to all excise taxes other than the HTF and the AATF, was selected for testing.<sup>15</sup>

2. Detailed tests of transactions

- (a) For each prorated excise tax collection sampled from the HTF population:
- Check to determine whether the assessment amount on the tax return, for the sampled abstract, agrees with the amount recorded in the master file.

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<sup>13</sup>The planned sample size using DUS was 139 items. DUS selects dollars instead of specific transaction items by dividing the population by dollar intervals. The dollar interval for the HTF was \$125 million. Accordingly, any item with a dollar value matching or exceeding the sampling interval would be selected, whereas items with dollar values below the sampling interval might not be selected. For example, an item of \$250 million would cover 2 dollar-intervals, but represent one sample item. Due to large dollar items covering more than one interval, the 102 unique sampled transactions selected represent 139 dollar-intervals.

<sup>14</sup>The planned sample size using DUS was 143 items. As explained in footnote 13, DUS selects dollars instead of specific transaction items by dividing the population by dollar intervals. The dollar interval for the AATF was \$32 million. Because large dollar items cover more than one interval, the 73 unique sampled transactions selected represent 143 dollar-intervals.

<sup>15</sup>For this sample, if no errors are found in testing the 45 items, we would be 90 percent confident that the error rate in the population would not exceed 5 percent.

Description of findings and results

The assessment amount on the tax return agreed with the amount recorded in the master file for all of the sampled items.

- Check the mathematical accuracy of the taxpayers' calculations on the tax returns for the related abstract.

Description of findings and results

The taxpayers' calculations on the tax return were mathematically correct for all of the sampled items.

- Recompute the prorated collection amount based on information from the master file and compare this amount to the sample items selected from the Collection Certification System audit files.<sup>16</sup>

Description of findings and results

The recomputed prorated collection, based on information from the master file, agreed with the amounts for all of the sampled items.

- (b) Perform detailed testing on the two samples of prorated collections from the non-HTF populations to determine if they contain any HTF excise tax collections.

Description of findings and results

The two samples of prorated collections from the non-HTF populations did not contain any HTF excise tax collections.

- (c) Evaluate the results of conducting steps (a) and (b).

Description of findings and results

As noted in the results from steps (a) and (b), we found no errors.

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<sup>16</sup>The purpose of this test is to determine whether the Collection Certification System prorates correctly. This test is not intended to determine whether amounts provided to the system are correct.



## II. Review of IRS's quarterly HTF receipt certifications

### A. Receipt certifications

Perform the following steps on IRS's HTF receipt certification for the quarters ended September 30, 2003, December 31, 2003, and March 31, 2004:

1. Inspect the certification letters<sup>17</sup> for authorizing signatures.

#### Description of findings and results

The certification letters for all three quarters had authorizing signatures.

2. Determine if evidence exists that the supervisor or another analyst checked the certification letters and supporting worksheets.

#### Description of findings and results

There was evidence that the supervisor or another analyst checked the certification letters and supporting worksheets for all three quarters.

3. Recalculate the totals on the certification letters to determine if they are mathematically correct.

#### Description of findings and results

The totals on the certification letters for all three quarters were mathematically correct.

4. Trace the certified amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59)<sup>18</sup> from the certification letters back to the *Report of Excise Tax Collection*<sup>19</sup> and the

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<sup>17</sup>IRS prepares two certification letters for the HTF each quarter: one for the Highway Account and the other for the Mass Transit Account.

<sup>18</sup>The certified amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59), along with the heavy vehicle use tax (traced separately), made up over 85 percent of the total amount certified to the HTF each quarter.

<sup>19</sup>IRS uses data from two of these reports, covering sequential processing intervals, for each quarterly certification. Collections are classified by abstract on the report when the related Form 720 tax return has been recorded in IRS's master file during the processing interval covered by the report. The second of the two reports used may contain collections related to previous quarters not classified by abstract until the current quarter because the related return was not recorded on the master file until the current quarter.

*Treasury 90 Report.*<sup>20</sup>

Description of findings and results

The certified amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) from the certification letters agreed with the related *Report of Excise Tax Collection* and the *Treasury 90 Report* for all three quarters.

5. Review the distribution rates used by IRS to determine if the distribution rates for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) agree with the applicable laws.<sup>21</sup>

Description of findings and results

The distribution rates used by IRS for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) agreed with the applicable laws in effect during all three quarters.

6. Review the *Report of Excise Tax Collection* used in the certification to determine if it contains significant<sup>22</sup> collections from prior quarters.

Description of findings and results

The *Report of Excise Tax Collection* used in the certification for all three quarters did not contain significant collections from prior quarters.

7. Trace heavy vehicle use tax amounts from the Highway Account certification letters to the master file. These taxes, which go to the HTF, are reported on Form 2290 and are not included in the Collection Certification System.

Description of findings and results

The heavy vehicle use tax amounts from the Highway Account certification letter agreed with the master file for all three quarters.

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<sup>20</sup>The *Treasury 90 Report* summarizes excise tax credit information and is produced quarterly by IRS submission processing campus systems. IRS has nine submission processing campuses that receive and process tax returns and payments.

<sup>21</sup>IRS calculates certified collections to the Highway Account and the Mass Transit Account using the total prorated collection amount, tax rate, and distribution rates applicable to each account.

<sup>22</sup>For this test, "significant" is defined as \$175 million, which represents approximately 2 percent of the quarterly total certified to the HTF.

### III. Review of Financial Management Service adjustments

Perform the following steps on Financial Management Service (FMS) adjustments to HTF excise tax distributions for the quarters ended September 30, 2003, December 31, 2003, and March 31, 2004:

- A. Compare the FMS adjustments made to the HTF for fiscal year 2004 with original Office of Tax Analysis (OTA) estimates and IRS-certified amounts to determine if they agree with the supporting schedules.<sup>23</sup>

#### Description of findings and results

For the FMS adjustments made to the HTF accounts (Highway and Mass Transit), the original OTA estimates and IRS-certified amounts agreed with the supporting schedules for all three quarters.

- B. Recompute the difference between the OTA estimates and final IRS-certified amounts to determine if the amounts agree with the differences computed by FMS.

#### Description of findings and results

The independently recalculated differences between the OTA estimates and the final IRS-certified amounts for the Highway Account agreed with the differences computed by FMS for all three quarters. These amounts were<sup>24</sup>

- \$29,543,000 for the quarter ended September 30, 2003,
- (\$750,127,000) for the quarter ended December 31, 2003, and
- (\$251,860,000) for the quarter ended March 31, 2004.

The independently recalculated differences between the OTA estimates and final IRS-certified amounts for the Mass Transit Account agreed with the differences computed by FMS for all three quarters. These amounts were

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<sup>23</sup> An FMS accountant compiles this schedule, called the "Subsidiary Quarterly Account of Estimates and Actual Related Taxes Appropriated to Highway Trust Fund." This schedule computes the difference between IRS-certified amounts and the OTA estimate for excise taxes, individually and in total, that relate to the Highway Account. A similar schedule is prepared for the Mass Transit Account. The schedules, along with OTA transfer forms and IRS certifications, support the FMS adjustment.

<sup>24</sup> A positive amount indicates that the FMS adjustment increased excise taxes distributed to the trust fund. A negative amount, shown in parentheses, indicates that the FMS adjustment decreased excise taxes distributed to the trust fund. Since the adjustment amount is the difference between OTA's estimate and IRS's certified amount, it may be significantly affected by IRS's ability to certify receipts in the appropriate quarter.

- (\$13,769,000) for the quarter ended September 30, 2003,
- (\$78,124,000) for the quarter ended December 31, 2003, and
- (\$38,537,000) for the quarter ended March 31, 2004.

**IV. Review of IRS precertification for the quarters ended March 31, 2004, and June 30, 2004<sup>25</sup>**

- A. Determine if evidence exists that the supervisor or another analyst checked the results and supporting worksheets.

Description of findings and results

There was evidence that the supervisor or another analyst checked the results and supporting worksheets for both quarters.

- B. Recalculate the totals on the precertification to determine if they are mathematically correct.

Description of findings and results

The totals on the precertification were mathematically correct for both quarters.

- C. Trace the amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59)<sup>26</sup> from the precertification back to the *Report of Excise Tax Collection* and the *Treasury 90 Report*.

Description of findings and results

The amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) from the precertification agreed with the related *Report of Excise Tax Collection* and the *Treasury 90 Report* for the quarter ended June 30, 2004.

In the precertification for the quarter ended March 31, 2004, IRS erroneously omitted returns related to the quarter that posted during the month of March. The total amount of prorated collections related to the HTF for these returns

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<sup>25</sup>In order to accommodate the Department of Transportation's November 15 reporting date for fiscal year 2004, IRS performed precertifications. The data in the precertification are for information purposes only and do not represent an official certification.

<sup>26</sup>The certified amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) made up over 83 percent of the precertified total to the HTF.

was approximately \$41,000. Because IRS's precertification is not an actual certification that results in any redistributions of excise taxes among the trust funds, this error did not have an effect on fiscal year 2004 distributions to the HTF.

- D. Review the distribution rates used by IRS to determine if the rates for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) agree with the applicable laws.

Description of findings and results

The distribution rates used by IRS for diesel fuel tax (abstract 60), gasoline tax (abstract 62), and tax on 10 percent gasohol (abstract 59) agreed with the applicable laws in effect during both quarters.

- E. Review the *Report of Excise Tax Collection* used in the precertification to determine if it contains significant<sup>27</sup> collections from prior quarters.

Description of findings and results

The *Report of Excise Tax Collection* supporting IRS's precertification for both quarters did not contain significant collections from prior quarters.

- F. Review the Collection Certification System information to determine whether IRS omitted any significant<sup>28</sup> returns from the precertification. If so, report for the Highway Account and the Mass Transit Account (1) the average amount of HTF-related excise taxes from these taxpayers' returns that were included in IRS's certification from the four previous quarters and (2) the amount of HTF-related excise taxes from these taxpayers' returns that were included in IRS's certification for the quarters ended March 31, 2003, and June 30, 2003.

Description of findings and results

IRS did not omit any significant returns from the precertifications for both quarters.

- G. Trace heavy vehicle use tax amounts from the Highway Account precertification letter to the master file.

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<sup>27</sup>For this test, "significant" is defined as \$175 million. This represents approximately 2 percent of the precertified total to the HTF.

<sup>28</sup>For this test, "significant" is defined as tax returns with a total quarterly excise tax liability equal to or greater than \$10 million during each of the prior four quarters. Tax returns related specifically to the HTF with liabilities equal to or greater than \$10 million have, in the aggregate, historically accounted for over 91 percent of distributions certified to the HTF.

Description of findings and results

The heavy vehicle use tax amount from the Highway Account precertification letter agreed with the master file for the quarter ended June 30, 2004.

The heavy vehicle use tax amount of \$89,908,000 from the precertification letter for the quarter ended March 31, 2004, included only the amount for the month of March rather than the total amount of \$205,962,000 for the quarter. The IRS analyst erroneously entered only the March amount from the supporting worksheet when carrying the amount onto the precertification letter. Because the precertification is not an actual certification that results in any redistributions of excise taxes among the trust funds, this error did not have an effect on fiscal year 2004 distributions to the HTF.

**V. Procedures performed on excise tax distributions to the HTF for the quarter ended September 30, 2004**

- A. Determine if OTA's process for identifying and incorporating the effect of new legislation on excise tax receipts into its trust fund estimates<sup>29</sup> was in place during the quarter ended September 30, 2004.

Description of findings and results

OTA's process for identifying and incorporating into its trust fund estimates the effect of new legislation on excise tax receipts was in place during the quarter ended September 30, 2004. OTA prepares a tax rate table<sup>30</sup> to capture information relating to legislation that affects tax rates, tax basis, accounts, and deposit rules in effect during the quarter.

- B. Determine if there is evidence of review of the transfer forms and supporting schedules.

Description of findings and results

There was evidence that another OTA economist reviewed the transfer forms and supporting schedules for the semimonthly transfers affecting distributions to the HTF for the quarter ended September 30, 2004.

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<sup>29</sup>OTA makes semimonthly estimates of excise tax collections for transfer to trust funds. There are five semimonthly estimates for the quarter ended September 30, 2004, which affect fiscal year 2004 distributions to the HTF.

<sup>30</sup>OTA communicates this information to interested parties at Treasury, the Federal Highway Administration, the Federal Transit Administration, and the Department of Transportation. IRS uses the tax and distribution rates from this table in its subsequent certification of collections to trust funds.

## Enclosure

- C. Recalculate the totals on the transfer forms to determine if they are mathematically correct.

### Description of findings and results

The totals on the transfer forms affecting distributions to the HTF for the quarter ended September 30, 2004, were mathematically correct.

- D. Trace the transfer amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), tax on 10 percent gasohol (abstract 59), and heavy vehicle use tax<sup>31</sup> from the transfer letter through the supporting schedules and back to the related source documents.<sup>32</sup>

### Description of findings and results

The transfer amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), tax on 10 percent gasohol (abstract 59), and heavy vehicle use tax from the transfer letter agreed with the supporting schedules and source documents for the semimonthly transfers affecting distributions to the HTF for the quarter ended September 30, 2004.

## VI. Other procedures

- A. Compile and report the net amount of fiscal year 2004 excise taxes distributed to the HTF.

### Description of findings and results

Based on a compilation of IRS's certifications, OTA's estimations, and adjustments, the net amount of fiscal year 2004 excise taxes distributed to the HTF was \$34,692,294,040.

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<sup>31</sup>The transfer amounts for diesel fuel tax (abstract 60), gasoline tax (abstract 62), tax on 10 percent gasohol (abstract 59), and heavy vehicle use tax made up 88 percent of the total amount transferred to the HTF for the fourth quarter of fiscal year 2004.

<sup>32</sup>The source documents include the IRS report of excise taxes used to derive the percentages applied to reported receipts, the Daily Treasury Statement, the Monthly Treasury Statement, and the excise tax rate tables.

B. Procedures performed as part of the fiscal year 2004 IRS financial statement audit:

1. From IRS's master files for the first 8 months of fiscal year 2004, use DUS to select statistical samples of (1) total tax revenue receipts and (2) refunds. For each sample item, test that the collection or refund amount, tax period, and tax class<sup>33</sup> from source documentation agree with those recorded in the master files.

Description of findings and results

Detailed testing of 135 revenue receipts and 48 refund sample transactions showed that the collection or refund amount, tax period, and tax class from source documents agreed with amounts recorded in the master files.

2. Review selected IRS service center campuses' monthly Treasury SF-224 reconciliations to determine if IRS-reported revenue receipts were properly classified and reconciled to Treasury FMS records. For refunds, review selected IRS service center campuses' monthly Treasury SF-224 reconciliations to determine if IRS-reported total refunds (all tax classes) materially<sup>34</sup> reconciled to Treasury FMS records.<sup>35</sup>

Description of findings and results

Tax revenue receipts reported by selected IRS service center campuses through the monthly Treasury SF-224 reconciliation process were properly classified and materially reconciled to Treasury FMS records. Total refunds reported by selected IRS service center campuses through the monthly Treasury SF-224 reconciliation process materially reconciled to Treasury FMS records.

3. Perform procedures to determine whether tax revenue receipt balances by tax class, including excise taxes, recorded in IRS's general ledger materially agree with the master files and Treasury records. For refunds, perform a comparison of total refund balances between the master files, the general ledger, and Treasury records.

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<sup>33</sup>IRS assigns a tax class number to specific types of taxes. Excise taxes are tax class 4.

<sup>34</sup>For the purpose of this procedure and procedure VI.B.3, we define "material" as \$20 billion. This represents 1 percent of the estimated total tax revenue receipts collected by IRS in fiscal year 2004.

<sup>35</sup>IRS maintains records of refund balances by tax class in its master file and reports this information monthly to Treasury on the SF-224. Treasury provides IRS with a Statement of Differences (TFS-6652), which reports differences between total refunds reported by IRS on the SF-224 and the total refunds in Treasury records.



Enclosure

Description of findings and results

Tax receipt balances for all tax classes, including excise taxes, recorded in IRS's general ledger materially agreed with the master files and Treasury records. Refund balances recorded in IRS's general ledger materially agreed with the master files and with Treasury records.

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