



*Procurement's Control Environment Was
Ineffective and Did Not Prevent
Overpayments to Contractors*

March 28, 2008

Reference Number: 2008-10-092

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

Redaction Legend:

3(d) = Identifying Information - Other Identifying Information of an Individual or Individuals



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 28, 2008

MEMORANDUM FOR CHIEF, AGENCY-WIDE SHARED SERVICES

FROM: *Michael R. Phillips*
Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Procurement’s Control Environment Was Ineffective and Did Not Prevent Overpayments to Contractors (Audit # 200710035)

This report presents the results of our review of the Office of Procurement’s (Procurement) voucher/invoice verification process. The overall objective of this review was to perform a trend analysis of common issues and findings identified in previously issued invoice and voucher audits. This audit was conducted as part of our commitment to review the Internal Revenue Service’s (IRS) procurement activities.

Impact on the Taxpayer

Most IRS mission critical programs rely on contract support. Because contract expenditures represent a significant outlay of IRS funds, the Treasury Inspector General for Tax Administration audited some of these expenses and issued 16 reports from September 2003 through April 2007.¹ The internal controls and practices the IRS had in place to verify contract charges were not effective during the period covered by these audits. In the voucher/invoice payments sampled (approximately \$117 million), we identified approximately \$7.5 million (6 percent) in questionable charges and 2 instances of contractors submitting false claims for reimbursement. Without effective practices and internal controls in place to verify contract charges, the IRS is at risk of making improper payments and misusing taxpayer funds.

¹ See Appendix V.



Procurement's Control Environment Was Ineffective and Did Not Prevent Overpayments to Contractors

Synopsis

The internal controls and practices the IRS had in place to verify contract charges were not effective during the period covered by the 16 prior voucher/invoice payment audits included in this report. In 15 of the 16 reports, we identified weaknesses in the control environment regarding the voucher/invoice verification process. The IRS did not perform comprehensive verifications of actual hours worked or a detailed review of travel expenses but simply accepted the contractors' certifications. We also reported in two of the audit reports that the IRS was not verifying the skills/qualifications of contractor employees and, therefore, overpaid the contractors for employees not qualified for the charged positions. Interviews confirmed that designated IRS employees did not believe they were provided with sufficient written verification procedures, adequate training, or sufficient contractor supporting documentation to perform their duties. Unless adequate supporting documentation for charges and contractor employee qualifications is obtained and reviewed, the IRS cannot assure the accuracy and allowability of the charges included on the invoices/vouchers. This overall weak control environment puts the IRS at risk of making improper payments.

In response to our audits, Procurement has developed a Guidebook for Acquisition Practices (Guidebook)² that provides a detailed process for reviewing vouchers/invoices. Procurement planned to have this Guidebook distributed to all Contracting Officer's Technical ^{3(d)} Representatives by the end of Calendar Year 2007.

In addition, we identified two instances, [REDACTED] in which corrective actions were reported as being completed even though all the questionable charges had not been recovered. We do not believe this condition is indicative of a Procurement-wide systemic problem. Nonetheless, we reported the issue to Procurement management, who agreed to change the reporting process and to ensure all agreed-to questionable charges are recovered before they close corrective actions.

Recommendation

We recommended the Director, Procurement, provide training on the Guidebook and follow up to ensure it is being used to verify vouchers and invoices. The Guidebook should be revised to include a résumé review to ensure contractor employees are qualified for the positions at which they are being charged.

² The Guidebook is a web-based system that includes standardized process, procedures, templates, and best practices used by Contracting Officers, Contracting Officer's Technical Representatives, and Procurement customers.



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Response

IRS management agreed with our recommendation. Training on the Guidebook for Acquisition Practices Voucher/Invoice Review process was provided to Procurement personnel in October 2007. The Guidebook will be revised to include a contractor employee qualification/verification process, and training will be provided on this process. A quality review process will be implemented to monitor compliance with the voucher verification process. The Guidebook will be discussed at the 2008 Acquisition Planning Conference and copies made available to all attendees. Management's complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report recommendation. Please contact me at (202) 622-6510 if you have questions or Nancy A. Nakamura, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.



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Abbreviations

CO	Contracting Officer
COTR	Contracting Officer's Technical Representative
DCAA	Defense Contract Audit Agency
IRS	Internal Revenue Service



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Background

The Office of Procurement (Procurement) is a key partner in accomplishing the Internal Revenue Service (IRS) mission. Most IRS mission critical programs rely on contract support. Procurement's mission is to deliver world-class, customer-focused acquisition services with the highest degree of integrity and the cooperative effort of partners. Procurement's vision is to be the best acquisition organization in the Federal Government, with the best people, practices, and performance.

Procurement's vision is to be the best acquisition organization in the Federal Government with the best people, practices, and performance.

Because contract expenditures represent a significant outlay of IRS funds, the Treasury Inspector General for Tax Administration committed to audit these expenditures. We performed 16 audits¹ from September 2003 through April 2007, focusing on whether amounts paid by the IRS under various contracts were accurate, supported, and allowable.

Our contract audit responsibility includes audits of both the IRS' management of Procurement and contractors' performance. The Treasury Inspector General for Tax Administration has an interagency agreement in place with the Defense Contract Audit Agency (DCAA) to conduct audits of the contractors doing business with the IRS. These include DCAA audits of proposals, incurred costs, cost accounting systems, financial capability, forward pricing, termination claims, defective pricing, and progress payments. In Fiscal Years 2006 and 2007, we issued 107 audit reports relating to DCAA contract audits.

This review was performed at Procurement in the Office of Agency-Wide Shared Services in Oxon Hill, Maryland, during the period June through November 2007. 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

¹ See Appendix V.



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Results of Review

An Incomplete Voucher/Invoice Verification Process Resulted in the Payment of Questionable Contract Charges

The internal controls and practices the IRS had in place to verify contract charges were not effective during the period covered by the audits included in this review. We analyzed 16 audit reports issued from September 2003 through April 2007, 15 of which identified weaknesses in the control environment regarding the voucher/invoice verification process.² These audits included the review of approximately \$117 million in voucher/invoice payments out of approximately \$2 billion (6 percent) paid on the contracts at the time the audits were performed. The audits identified approximately \$7.5 million (6 percent) in questionable charges. In addition, our analysis of DCAA reports issued in Fiscal Years 2006 and 2007 identified approximately \$167 million in questionable charges directly related to IRS contracts. In our opinion, these questionable charges are the result of ineffective controls and practices the IRS had in place to verify whether contract charges were accurate, supported, and allowable before it made payments to contractors.

Another result of the ineffective controls is the potential nonidentification of illegal acts. The Treasury Inspector General for Tax Administration referred 1 of the contractors included in the 16 reports to our Office of Investigations for potential fraud. In this instance, the contractor overstated expenses and understated related income to justify more than \$1.3 million in false claims for reimbursement. This case was successfully prosecuted, with the two individuals involved in the fraud pleading guilty and agreeing to pay restitution. The Office of Audit worked with the Office of Investigations on another case involving contract fraud. In this instance, the contractor pleaded guilty to making false and fraudulent claims. We believe that if sufficient cost-verification controls had been in place, these two instances might have been identified or even prevented.

Examples of the ineffective controls and practices we reported involved the IRS not having a consistent and complete voucher/invoice verification process. The IRS did not perform comprehensive verifications of actual hours worked, such as a review of the contractor's time reports, or a detailed review of all contractor travel expenses through a verification of supporting receipts. In addition, in 2 of the 16 reports, we found that the IRS was not verifying, through a review of résumés, the skills/qualifications of the contractor employees. Therefore, the IRS overpaid the contractor for employees not qualified for the charged positions.

² See Appendix V.



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The Federal Acquisition Regulation³ stipulates that contracts may be entered into and signed on behalf of the Federal Government only by Contracting Officers (CO). The COs have the authority to administer or terminate contracts and make related determinations and findings. The Regulation also states that the CO is responsible for ensuring the performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the Federal Government in its contractual relationships.

The Contracting Officer's Technical Representative (COTR) is the designated program office official. The program office nominates a COTR, who is the CO's technical expert and representative in the administration of a contract. Usually, the CO will appoint the COTR by issuing a signed letter of appointment tailored to meet the needs of each contract. IRS guidance includes a sample appointment letter that outlines delegated authorities of the COTR. These authorities include requirements for (1) reviewing contractor vouchers/invoices to ensure they accurately reflect the work completed in accordance with the requirements of the contract, (2) certifying acceptance, and (3) forwarding a copy of the invoice to the CO. However, the appointment letters are a broad delegation of authority from the CO to the COTR to perform various contract administrative functions. They do not provide specifics as to how to perform the duties.

The COTRs interviewed concerning specific performance direction during the course of the 16 audits identified the following reasons why consistent, comprehensive verifications of voucher/invoice charges were not performed (i.e., weak internal controls):

- COTRs did not receive any written procedural guidance from within the IRS.
- COTRs did not receive adequate training for their assigned tasks.
- At times, contractors were not required to provide supporting documentation for voucher/invoice charges.

3(d) In addition, [REDACTED]

[REDACTED] However, our analysis of DCAA reports we issued in Fiscal Years 2006 and 2007 showed that nine contractors had reported issues with one or more of their systems (e.g., accounting system, budgeting and planning system, indirect and other direct costs system, billing system). Therefore, these systems should not have been relied upon to properly accumulate, segregate, report, and charge costs for Federal Government contracts.

Unless adequate supporting documentation for invoiced charges and contractor employee qualifications is obtained and reviewed, the IRS cannot assure the accuracy and allowability of the charges included on the vouchers/invoices. This puts the IRS at risk of making improper contractor payments and misusing taxpayer funds.

³ 48 C.F.R. ch. 1 (2006).



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In response to our audits, Procurement has developed a Guidebook for Acquisition Practices (Guidebook)⁴ which provides a detailed process for reviewing vouchers/invoices. A Procurement official stated that the Guidebook should be distributed to all COTRs by the end of Calendar Year 2007. The Guidebook includes checklists for detailed voucher/invoice reviews, including ensuring adequate supporting documentation (e.g., timesheets, travel receipts) is submitted by the contractor.

Recommendation

Recommendation 1: The Director, Procurement, should provide training on the Guidebook and follow up to ensure that all COTRs receive and use the voucher verification guidance developed as part of the Guidebook. In addition, the Guidebook should be revised to include reviewing résumés to ensure that contractor employees are qualified for the positions at which they are being charged.

Management's Response: The IRS agreed with the recommendation. Training on the Guidebook Voucher/Invoice Review process was provided to Procurement personnel in October 2007. In addition, the Director, Procurement, will take the following actions:

- The Guidebook will be revised to include a contractor employee qualification/verification process.
- Training will be provided on the revised contractor employee qualification/verification guidance.
- A quality review process will be implemented to monitor compliance with the voucher verification guidance.
- The 2008 Acquisition Planning Conference will include a discussion on the Guidebook process, and copies of the Guidebook will be available to attendees.

Corrective Actions Were Closed Before Ensuring Questionable Charges Were Recovered

We analyzed corrective actions taken for the 14 of 16 prior voucher/invoice payment audit reports that contained recommendations. Audit recommendations and corrective actions are tracked on the Department of the Treasury Joint Audit Management Enterprise System to ensure corrective actions are taken in a timely manner. At the time of this review, the System indicated the IRS had closed corrective actions for the recommendations in 11 of the 14 audits, reporting recovery of approximately \$87,000. Corrective actions for recommendations in the remaining

⁴ The Guidebook is a web-based system that includes standardized processes, procedures, templates, and best practices used by COs, COTRs, and Procurement customers.



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three reports had not been completed at the time of our review. However, Procurement officials informed us they planned to recover an additional \$2.8 million from the contractors evaluated in these 3 prior audit reports.

Our analysis of the corrective actions reported as being taken (completed) identified two instances, [REDACTED] in which none of the questionable charges had been recovered. Discussions with Procurement officials confirmed that they had closed the corrective actions on the System when [REDACTED]

3(d)

[REDACTED] After we brought this condition to Procurement's attention, responsible managers stated that they would [REDACTED]

[REDACTED] In addition, Procurement management agreed to change the reporting process and to ensure that all agreed-to questionable charges are recovered before they close the corrective action. Because both of these instances [REDACTED] and were unique, we do not believe this condition is indicative of a Procurement-wide systemic problem or a contractor integrity issue. Therefore, we are making no recommendation.

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⁵ See Appendix IV.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to perform a trend analysis of common issues and findings identified in previously issued invoice and voucher audits.¹ To accomplish our objective, we:

- I. Performed a trend analysis of common issues and findings from Treasury Inspector General for Tax Administration audit reports related to invoice and voucher processing.
 - A. Identified 16 invoice/voucher payment audit reports issued from September 2003 through April 2007.
 - B. Analyzed the reports and identified conditions and recommendations that were indicative of Procurement control or process weaknesses.
- II. Performed a trend analysis of common issues and findings from DCAA audit reports related to contractor invoice and voucher processing.
 - A. Identified 107 DCAA audit reports issued during Fiscal Years 2006 and 2007.
 - B. Analyzed the DCAA reports and identified similar conditions and recommendations that could contribute to Procurement-wide control or process weaknesses.
- III. Performed a trend analysis of common issues and findings from Treasury Inspector General for Tax Administration Office of Investigations cases.
 - A. Identified two Office of Investigations procurement-related cases resolved in Fiscal Years 2006 and 2007.
 - B. Analyzed case information and identified similar conditions and outcomes that could contribute to Procurement-wide control or process weaknesses.
- IV. Confirmed whether planned corrective actions were taken to resolve the individual conditions identified in our audit reports.
 - A. Confirmed with Procurement officials whether all actions had been completed.
 - B. Obtained documentation to support completed corrective actions.

¹ See Appendix V.



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Appendix II

Major Contributors to This Report

Nancy A. Nakamura, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

Alicia P. Mrozowski, Director

Thomas Brunetto, Audit Manager

Terrey Haley, Senior Auditor

Debra Kisler, Senior Auditor

James Mills, Auditor



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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Acting Chief of Staff C
Deputy Commissioner for Operations Support OS
Director, Procurement OS:A:P
Chief Counsel CC
National Taxpayer Advocate TA
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
Office of Internal Control OS:CFO:CPIC:IC
Audit Liaisons:
 Chief, Agency-Wide Shared Services OS:A
 Director, Procurement OS:A:P



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Appendix IV

Outcome Measure

This appendix presents detailed information on the measurable impact that our audit will have on tax administration. This benefit will be incorporated into our Semiannual Report to Congress.

3(d)

Type and Value of Outcome Measure:

- Reliability of Information – Actual [REDACTED] (see page 4).

Methodology Used to Measure the Reported Benefit:

Our analysis of the corrective actions reported as being taken on the 14 of 16 prior voucher/invoice payment audit reports¹ that contained recommendations identified 2 instances, [REDACTED] in which the corrective actions were reported as being completed even though all the questionable charges had not been recovered. Discussions with Procurement officials confirmed that they had closed the corrective actions on the Department of the Treasury Joint Audit Management Enterprise System [REDACTED]

3(d)

[REDACTED] After we brought this condition to Procurement's attention, responsible managers stated that they would [REDACTED]

3(d)

3(d)

3(d)

¹ See Appendix V.



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Appendix V

List of Voucher/Invoice Verification Audit Reports

Audit of Personnel Classification Support Services Contract (Reference Number 2003-10-194, dated September 2003)

Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract (Reference Number 2004-10-117, dated June 2004)

Review of the Nationwide Electronic Tax Forum Conferences and Exhibitions Contract (Reference Number 2004-10-128, dated July 2004)

Audit of the Asset Seizure and Forfeiture Program Contract (Reference Number 2004-10-174, dated September 2004)

Voucher Audit of the Treasury Information Processing Support Services Contract – TIRNO-00-D-00014 (Reference Number 2005-10-076, dated April 2005)

Voucher Audit of the Treasury Information Processing Support Services Contract – TIRNO-00-D-00015 (Reference Number 2005-10-124, dated August 2005)

Voucher Audit of the Treasury Information Processing Support Services Contract – TIRNO-00-D-00013 (Reference Number 2005-10-145, dated September 2005)

Voucher Audit of the Integration Support Contract – TIRNO-92-C-00014 (Reference Number 2005-10-162, dated September 2005)

Voucher Audit of the Federal Financial System Software Technical Support Services Contract – TIRNO-04-T-00116 (Reference Number 2006-10-027, dated December 2005)

Invoice Audit of the Taxpayer Burden Simulation Models Contract – TIRNO-03-D-00001 (Reference Number 2006-10-060, dated March 2006)

Invoice Audit of the Microsoft Consulting Services Contract – TIRNO-03-K-00191 (Reference Number 2006-10-086, dated June 2006)

Voucher Audit of the Infrastructure Shared Services Task Order of Contract TIRNO-99-D-00001 (Reference Number 2006-10-087, dated June 2006)

Voucher Audit of the Federally Funded Research and Development Center Contract – TIRNO-99-D-00005 (Reference Number 2006-10-140, dated August 31, 2006)

Invoice Audit of the Management of Seized and Forfeited Assets Contract – TIRNO-05-C-00010 (Reference Number 2007-10-025, dated January 11, 2007)



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Voucher Audit of the Information Processing Support Services Contract – TIRNO-00-D-00009
(Reference Number 2007-10-050, dated February 27, 2007)

Invoice Audit of the Financial Statement/Government Accountability Office Audit Support Services Contract – TIRNO-03-K-00167 (Reference Number 2007-10-069, dated April 23, 2007)



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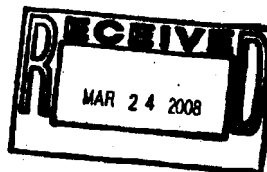
Appendix VI

Management's Response to the Draft Report



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

March 24, 2008



MEMORANDUM FOR MICHAEL R. PHILLIPS
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

James P. Falcone *James P. Falcone*
Chief, Agency-Wide Shared Services

SUBJECT:

Draft Audit Report – Procurement's Control Environment
Was Ineffective and Did Not Prevent Overpayments to
Contractors (Audit #200710035) (I-trak #2008-33507)

Thank you for the opportunity to respond to the subject audit report. The audit was conducted to perform a trend analysis of common issues and findings identified in previous invoice and voucher audits.

The audit reviewed 16 previous reports, 15 of which identified weaknesses in the invoice/voucher verification control environment where hours worked and claimed travel were accepted based simply on the contractor's certification. Two previous audits identified that skills and qualifications of contractor employees were not verified resulting in overpayment for employees who were not qualified for the charged positions.

As noted in your report, we have developed a Guidebook for Acquisition Practices (GAP) which includes a Voucher/Invoice Review process. Training has been provided for this process and additional training is planned throughout this fiscal year for our field offices. Additionally, to increase communications, our annual Advanced Acquisition Planning Conference will include a discussion on proper voucher/invoice processing.

We agree with the outcome measure of improved reliability of information in the amount of [redacted] resulting from two instances where the corrective actions were reported as being completed, even though all the questionable charges had not been recovered. Once this was brought to our attention, we agreed to change our reporting process to ensure all agreed-to questionable charges are recovered prior to closing a corrective action.

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We appreciate your continued support and the valuable assistance and guidance that your team provides. If you have any questions, please contact me or a member of your staff may contact Nick Nayak, Office of Strategic Acquisition Initiatives, at (202) 283-6857.

Attachment



Procurement's Control Environment Was Ineffective and Did Not Prevent Overpayments to Contractors

Attachment

Management response to Draft Audit Report – Procurement's Control Environment Was Ineffective and Did Not Prevent Overpayments to Contractors (Audit # 200710035) (I-trak #2008-33507)

RECOMMENDATION #1: The Director, Procurement, should provide training on the Guidebook and follow up to ensure all COTRs receive and use the voucher verification guidance developed as part of the Guidebook. Additionally, the Guidebook should be revised to include reviewing resumes to ensure contractor employees are qualified for the positions at which they are being charged.

CORRECTIVE ACTION TO RECOMMENDATION #1: We agree with this recommendation. Training on the Guidebook for Acquisition Practices (GAP) Voucher/Invoice Review process was provided to Procurement personnel in October, 2007. Additionally, the Director, Procurement, will take the following actions:

- The Guidebook will be revised to include a contractor employee qualification/verification process.
- Training will be provided on the revised contractor employee qualification/verification process.
- A quality review process will be implemented to monitor compliance with the voucher verification guidance.
- The 2008 Acquisition Planning Conference will include a discussion on the Guidebook process and copies of the Guidebook will be available to attendees.

IMPLEMENTATION DATE: July 15, 2009

RESPONSIBLE OFFICIAL: Director, Procurement, OS:A:P

CORRECTIVE ACTION MONITORING PLAN: Customer feedback from the Acquisition Planning Conference will be monitored and considered for further improvements. Quality review results will also be utilized to determine where improvements may be necessary.