

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
OFFICE OF THE INSPECTOR GENERAL**

**AUDIT OF THE MOTOR FUEL  
SALES AND TAX PROCESS**



**CHARLES J. WILLOUGHBY  
INSPECTOR GENERAL**

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**Office of the Inspector General**

Inspector General



July 23, 2009

Stephen M. Cordi  
Deputy Chief Financial Officer  
Office of Tax and Revenue  
Office of the Chief Financial Officer  
941 North Capitol Street, N.E., 8<sup>th</sup> Floor  
Washington, D.C. 20002

Gabe Klein  
Director  
District Department of Transportation  
2000 14<sup>th</sup> Street, N.W., 6<sup>th</sup> Floor  
Washington, D.C. 20009

Dear Mr. Cordi and Mr. Klein:

Enclosed is our final report summarizing the results of the Office of the Inspector General's (OIG) Audit of Motor Fuel Sales and Tax Process (OIG No. 09-2-02KA).

As a result of our audit, we directed four recommendations to the Office of Tax and Revenue (OTR) and two recommendations to the District Department of Transportation (DDOT) for necessary actions to correct reported deficiencies. We received OTR's response to the draft report on June 29, 2009. OTR concurred with all of the recommendations and DDOT has advised OTR that it will undertake coordinating the International Fuel Tax Agreement application Process. We consider the responses received to be responsive to our recommendations. However, we request that DDOT provide an estimated completion date for Recommendations 5 and 6. The full text of OTR's response to the draft report is included at Exhibit B.

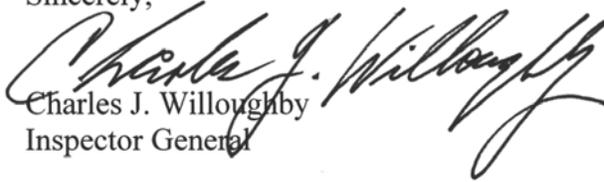
Our audit report also identifies an error in the calculation of bond liability for a licensee. We did not make a specific recommendation on this matter; but we did discuss the issue with OTR officials. We have reviewed OTR's legal opinion and disagree with the analysis and the applicability of the case cited therein. The bond required of a licensee pursuant to D.C. Code § 47-2303(a) is based upon the taxes due from that licensee to the District, whether the taxes were paid to the District directly by the licensee or a third party, in this case another state. Based on the OIG's interpretation, we ask that OTR reconsider its position and require bond liability due from importers to be calculated based on the amount of District motor fuel tax due from the licensee.

We ask that OTR respond to the two open items identified above within 60 days of the date of this report.

Mr. Cordi and Mr. Klein  
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We appreciate the cooperation extended to our staff during this audit. If you have any questions, please contact William J. DiVello, Assistant Inspector General for Audit, at (202) 727-2540.

Sincerely,

  
Charles J. Willoughby  
Inspector General

CJW/cf

Enclosure

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**AUDIT OF THE MOTOR FUEL SALES AND TAX PROCESS**

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## AUDIT OF THE MOTOR FUEL SALES AND TAX PROCESS

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### ACRONYMS

DDOT	District Department of Transportation
DMV	Department of Motor Vehicles
IFTA	International Fuel Tax Association
IRP	International Registration Plan
ITS	Integrated Tax System
OCFO	Office of the Chief Financial Officer
OIG	Office of the Inspector General
OTR	Office of Tax and Revenue
RAA	Revenue Accounting Administration
RCA	Revenue Collection Administration
RPA	Return Processing Administration
SOP	Standard Operating Procedures

## **EXECUTIVE DIGEST**

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### **OVERVIEW**

The District of Columbia Office of the Inspector General (OIG) has completed an audit of the motor fuel sales and tax process. The audit was initiated in response to concerns of decreasing motor fuel tax revenues raised by the former City Administrator. Our overall audit objective was to determine whether motor fuel taxes – relative to District wholesalers/importers, distributors, and retail gas stations – are complete and accurate.

### **CONCLUSIONS**

This report contains two findings that detail the conditions found during our audit. In our first finding, we identified that importer motor fuel tax liabilities have gone uncollected for more than 6 years. Unremitted importer motor fuel taxes were the result of: 1) a lack of internal controls in the Office of Tax and Revenue's (OTR's) manual processes for motor fuel tax revenues; 2) insufficient oversight by OTR's Audit Division; and 3) the exclusion of a module in the OTR Tax Integrated System (ITS) that would assign delinquent motor fuel tax accounts to tax revenue officers to take the necessary enforcement actions. As a result, we identified uncollected motor fuel tax revenues of about \$733,000 for 6 years. We also found that the District assumed an increased risk of loss due to the miscalculation of bond liability owed by motor fuel taxpayers, which would provide monies to cover potential losses from delinquent taxes or damages caused by a fuel spill or other accidents.

The second finding was reported in a previous audit issued by our Office almost 5 years ago. We found that the District did not implement previously agreed-to recommendations and, therefore, lost interstate bus tax revenues totaling at least \$2.3 million over the last 10 years (\$229,000 annually) by not participating in the International Fuel Tax Agreement managed by the International Fuel Tax Association (IFTA). The last time the District applied for membership in IFTA was in 1999. The District was rejected for membership because the District's proposal did not conform to IFTA regulations and requirements, and because of the Department of Motor Vehicles (DMV) non-compliance with the International Registration Plan (IRP) requirements.

### **PERSPECTIVE**

Fiscal year (FY) 2008 presented the city's leadership with significant fiscal challenges that we believe will continue into the near future, given the national downturn in the economy. A tightening of revenue streams due to falling real estate values, combined with lower wages due to higher unemployment, will place added stress on the city's tax revenues. Because tax collections generate the bulk of revenue to finance District operations paid from the General Fund, the efficiency of the tax collection systems and the effectiveness of policies, procedures, and internal controls determine whether the District is maximizing collection of its taxes. As such, it is vital that District managers ensure that all revenues due to the District are properly reported and timely collected. This report concludes that the District has not been aggressively pursuing potential revenues in the areas of importer motor fuel taxes and interstate bus tax

## **EXECUTIVE DIGEST**

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revenues. We believe that if recommendations in this report are implemented, increases in revenues can be realized.

### **SUMMARY OF RECOMMENDATIONS**

We directed four recommendations to the Deputy Chief Financial Officer, OTR, Office of the Chief Financial Officer (OCFO) and two recommendations to the Director of the District Department of Transportation (DDOT) that we believe are necessary to correct the deficiencies noted in this report. The recommendations, in part, center on:

- Implementing controls over the manual processing of motor fuel tax returns to ensure that that amounts entered into the system are correct and timely filed, and that related tax liabilities due are collected.
- Establishing procedures to ensure coordination between the audit section at OTR, the collection department within OTR, and the users/responsible persons of the ITS to reconcile and ensure amounts are properly reported and collected.
- Adopting a quality control system to ensure that the internal auditors are complying with OTR operating procedures.
- Establishing a Case Management System that classifies delinquent tax cases by tax type, dollar amount, and tax year.
- Contacting the International Fuel Tax Association to identify what changes or corrections are needed in the DDOT's administration of the IRP program to ensure compliance and gain acceptance in the IFTA.
- Completing the necessary paperwork for participation in the IFTA Clearinghouse for processing and payment of fuel taxes.

A summary of the potential benefits resulting from the audit is shown at Exhibit A.

### **MANAGEMENT ACTIONS AND OIG COMMENTS**

On June 29, 2009, OTR provided a response to the recommendations in our draft audit report, which included actions to be taken by DDOT. The response fully addresses all of the recommendations, and we consider the reported planned and/or taken actions to be responsive to the recommendations. The full text of OTR's response is included at Exhibit B.

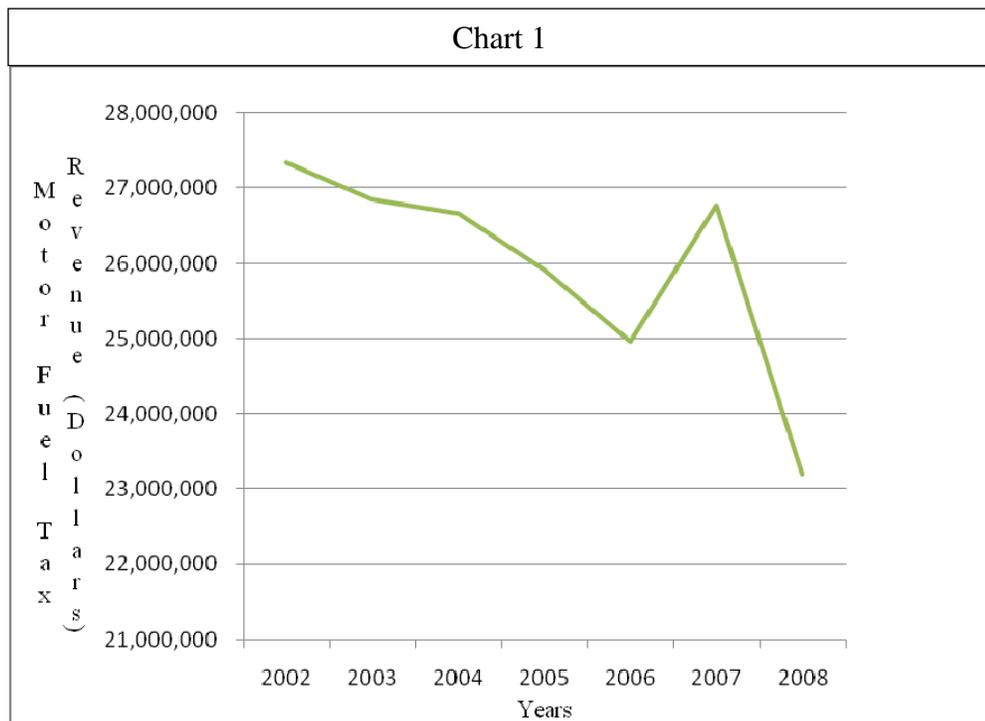
## INTRODUCTION

### BACKGROUND

The motor fuel tax is an excise tax imposed primarily on importers (wholesale businesses) for motor vehicle fuel sold and used within the District. D.C. Code § 47-2301(a) (2005) states that the District's motor fuel tax rate is 20 cents per gallon of fuel sold or used. D.C. Code § 47-2303(a) requires motor fuel taxpayers to obtain an annual license. D.C. Code § 47-2304 requires each importer to file a monthly motor fuel tax return (Form FR-400M) on or before the 25<sup>th</sup> day of each calendar month.

A motor fuel tax may also be assessed on any bus company operating in the District. A bus company is required to file an Interstate Bus Report (Form FR-462) for each month in which the bus company is operating in the District. The Interstate Bus Report is due on or before the last business day of the month, for the previous month's usage. The tax is equal to the tax rate (20 cents) multiplied by the number of gallons the bus company used while operating in the District.

Over the past 7 years, motor fuel tax collections have ranged from an annual high of \$27.4 million to a low of \$23.2 million. The District has realized a steady decline of motor fuel tax collections over this time period; OTR officials have attributed this decrease to rising gas prices and the resultant shift from the use of personal owned vehicles to public transportation. Chart 1 below shows this decline for fiscal years (FYs) 2002 through 2008.



## INTRODUCTION

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For FY 2008, 70 motor fuel importers and 9 bus companies filed with the District. For FYs 2006, 2007, and 2008, the total motor fuel tax collected was \$23 million, \$26 million, and \$23 million, respectively.

### CRITERIA

Title 47, Chapter 23 of the D.C. Code and Title 49, Chapter 317 of the U.S. Code provide the governing regulations for reporting, collecting, and enforcing motor fuel taxes and interstate bus taxes.

**D.C. Code § 47-2304** requires motor fuel importers to file a monthly tax return on or before the 25<sup>th</sup> day of each calendar month. It specifically states:

Each importer engaged in the District of Columbia in the sale or other disposition or use of motor vehicle fuel shall render to the Assessor of the District of Columbia, on or before the 25<sup>th</sup> day of each calendar month on forms prescribed, prepared, and furnished by the said Assessor, a sworn report of the total number of gallons of motor vehicle fuel within the District of Columbia sold or otherwise disposed of by such importer or used. . . .

**D.C. Code § 47-2303(c)** provides for a penalty for failure to file required tax forms. Specifically, it states:

If any importer fails, refuses, or neglects to file the monthly report, or to pay the tax within the time required by this subchapter, the Mayor shall promptly notify the importer and the bonding company by notice sent by registered mail or by certified mail to such importer requiring him to show cause why the license should not be revoked. If in the opinion of the Assessor, the importer fails within 10 days after the mailing of such notice to show that failure to file the monthly report or to pay the tax as the case may be within the time required was due to accident or justifiable oversight, the Assessor shall forthwith revoke such license. Any importer whose license has been revoked shall not be issued another license for 12 months following the date of said revocation.

**Title 49 U.S.C.S. § 31705(a)** states:

Reporting requirements. After September 30, 1996, a State may establish, maintain, or enforce a law or regulation that has a fuel use tax reporting requirement (including any tax reporting form) only if the requirement conforms with the International Fuel Tax Agreement.

## **INTRODUCTION**

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### **ROLES AND RESPONSIBILITIES RELATED TO MOTOR FUEL TAX RETURNS**

OTR, under the direction of the Deputy Chief Financial Officer, is responsible for collecting and processing the motor fuel tax.

The Returns Processing Administration (RPA) within OTR is responsible for receiving the motor fuel tax returns and payments, ascertaining the accuracy and completeness of the tax returns, indexing, and scanning the returns into the Integrated Tax System (ITS). The Revenue Accounting Administration (RAA) is responsible for accounting and reporting on the District's general fund for the motor fuel tax revenue.

The Revenue Collection Administration (RCA) is responsible for collecting taxes owed to the District and taking the necessary enforcement actions to collect any delinquent taxes. These actions include issuing a levy to seize wages, bank accounts, and accounts receivable, and seizing property such as a residence, business establishment, business properties, automobile, boat, etc. After the property has been seized, OTR may sell the property at public auction if the tax remains unpaid.

The OTR Audit Division is responsible for managing motor fuel tax returns, processing importer licenses, reviewing tax returns, contacting taxpayers for miscalculation or missing information, processing the tax refund documents, and reconciling motor fuel tax returns. In addition, the Audit Division is responsible for conducting audits of the motor fuel tax filings to ensure compliance with laws and regulations, and verifying the accuracy of tax returns.

### **OBJECTIVES, SCOPE, AND METHODOLOGY**

The overall objective of the audit was to determine whether motor fuel tax - relative to District wholesalers/importers, distributors, and retail gas stations - are complete and accurate. Our audit covered motor fuel tax returns filed by 70 importers during FYs 2006, 2007, and 2008. To meet our objectives, we reviewed 695 tax returns for 21 of the 70 importers filed during the audit period. In addition, we documented and tested the procedures within OTR to process, record, and collect motor fuel taxes. We interviewed and obtained information from OTR officials within its Audit Division, RAA, RPA, RCA, and legal division to determine their roles and responsibilities relative to motor fuel tax collections. Furthermore, we added an objective to review OTR's process to obtain and record bus tax collections during the audit period.

We relied on computer-processed data provided to us, which detailed information on the motor fuel tax for the audit period. Although we did not perform a formal reliability assessment of the computer-processed data, we determined that the hard copy documents we reviewed were reasonable and generally agreed with the information contained in the computer-processed data. We did not find errors that would preclude use of the computer-processed data to meet the audit objectives or that would change the conclusions in this report.

## **INTRODUCTION**

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We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards 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.

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## FINDINGS AND RECOMMENDATIONS

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### FINDING 1: IMPORTER MOTOR FUEL TAX REVENUES

#### SYNOPSIS

We identified that importer motor fuel tax liabilities have gone uncollected for more than 6 years. Unremitted importer motor fuel taxes were the result of: 1) a lack of internal controls in OTR's manual processes for motor fuel tax revenues; 2) insufficient oversight by OTR's Audit Division; and 3) the exclusion of a module in the OTR Tax Integrated System (ITS) that would assign delinquent motor fuel taxes to tax revenue officers to take the necessary enforcement actions. As a result, we identified uncollected motor fuel tax revenues of about \$733,000 for 6 years. We also identified that the District assumed an increased risk of loss due to the miscalculation of bond liability owed by motor fuel taxpayers that would provide monies to cover potential losses from delinquent taxes or damages caused by a fuel spill or other accidents.

#### DISCUSSION

OTR Standard Operating Procedures established policies and procedures to process, manage, and collect the motor fuel taxes. OTR's Returns Processing Administration (RPA) receives and processes motor fuel tax returns and payments. OTR's Audit Division is responsible for managing motor fuel tax returns, processing importer licenses, reviewing tax returns, contacting the taxpayers for mistakes or missing information in the tax return, processing the tax refund documents, and reconciling motor fuel tax returns among. In addition, the Audit Division is responsible for conducting audits of motor fuel taxpayer filings to ensure compliance with laws and regulations and verify the accuracy of tax returns. OTR's RCA is responsible for collecting any delinquent motor fuel tax and taking the necessary enforcement actions.

During our audit, we reviewed 695 motor fuel tax returns for 21 motor fuel taxpayers (out of 70 taxpayers) for FYs 2006 – 2008. We found the following:

- 4 motor fuel tax returns were not scanned into ITS;
- 223 motor fuel tax returns were incomplete (e.g., missing schedules of gas purchases or information about the gas supplier);
- 28 motor fuel tax returns were not filed; and
- 30 motor fuel tax returns were filed late.

## FINDINGS AND RECOMMENDATIONS

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The following subsections (Receipt and Processing, Audit Coverage, Collection Efforts, and Bond Calculation) describe our review of the stages of the motor fuel tax return process and collection and the deficiencies we identified.

### **Receipt and Processing**

OTR's RPA is responsible for scanning the motor fuel tax return documents into ITS. The RPA is also responsible for reviewing the scanning process to ensure correct submission of every document into ITS. OTR's Audit Division shares responsibility with RPA to ensure that every motor fuel tax return and its attached schedules are scanned into ITS. During our audit, we identified four motor fuel tax returns that were not scanned into ITS.

We also found 101 missing schedules from a sample of 695 motor fuel tax returns. We were informed that OTR auditors do not attempt to obtain missing schedules or determine whether they are missing because the taxpayers did not send them or they were never scanned into the ITS. These schedules are necessary to verify the information reported in the tax return and reconcile with other taxpayers returns. Lastly, we found that poor coordination existed between the audit division at OTR, the revenue collection administration within OTR, and the users/responsible persons of the ITS to reconcile and ensure amounts are properly reported and collected.

In addition, we found that 28 motor fuel tax returns were not filed and 30 were filed late. OTR's Audit Division neither enforces D.C. Code § 47-2303(c) requirements nor informs the taxpayers who did not file or filed late about the possible enforcement actions that OTR may take. Furthermore, we found that the ITS does not include a module for Tax Period Delinquency Investigation. This module would generate a notice or a letter if a taxpayer did not file on time. Consequently, a taxpayer may delay for 2-3 years without filing tax returns and OTR takes no action.

Our review further revealed 122 motor fuel tax returns that lacked information about gas suppliers. This information is necessary for the tax auditor to perform reconciliation among the motor fuel taxpayers. OTR's Audit Division did not attempt to obtain this missing information or inform the motor fuel taxpayers about the requirement of filing a complete motor fuel tax return.

OTR needs to establish controls to ensure that amounts entered into the ITS are correct, returns are timely filed, and that related tax liabilities due are collected.

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## FINDINGS AND RECOMMENDATIONS

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### Audit Coverage

The OTR Audit Division consists of 69 tax auditors, whose primary duties include audits of income taxes, sales and use taxes, and other business taxes. Our review disclosed that the Audit Division did not perform any audits of motor fuel tax returns filed in FYs 2006 and 2007. For FY 2008, the Audit Division conducted four audits of the motor fuel tax. OTR Audit Division officials justified the low number of audits performed over motor fuel tax returns by stating that they concentrated their audit efforts on other tax types that produce more revenue for the District than the motor fuel tax. The universe of motor fuel tax returns each year is 840 (excluding bus tax returns) for the 70 identified taxpayers importing fuel into the District. We reviewed 695 motor fuel tax returns, and performed reconciliations of selected fuel purchases reported as purchased from the state of Virginia.

A review of the audit workpapers for the four audits conducted by OTR and discussions with OTR audit personnel, disclosed that OTR auditors did not comply with OTR Standard Operating Procedures (SOP) for auditing motor fuel taxes. Specifically, these procedures require OTR tax auditors to: reconcile inventory to verify that recorded purchases include all receipts of motor fuel and that metered withdrawals from storage are reported accurately in gallon and dollar amounts; obtain a schedule of purchases from the distributor for determining the grade of fuel and gallons involved; and examine whether the volume of gasoline sold appears to be in balance with the volume of gasoline acquired. We found that when performing audits of the motor fuel tax, OTR auditors focused only on examining whether gas was sold to a tax-exempt organization in the District and were not ensuring compliance with OTR SOP requirements.

Further, we were informed that the OTR Audit Division does not audit motor fuel tax returns that do not report a tax liability. Such returns are referred to as “zero tax returns” because the tax is paid to the vendor when purchased in a state outside of the District of Columbia. For example, if a supplier purchases gasoline from a vendor in Virginia to be delivered to a location in the District of Columbia, the supplier is charged the applicable District tax at the time of purchase. It is then the responsibility of the vendor to remit the tax collected for gasoline delivered to the District. The supplier would file a tax return reporting the amount of gallons purchased in Virginia for delivery to the District, and the corresponding amount of tax paid. Because the supplier has already paid the tax, no tax liability would be reported on the supplier’s tax return. OTR should include in their audit selection motor fuel tax returns that do not report any tax liability, and perform a reconciliation of fuel amounts reported as purchased from vendors outside the District, in order to verify the corresponding tax return of the vendor, proper reporting of gallons purchased, corresponding taxes collected, and to ensure that the taxes collected were remitted to the District.

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## FINDINGS AND RECOMMENDATIONS

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While we have commented on the fact that OTR only conducted four audits during the period of our audit, we want to point out that audit coverage is not only a factor of the number performed, but also more importantly the depth of the review. Management should determine the number of audits to be conducted based on a factor of risk, return on investment and available audit resources. In determining how to best use its audit resources, OTR may want to consider implementing a Case Management System that classifies delinquent tax cases by tax type, dollar amount, and tax year. This system would increase productivity and efficiency of the audit division and the RCA by distributing certain tax areas to specific tax revenue officers.

### **Motor Fuel Tax Collection Efforts**

Taxpayers are responsible for filing tax returns on time and paying the full amount owed. If a tax is not fully paid, the ITS generates a 30-day notice, which is mailed to the taxpayer. In addition to the amount of delinquent tax owed, taxpayers will be charged interest (10% compounded daily) and a failure-to-pay penalty (5% monthly up to 25%). If payment is not received, ITS generates a 60-day notice, which is sent to the taxpayer requesting the payment of the delinquent tax immediately.

We were provided data showing that OTR sent out 2 delinquent notices for 21 taxpayers. Some of these notices dated back to 2003. These notices were automatically generated by OTR's ITS system after the taxpayers were 30-days delinquent, and another after 60-days delinquent. We could not find evidence that any of these 21 taxpayers sent payments on their account or contacted OTR to arrange to pay tax liabilities due. More importantly, we found that prior to our on-site fieldwork, no collection efforts were conducted by OTR for motor fuel taxes other than these automatically generated delinquency notices. However, we noted that ITS does not include a module that assigns motor fuel tax returns to OTR revenue officers for review after issuing notices to taxpayers who had delinquent tax.

As soon as OTR officials learned that the ITS did not assign delinquent cases to tax revenue officers, the RCA prepared and sent Statements of Account to these 21 delinquent taxpayers. These statements were dated March 18 and 19, 2009, and included information about the taxpayer's current liability. We determined that the total delinquent motor fuel tax is about \$733,000 (including interest and penalties).

RCA officials stated that the motor fuel tax delinquency is not a collection case; meaning that ITS does not assign cases to tax revenue officers in order to take the necessary enforcement actions. Consequently, for many years, RCA has not taken any collection or enforcement actions regarding the motor fuel tax.

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## FINDINGS AND RECOMMENDATIONS

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### **Bond Calculation**

D.C. Code § 47-2303(a) requires the motor fuel taxpayer to file a bond payable to the District. The bond is calculated based on the sum of 3 times the average monthly motor fuel tax due for the next preceding 12 months or estimated to be due in the next succeeding 12 months. In addition, the statute provides that the bond should not be less than \$5,000 and no more than \$100,000. OTR miscalculated the bond for taxpayers who paid motor fuel tax outside of the District and filed a zero tax return with the District.

A bond provides assurances that losses from delinquent taxes and/or penalties associated therein will be paid. OTR calculates the bond amount based on the amount of taxes due to the District as reported on the importer's monthly tax return. If the taxpayer reports that no tax liability is due to the District because it was paid to another state, OTR will set the bond liability at the minimum (\$5,000). Our interpretation of the bond requirement is that the total tax liability, regardless of whether it was paid to another state outside of the District, should be due based on the volume of importer's business to ensure that the bond is sufficient to recover any uncollected amounts from this taxpayer. Calculating a bond on total taxes due, regardless of amount of taxes paid, could cause the District to have a limited recourse to be made whole. In essence, OTR shifted the bond liability from a taxpayer who is actually selling gas in the District to a third party who is simply collecting the tax for the District. In summary, the bond for each taxpayer should be calculated based on the amount of gas delivered and sold in the District regardless of whether the tax was paid to a third party in another state or directly to the District.

The following example identifies the increased risk of calculating the bond on the amount of tax due rather than the volume of fuel imported. An importer buys 866,000 gallons of gas in 2007 from a supplier in Virginia, files zero tax returns with the District; therefore, his bond liability for FY 2008 is set at the minimum amount of \$5,000. To adequately insure the District against potential loss, we believe that the bond calculation for this taxpayer should have been \$43,000 (866,000 X .20/12 X 3). While we were unable to calculate the total increased risk assumed by the District by not obtaining appropriate bond amounts for the 70 suppliers, we do believe the amounts could be substantial.

### **OTR Chief Counsel Ruling**

OTR referred to its Chief Counsel our finding that bonds to secure the payment of District motor fuel taxes should be set in relation to the volume of the motor fuel taxpayer's business whether the taxes are collected by the District or collected by another state and remitted to the District. An excerpt from that opinion follows:

[T] the term "tax" as used in this statute, is generally understood to refer to taxes imposed by the District, and not taxes imposed by other jurisdictions. *See Kansas ex rei. Taggart v. Holcomb*, 116 P. 251 (Kan. 1911) (ruling that a provision of the Kansas constitution exempting "state" property from

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## FINDINGS AND RECOMMENDATIONS

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taxation applied only to the property of Kansas, although this qualification was not expressly set forth, and the provision did not exempt the property of other jurisdictions that might be located in Kansas).

There is accordingly no basis for taking into account the taxes paid by a licensee to another jurisdiction in computing the required amount of the bond provided under section 47-2303(a). Furthermore, there is no basis for setting the bond amount based on the gallonage of motor fuels imported into the District, as the statute clearly provides that the amount of the bond is to be determined according to the amount of District motor fuel tax due from the licensee. (*See Exhibit C for the entire text of OTR's Chief Counsel's opinion.*)

### OIG Reply

We have reviewed OTR's legal opinion and disagree with the analysis and the applicability of the case cited therein. The bond required of a licensee pursuant to D.C. Code § 47-2303(a) is based upon the taxes due from that licensee to the District, whether the taxes were paid to the District directly by the licensee or a third party, in this case another state. D.C. Code § 47-2306. The situation expounded upon by the OIG during the audit occurred where another state, namely Virginia, collected *District owed* taxes from a licensee and then distributed those sums to the District on behalf of the licensee. Additionally, the tax that is due to the District pursuant to the Motor Fuel Tax is derived from that motor vehicle fuel which is sold or otherwise disposed of within the District of Columbia by a licensee. *See* D.C. Code §§ 47-2305 - 2306. In other words, the volume of motor vehicle fuel brought into the District by a licensee is the direct basis from which the tax liability is determined.

We ask that OTR reconsider its position and require bond liability due from importers to be calculated based on the amount of District motor fuel tax due from the licensee.

### RECOMMENDATIONS

We recommend that the Deputy CFO, OTR, and OCFO:

1. Develop and implement controls to ensure that tax returns scanned into the ITS are correct, and timely filed, and that related tax liabilities are collected.

### OTR RESPONSE

OTR concurs with this recommendation. The Returns Processing Administration will review its procedures to make sure that returns are scanned as required. It will also take advantage of the Integrated Tax System's capability to suspend incomplete returns and notify taxpayers to supply missing schedules. The full text of OTR's response is included at Exhibit B.

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## FINDINGS AND RECOMMENDATIONS

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### OIG COMMENT

We consider actions taken by OTR to be responsive to our recommendation.

We recommend that the Deputy CFO, OTR, and OCFO:

2. Establish procedures to ensure coordination between the audit division at OTR, the revenue collection administration within OTR, and the users/responsible persons of the ITS to reconcile and ensure amounts are properly reported and collected.

### OTR RERESPONSE

OTR concurs with this recommendation. OTR will utilize the automated tax system's capability of identifying stop filers and the collection department will contact them regarding their missing returns. OTR has undertaken to collect the receivables from the 21 taxpayers referred to in your report. To improve collections going forward, OTR is modifying its billing stream across all tax types to send a 3rd billing to reflect the application of O-type collection fees, an enhancement expected to be operation during FY 2009. During FY 2010, OTR expects to modify its billing stream to generate an annual bill. OTR will review its case assignment system to make sure that motor fuel tax collection cases are assigned to revenue officers or collection agencies. The full text of OTR's response is included at Exhibit B.

### OIG COMMENT

We consider actions taken by OTR to be responsive to our recommendation.

We recommend that the Deputy CFO, OTR, and OCFO:

3. Adopt a quality control system to ensure that the internal auditors are complying with OTR SOP requirements. For example, OTR tax auditors should: 1) reconcile inventory to verify that recorded purchases include all receipts of motor fuel and that metered withdrawals from storage are reported accurately in gallon and dollar amounts; 2) obtain a schedule of purchases from the distributor for determining the grade of fuel and gallons involved; and 3) examine whether the volume of gasoline sold appears to be in balance with the volume of gasoline acquired.

### OTR RERESPONSE

OTR concurs with this recommendation. The audit department will ensure that audits of motor fuel companies include the verification of recorded purchases and withdrawals, obtaining a schedule of purchases from the distributor, and examining whether the volume of motor fuel sold appears in balance with the volume acquired, in accordance with OTR Standard Operating Procedures. The audit department will, moreover, expand its audit coverage to include motor

## **FINDINGS AND RECOMMENDATIONS**

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fuel tax accounts that do not report any tax liability. The full text of OTR's response is included at Exhibit B.

### **OIG COMMENT**

We consider actions taken by OTR to be responsive to our recommendation.

We recommend that the Deputy CFO, OTR, and OCFO:

4. Establish a Case Management System that classifies delinquent tax cases by tax type, dollar amount, and tax year. This system would increase productivity and efficiency of the audit division and Revenue Collection Administration by distributing certain tax areas to specific tax revenue officers.

### **OTR RERESPONSE**

OTR concurs with this recommendation. OTR has committed to replacing its existing integrated tax system with a more modern system that will include a state of the art case management system providing the recommended functionality across all tax types. OTR has hired a program manager to oversee this process and a contract for RFP services is now being let. OTR expects to issue an RFP during FY 2010. The full text of OTR's response is included at Exhibit B.

### **OIG COMMENT**

We consider actions taken by OTR to be responsive to our recommendation.

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## FINDINGS AND RECOMMENDATIONS

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<b>FINDING 2: INTERSTATE BUS TAX REVENUES</b>
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We found that the District did not implement previously agreed-to recommendations and, therefore, lost interstate bus tax revenues totaling at least \$2.3 million over the last 10 years (\$229,000 annually) by not participating in the International Fuel Tax Agreement managed by the International Fuel Tax Association (IFTA). The last time the District applied for membership in IFTA was in 1999. The District's application was rejected because its proposal did not conform to IFTA regulations and requirements; and the DMV was non-compliant with International Registration Plan (IRP) requirements. This exact issue was reported in a previous audit issued by our Office almost 5 years ago.

### RESULTS OF PREVIOUS AUDIT

OIG audit report No. 04-2-07KV(a), issued in December 2004, recommended that the Director of DMV contact IFTA to identify what changes or corrections were needed to gain acceptance into IFTA. The report also recommended that DMV work closely with the District's OTR to ensure that a successful reapplication for IFTA membership was achieved. OTR did not take any corrective actions to implement the OIG's recommendations.

DMV concurred with the recommendations and reported that the agency initiated action, which addressed the issues identified. In response, the Director stated that the DMV was working with the OCFO to reapply for IFTA membership and for participation in the IFTA Clearinghouse.

### DISCUSSION

IFTA is an agreement among 60 jurisdictions in the United States and Canada to simplify the reporting of fuel used by motor carriers operating in more than 1 jurisdiction. Persons who operate qualified motor vehicles<sup>1</sup> in more than one jurisdiction are subject to IFTA licensing. In FY 2009, the Office of the City Administrator assigned responsibility for applying for and obtaining IFTA membership to DDOT.

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<sup>1</sup> IFTA's Articles of Agreement (rev. Jan. 2008) defines "qualified motor vehicle" as one designed, or maintained for transportation of persons or property and: 1) has 2 axles and a gross vehicle weight or registered gross vehicle weight exceeding 26,000 pounds or 11,797 kilograms; 2) has 3 or more axles regardless of weight; or 3) is used in combination, when the weight of such combination exceeds 26,000 pounds or 11,797 kilograms gross vehicle or registered gross vehicle weight. Recreational vehicles are excluded.

*Id.* at 12.

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## FINDINGS AND RECOMMENDATIONS

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Title 49 U.S.C.S. § 31705 provides that “after September 30, 1996, a State may establish, maintain, or enforce a law or regulation that has a fuel use tax reporting requirement (including any tax reporting form) only if the requirement conforms with the International Fuel Tax Agreement.” As a result, Title 47 of D.C. Code was amended to provide for membership in IFTA. Since 1997, the District attempted three times to obtain membership into IFTA; the last attempt was in October 1999. OTR efforts were unsuccessful and the applications for membership were denied. The District was rejected for membership because the District’s proposal did not conform to IFTA regulations and requirements and because of the DMV’s non-compliance with IRP requirements. An example of how the IFTA program works is discussed in detail below.

### **Interstate Bus Tax Scenario**

An operator of an IFTA vehicle purchases 100 gallons of fuel in Maryland. The vehicle consumes 60 gallons of fuel while operating on roads in Maryland and consumes 40 gallons of fuel on Virginia roads. The fuel tax of \$.2425 per gallon<sup>2</sup> or \$14.55 (for the 60 gallons) is retained by Maryland, while fuel tax of \$.1750 per gallon<sup>3</sup> or \$7.00 (for the 40 gallons) is paid to Virginia by the state of Maryland after the vehicle operator files the quarterly IFTA tax report.

Using the same information and substituting the District of Columbia for Virginia, Maryland would retain the fuel taxes for the fuel consumed in Maryland and refund the carrier for the fuel taxes paid on the 40 gallons consumed in the District. In essence, the District’s licensed carriers receive a windfall of the fuel taxes paid for fuel consumed in the District, which would have gone to the District if it were an IFTA member.

For 10 years, OTR and DMV did not attempt to reapply for IFTA membership. The total interstate bus tax refund for FYs 2006, 2007, and 2008 was \$687,000. The average refund is \$229,000 a year. The total interstate bus tax refund for 10 years is approximately \$2,290,000. Had OTR continued its efforts to apply for IFTA membership, this lost amount could have been tax revenue for the District.

The revenue lost to the District increases substantially when mileage logged by vehicles registered in other jurisdictions, in addition to tour bus<sup>4</sup> mileage, is considered. The Metropolitan Washington Council of Governments’ Transportation Department, which routinely monitors all motor vehicle traffic that enters the District, estimates that over 3,700 IFTA-qualified vehicles travel on the District’s roadways on an average weekday.

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<sup>2</sup> Maryland’s 2<sup>nd</sup> Quarter 2009 per gallon fuel tax rate from IFTA Fuel Tax Matrix.

<sup>3</sup> Virginia’s 2<sup>nd</sup> Quarter 2009 per gallon fuel tax rate from IFTA Fuel Tax Matrix.

<sup>4</sup> Unlike the IRP program, tour buses are qualified IFTA vehicles.

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## FINDINGS AND RECOMMENDATIONS

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IFTA also provides a Clearinghouse service for IFTA participants, similar to the IRP Clearinghouse that would enhance the processing of IFTA payments to and from other IFTA jurisdictions. This service would reduce the administrative responsibilities required to administer the IFTA program in the District. In conclusion, DDOT should take action to prepare a successful application for IFTA membership and use the IFTA Clearinghouse for processing IFTA transactions.

### **Improper Interstate Bus Tax Collections**

Conversely, by not being a current member of IFTA, OTR has improperly retained \$54,700 collected in FYs 2006 – 2008 from bus companies who sent payments based on their motor fuel usage in the District. These companies are unaware that the District is not a member of IFTA and, therefore, is ineligible to collect bus tax revenues. We determined that the District has been ineligible since 1996 but OTR has continued to collect the motor fuel use tax on buses.

The Chief of the Audit Division justified this practice and stated that the small bus taxpayers do not ask for their tax back, so OTR keeps it. In addition, the improperly collected interstate bus tax should be recognized in the accounting record as a liability. However, OTR records these amounts as revenue. We informed OTR officials at the RAA of this accounting mistake, and they agreed to take the necessary corrective action.

### **RECOMMENDATIONS**

We recommend that the Director, DDOT:

5. Contact IFTA to identify what changes or corrections are needed in the DDOT's administration of the IRP program to ensure compliance and to gain acceptance in IFTA.
6. Complete actions necessary to participate in the IFTA Clearinghouse for processing and payment of fuel taxes.

### **OTR RESPONSE:**

The Office of Tax and Revenue concurs with these recommendations. The District Department of Transportation has advised OTR that it will undertake coordinating the IFTA application process. OTR has committed to provide any necessary assistance.

### **OIG COMMENT**

We consider actions taken by OTR to be responsive to our recommendations.

**EXHIBIT A: POTENTIAL MONETARY BENEFITS  
RESULTING FROM AUDIT**

<b>Recommendations</b>	<b>Description of Benefit</b>	<b>Amount and Type of Benefit</b>	<b>Agency Reported Estimated Completion Date</b>	<b>Status<sup>5</sup></b>
1	Internal Control. Implements controls over the manual processing of motor fuel tax returns to ensure that that amounts entered into the system are correct and timely filed, and that related tax liabilities due are collected.	None	To Be Determined	Closed
2	Internal Control. Establishes procedures to ensure coordination between the audit section at OTR, the collection department within OTR, and the users/responsible persons of the ITS to reconcile and ensure amounts are properly reported and collected.	\$733,000	To Be Determined	Closed
3	Program Efficiency. Adopts a quality control system to ensure that the auditors comply with OTR SOP requirements.	None	To Be Determined	Closed
4	Internal Control. Establishes a Case Management System that classifies delinquent tax cases by tax type, dollar amount, and tax year.	None	To Be Determined	Closed
5	Economy and Efficiency. Identifies what changes or corrections are needed in the DDOT's administration of the IRP program to ensure compliance and to gain acceptance in IFTA.	None	To Be Determined	Open
6	Economy and Efficiency. Ensures the District's participation in the IFTA Clearinghouse for processing and payment of fuel taxes.	\$2.3 million (\$229,000 annually for past 10 years)	To Be Determined	Open

<sup>5</sup> This column provides the status of a recommendation as of the report date. For final reports, "Open" means management, and the OIG agree on the action to be takes, but is not complete. "Closed" means management has advised that the action necessary to correct the condition is complete. If a completion date was not provided, the date of management's response is used. "Unresolved" means that management has agreed to neither take the recommended action nor proposed satisfactory alternative actions to correct the condition.

## EXHIBIT B: MANAGEMENT RESPONSE

GOVERNMENT OF THE DISTRICT OF COLUMBIA  
Office of the Chief Financial Officer  
Office of Tax and Revenue



Stephen M. Cordi  
Deputy Chief Financial Officer

June 29, 2009

Charles J. Willoughby  
Inspector General  
717 14<sup>th</sup> Street, N.W.  
Washington, DC 20005

Re: Motor Fuel Sales and Tax Process  
OIG No. 09-2-02KA

Dear Mr. Willoughby:

Your letter of June 9, 2009 provides Mr. Gabe Klein, Director, District Department of Transportation, and me with your draft report summarizing the results of your audit of the motor fuel sales and tax process.

The Office of Tax and Revenue (OTR) has had an opportunity to review the draft report. I am pleased to provide with our comments with respect to those issues which pertain to the Office of Tax and Revenue.

**Recommendation 1 – Implementing controls over the manual processing of motor fuel tax returns to ensure that amounts are correct and timely filed and that related tax liabilities due are collected.**

OTR concurs with this recommendation. The Returns Processing Administration will review its procedures to make sure that returns are scanned as required. It will also take advantage of the Integrated Tax System's capability to suspend incomplete returns and notify taxpayers to supply missing schedules.

**Recommendation 2 – Establishing procedures to ensure coordination between the audit section at OTR, the collection department within OTR, and the users/responsible persons of the ITS to reconcile and ensure amounts are properly reported and collected.**

OTR concurs with the recommendation to make sure that returns are timely filed. OTR will utilize the automated tax system's capability of identifying stop filers and the collection department will contact them regarding their missing returns.

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## EXHIBIT B: MANAGEMENT RESPONSE

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OTR has undertaken to collect the receivables from the 21 taxpayers referred to in your report. To improve collections going forward, OTR is modifying its billing stream across all tax types to send a 3<sup>rd</sup> billing to reflect the application of O-type collection fees, an enhancement expected to be operation during FY 2009. During FY 2010, OTR expects to modify its billing stream to generate an annual bill.

OTR will review its case assignment system to make sure that motor fuel tax collection cases are assigned to revenue officers or collection agencies. Under present procedures, lower dollar cases are assigned to a private collection agency for collection.

OTR referred to the Chief Financial Officer's General Counsel the recommendation that bonds to secure the payment of motor fuel taxes be set in relation to the volume of the motor fuel taxpayer's business whether the taxes are paid to the District or a state outside the District and not simply in relation to the taxes owed the District of Columbia. We have now been advised that the District may not require a bond in excess of three times the taxpayer's monthly motor fuel liability to the District. I have attached a copy of that opinion.

**Recommendation 3 – Adopting a quality control system to ensure that the internal auditors are complying with OTR operating procedures.**

OTR concurs with this recommendation. The audit department will ensure that audits of motor fuel companies include the verification of recorded purchases and withdrawals, obtaining a schedule of purchases from the distributor and examining whether the volume of motor fuel sold appears in balance with the volume acquired, in accordance with OTR Standard Operating Procedures.

The audit department will, moreover, expand its audit coverage to include motor fuel tax accounts which do not report any tax liability.

**Recommendation 4 – Establishing a Case Management System that classifies delinquent tax cases by tax type, dollar amount, and tax year.**

OTR concurs with this recommendation. OTR has committed to replacing its existing integrated tax system with a more modern system that will include a state of the art case management system providing the recommended functionality across all tax types. OTR has hired a program manager to oversee this process and a contract for RFP services is now being let. OTR expects to issue an RFP during FY 2010.

The final two recommendations relate to the District of Columbia becoming a participant in the International Fuel Tax Agreement (IFTA). The Office of Tax and Revenue concurs with these recommendations. The District Department of Transportation has advised OTR that it will undertake coordinating the IFTA application process. OTR has committed to provide any necessary assistance.

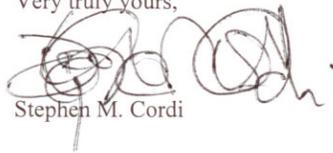
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## EXHIBIT B: MANAGEMENT REPOSENSE

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Thank you for the opportunity to respond to your audit recommendations. Please feel free to contact me if additional explanation is required.

Very truly yours,



Stephen M. Cordi

SMC: cs

Enclosure

cc: Dr. Natwar M. Gandhi, Chief Financial Officer  
Mr. Neil O. Albert, City Administrator, District of Columbia  
Mr. William Singer, Chief of Budget Execution  
Mr. Robert Andary, Executive Director, Office of Integrity and Oversight  
Mr. Gabe Klein, Director, District Department of Transportation

## EXHIBIT C: OTR CHIEF COUNSEL RULING

### GOVERNMENT OF THE DISTRICT OF COLUMBIA

Office of the Chief Financial Officer  
Office of Tax and Revenue



June 29, 2009

Stephen M. Cordi  
Deputy Chief Financial Officer  
Office of Tax and Revenue  
941 North Capitol Street, NE  
Washington, DC 20002

Re: Bonding Requirements of Motor Fuel Licensees

Dear Mr. Cordi:

Reference is made to your recent request for an opinion concerning the computation of the amount of bond required under D.C. Official Code § 47-2303(a) in connection with the issuance of a motor fuel importer's license.

The statute provides in pertinent part:

At the time of applying for [an importer's] license the applicant shall pay to the Collector of Taxes as an annual license fee the sum of \$5 and shall file with the Mayor of the District of Columbia a bond in the form to be prescribed by the Mayor, in the approximate sum of 3 times the average monthly motor fuel tax due from said such importer during the next preceding 12 months, or estimated to be so due in the next succeeding 12 months, to be executed by a surety company duly licensed to do business under the laws of the District of Columbia, payable to the District of Columbia and conditioned upon the prompt payment of any and all taxes and penalties, levied and imposed in § 47-2301 and this section to the Collector of Taxes of the District of Columbia, and generally upon faithful compliance with the terms of §§ 47-2301 to 47- 2315 by such importer; provided, that in no case shall such bond be less than \$5,000 nor more than \$100,000.

The foregoing language makes clear that the bond is to secure prompt payment of the taxes imposed by sections 47-2301 and 47-2303, as well as compliance with the other provisions of the District's motor fuel tax. The amount of the bond is to be determined according to the "average monthly motor fuel tax due," but in no case shall the bond be less than \$5,000. Given the purpose and language of the statute, it is clear that the tax upon which the amount of the bond is to be calculated is the tax imposed by the District under the referenced statutes.

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## EXHIBIT C: OTR CHIEF COUNSEL RULING

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Stephen M. Cordt

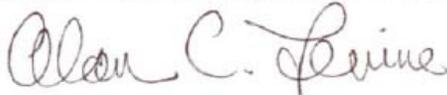
June 29, 2009

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Moreover, as a matter of statutory interpretation, the term "tax" as used in this statute, is generally understood to refer to taxes imposed by the District, and not taxes imposed by other jurisdictions. See Kansas ex rel. Taggart v. Holcomb, 116 P. 251 (Kan. 1911) (ruling that a provision of the Kansas constitution exempting "state" property from taxation applied only to the property of Kansas, although this qualification was not expressly set forth, and the provision did not exempt the property of other jurisdictions that might be located in Kansas).

There is accordingly no basis for taking into account the taxes paid by a licensee to another jurisdiction in computing the required amount of the bond provided under section 47-2303(a). Furthermore, there is no basis for setting the bond amount based on the gallonage of motor fuels imported into the District, as the statute clearly provides that the amount of the bond is to be determined according to the amount of District motor fuel tax due from the licensee.

Please let me know if you have further questions on this matter.



Alan C. Levine

Chief Counsel

Office of Tax and Revenue