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United States General Accounting Office
Washington, DC 20548

February 26, 2001

The Honorable Gordon S. Heddell
Inspector General
Department of Labor

Subject: Applying Agreed-Upon Procedures: Federal Unemployment Taxes

Dear Mr. Heddell:

We have performed the procedures contained in the enclosure to this letter, which we agreed to perform and with which you concurred, solely to assist your office in ascertaining whether the net federal unemployment tax (FUTA) revenue distributed to the Unemployment Trust Fund (UTF) for the fiscal year ended September 30, 2000, is supported by the underlying records. As agreed with your office, we evaluated fiscal year 2000 activity affecting distributions to UTF.

In performing the agreed-upon procedures, we conducted our work in accordance with 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 when 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 include (1) detailed tests of transactions that represent the underlying basis of amounts distributed to the UTF and (2) review of key reconciliations of the Internal Revenue Service records to the Department of the Treasury records. 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 net amount of FUTA taxes distributed to the UTF. 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. We completed the agreed-upon procedures on February 16, 2001.

We provided a draft of this letter to IRS, along with its enclosure, for review and comment. IRS officials agreed with the contents of this letter.

This letter is intended solely for the use of the Office of Inspector General of the Department of Labor 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 purposes. However, this letter is a matter of public record and its distribution is not limited. Consequently, copies are available to others upon request. If you have any questions, please call Steven J. Sebastian, Acting Director at (202) 512-3406.

Sincerely yours,



Jeffrey C. Steinhoff
Managing Director
Financial Management and Assurance

Enclosure

Enclosure

Unemployment Trust Fund Procedures and Results

(A) General

(1) Compare fiscal year 2000 net FUTA collections per the Internal Revenue Service's (IRS) statement of custodial activity and related footnote disclosures to (a) the Treasury's Bureau of Public Debt (BPD) accounting records for the Unemployment Trust Fund (UTF) and (b) drafts of the Department of Labor's (DOL) consolidated financial statements. Obtain explanations/support for material variances.[a]

Description of findings and results

There were no significant variances between net FUTA collections per IRS' statement of custodial activity and BPD's accounting records for UTF. Similarly, there were no significant variances between IRS' statement of custodial activity and related footnote disclosures and drafts of DOL's consolidated financial statements.

(B) Sampling

(1) Obtain from IRS total FUTA collections and refunds reflecting the first 9 months of fiscal year 2000 posted to the master file.[b] Determine if FUTA collections and refund data per the master file materially reconcile to the general ledger.

Description of findings and results

Total FUTA collections and refunds for the first 9 months of fiscal year 2000 per the IRS master file materially reconciled to IRS' general ledger.

(2) Use Dollar Unit Sampling (DUS) to select a sample of combined FUTA collection and refund transactions from the master file for the first 9 months of fiscal year 2000, using a confidence level of 80 percent, a test materiality of $318 million, and an expected aggregate error amount of $159 million.

Description of findings and results

Use of Dollar Unit Sampling with a confidence level of 80 percent, a test materiality of $318 million, and an expected aggregate error amount of $159 million resulted in a sample of 84 transactions for the first 9 months of

[a]Except where noted for certain procedures, significant or material is defined as $318 million. This represents one percent of the Unemployment Trust Fund collections for fiscal year 1999.

[b]The master file is a detailed database containing taxpayer information.

fiscal year 2000. Of this total, 82 transactions represented collections and 2 transactions represented refunds.

(C) Detailed tests of transactions

(1) For each sampled FUTA tax collection transaction:

(a) Determine if collection amounts are accurately recorded by tracing collection transaction amounts from IRS' master files to deposit confirmation documents (e.g., federal tax deposit coupons).

Description of findings and results

Based on supporting documentation, collection amounts were accurately recorded for all of the 82 sampled FUTA collection transactions.

(b) Determine if amounts were recorded to the appropriate period by reviewing the date on source documents.

Description of findings and results

Based on supporting documentation, collection amounts were recorded to the appropriate period for all of the 82 sampled FUTA collection transactions.

(c) Determine whether the transactions were properly categorized as FUTA receipts by reviewing source documentation maintained in IRS' files (e.g., tax returns).

Description of findings and results

Based on supporting documentation, collection amounts were recorded in the correct tax class[c] for all of the 82 sampled FUTA collection transactions.

(d) Confirm FUTA transactions paid via the Electronic Federal Tax Payment System (EFTPS)[d] to determine whether the recorded transactions are valid

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[c]IRS assigns a tax class number to specific types of taxes. FUTA taxes are tax class 8.

[d]EFTPS is a system for initiating tax payments electronically. Starting January 1, 2000, employers who made Federal tax deposits exceeding $200,000 in 1998 must use EFTPS to pay their FUTA taxes. The $200,000 threshold includes all federal tax deposits, such as deposits for employment tax, excise tax, and corporate income tax. Taxpayers who are not required to make electronic deposits may voluntarily participate in EFTPS.

and reflect the proper amounts, are applied to the proper tax period, and are properly categorized as FUTA receipts.

Description of findings and results

Of the 82 sampled FUTA receipt transactions, 68 were paid via EFTPS. The bank confirmation showed that all 68 transactions are valid and had been recorded to the proper tax period and tax class and for the proper amounts.

(e) Recalculate each tax return to check mathematical accuracy.

Description of findings and results

The tax returns associated with all of the 82 FUTA collection sampled transactions were mathematically correct.

(2) For each sampled FUTA tax refund transaction:

(a) Confirm sampled FUTA refund transactions with Treasury's Financial Management Service (FMS) by checking that the amount of the refund is correct, and that it was recorded to the appropriate period and tax class.

Description of findings and results

For both of the FUTA refund transactions sampled, confirmation with Treasury's FMS showed that the amount of the refund was correct and that it was recorded to the appropriate period and tax class.

(b) Recalculate each tax return to verify mathematical accuracy.

Description of findings and results

The tax returns for the two FUTA refund transactions were mathematically correct.

(c) For FUTA tax returns, determine whether the taxpayer provided a written explanation for exempt payments, and whether the explanation meets IRS' criteria for FUTA exempt wage payments.

Description of findings and results

For both of the FUTA transactions sampled, the taxpayer did not claim exempt wage payments requiring an explanation.

(d) For manual refunds, check to see that the appropriate supporting documentation is attached and that individuals who approved the manual refunds were authorized to do so.

Description of findings and results

Neither of the two sampled FUTA refund transactions were manual refunds.

(D) Analytical Procedures

(1) Perform a predictive test on FUTA revenue collection and refund data for the final 3 months of the fiscal year to determine if reported fiscal year 2000 revenue collections and refunds appear consistent and reasonable. Project the expected fourth quarter FUTA revenue collection and refund amounts for fiscal year 2000, based on fiscal year 1999 quarterly amounts, and compare the projection to actual revenue collections and refunds. If a material variance exists, discuss with IRS to obtain an explanation/support.

Description of findings and results

The predicted fourth quarter FUTA revenue collection and refund amounts for fiscal year 2000 did not materially vary from the actual amount of revenue collections and refunds during this period.

(2) Perform an analytical test comparing reported FUTA net revenue collections as of the interim test period (June 30, 2000) and as of the end of the fiscal year (September 30, 2000) to the respective prior periods.

Description of findings and results

FUTA net revenue collections as of the interim test period and the fiscal year ended September 30, 2000 increased by $328.5 million and $337 million respectively. Both of these variances exceed FUTA test materiality of $318 million.

(E) Other FUTA Procedures

(1) For each of the 12 months in fiscal year 2000, obtain and review supporting documentation for monthly revenue reclassification adjustments transmitted by IRS to Treasury's FMS. Check to see that the supporting documentation agrees with the reclassification adjustment transmitted to FMS.

Description of findings and results

Documentation supported the monthly FUTA reclassification adjustment amount transmitted to Treasury's FMS for all 12 months of fiscal year 2000.

(2) For each of the 12 months in fiscal year 2000, obtain and review supporting documentation for the monthly entry of FUTA refund data onto the Government Online Accounting Link System (GOALS) to charge back the Unemployment Trust Fund account for FUTA tax refunds issued. Check to see that the supporting documentation agrees with the monthly entries reported on GOALS.

Description of findings and results

Documentation supported the monthly FUTA refund amount entered on GOALS to charge the Unemployment Trust Fund for FUTA tax refunds issued for all 12 months of fiscal year 2000.

(F) Other procedures performed as part of the Fiscal Year 2000 IRS financial statement audit

(1) Use DUS to select statistical samples of a) total revenue receipts and b) refunds from IRS master files for the first 9 months of fiscal year 2000. For each item in the samples of revenue receipts and refunds, test that the collection or refund amount and tax class from source documentation agrees with amounts recorded in IRS master files.

Description of findings and results

Detailed testing of 199 revenue receipts and 18 refund sample transactions showed that the collection or refund amount and tax class from source documents agreed with amounts recorded in the IRS master files.

(2) Review selected IRS service centers' 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 centers' monthly Treasury SF-224 reconciliations to determine if IRS-reported total refunds (all tax classes) materially[e] reconciled to Treasury FMS records.[f]

Description of findings and results

Tax revenue receipts reported by selected IRS service centers via the monthly Treasury SF-224 reconciliation process were properly classified and materially agreed with Treasury FMS records.

Total refunds reported by the selected IRS service centers via the monthly Treasury SF-224 reconciliation process materially agreed with Treasury FMS records.

(3) Perform a proof of cash for fiscal year 2000 to determine whether revenue receipt balances by tax class per the general ledger materially agree with IRS' master files and Treasury records. For refunds, perform a comparison of total refund balances between the master file, the general ledger, and Treasury records. Also, compare FUTA refunds per the master file to the general ledger.

Description of findings and results

Fiscal year-end tax receipt balances for all tax classes, including FUTA, per IRS' general ledger materially agreed with IRS' master files and with Treasury records.

Fiscal year-end refund balances per IRS' general ledger materially agreed with the master file and with Treasury records.

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[e]For the purpose of this section, we define material as $20 billion.

[f]IRS maintains records of refund balances by tax class in its master file, and reports this information monthly to Treasury via 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 per Treasury records.