



*The Redesign of the Learning and Education
Activity Involved Unnecessary Delays,
Additional Costs, and Delayed Savings*

September 27, 2006

Reference Number: 2006-10-173

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.

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 27, 2006

MEMORANDUM FOR CHIEF HUMAN CAPITAL OFFICER
CHIEF, AGENCY-WIDE SHARED SERVICES

Michael R. Phillips

FROM: Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Redesign of the Learning and Education Activity Involved Unnecessary Delays, Additional Costs, and Delayed Savings (Audit # 200510027)

This report presents the results of our review of the Internal Revenue Service's (IRS) decision to remove the Learning and Education activity from the Competitive Sourcing Program. The overall objective of this review was to determine whether the decision was appropriate. This audit was conducted as part of the Treasury Inspector General for Tax Administration's Fiscal Year 2006 Annual Audit Plan.

Impact on the Taxpayer

Competitive sourcing is the process for determining whether an activity will be performed by a public or private source, using the disciplines of competition. It should result in significant savings and performance improvements. Converting the Learning and Education activity competitive sourcing project to a Business Process Reengineering effort—with competitive sourcing disciplines—was not an efficient way to redesign the activity. This decision cost the IRS considerable additional time and cost.

Synopsis

The IRS' decision to remove the Learning and Education activity from the Competitive Sourcing Program was based on legitimate business decisions. However, the time and resources spent on the Learning and Education activity competitive sourcing project could have been reduced if this decision had been made sooner and implemented more efficiently. The IRS nominated the Learning and Education activity as part of its Fiscal Year 2004 Competitive Sourcing Program.



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After nominating an activity, the IRS conducts a Business Case Analysis, which is intended to assess whether there is an opportunity to improve the efficiency of the activity by subjecting it to the competitive sourcing process. In February 2004, the Strategy and Resource Committee, the key decision maker for competitive sourcing in the IRS, agreed with the Business Case Analysis recommendation to compete the Learning and Education activity. As a result, in June 2004, the Office of Competitive Sourcing began preliminary planning for a standard competition of the Learning and Education activity. However, in April 2005, the Strategy and Resource Committee voted to suspend the competitive sourcing project and conduct a “hybrid” study, which can be described as an internal Business Process Reengineering solution with competitive sourcing disciplines and expectations. The final redesign using the hybrid approach was approved in March 2006.

This decision resulted in considerable additional time and cost for the IRS and may not have saved any time over a competitive sourcing project. The hybrid design did not achieve its goal of a 40 percent reduction in costs. In addition, the IRS does not have assurance that its redesign of the Learning and Education activity is more efficient than options that could be provided by commercial vendors.

We identified opportunities for reduced costs and time. For example, the IRS’ concerns with using the competitive sourcing process should have been known and considered at the time the decision was made to nominate the Learning and Education activity for competitive sourcing, not 25 months later. Also, during the 36 months the IRS spent to plan and redesign the Learning and Education organization, there were inefficiencies and nonproductive time and resources spent because some of the competitive sourcing disciplines used in the hybrid approach were unnecessary. We could not quantify how much of the cost expended on the redesign could have been avoided because IRS cost information did not include details sufficient for us to evaluate and measure those costs. Another impact of the delayed redesign was a corresponding delay in the cost savings and other anticipated benefits. The IRS estimated the redesign would save the IRS approximately \$30 million annually.

Another questionable factor of the Strategy and Resource Committee’s decision to adopt the hybrid approach was inclusion of the option to resume the competitive sourcing process if the redesign of the Learning and Education activity did not meet predetermined efficiency goals. Specifically, the Strategy and Resource Committee established a “mandate” of 40 percent cost reduction and full implementation of the redesigned activity by December 2006 using the hybrid approach. However, it was not realistic to believe the IRS could quickly revert to competitive sourcing for the Learning and Education activity. To do so with the same team would have given the IRS an unfair advantage over potential bidders because the Business Process Reengineering team had access to documents for extended time periods. To remedy this advantage, the IRS would have needed to appoint a completely different team to prepare a proposal for competition, resulting in additional delays.



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Finally, the IRS advised the Office of Management and Budget that the hybrid approach was a creative alternative to traditional competitive sourcing. However, the savings and efficiencies created by the competitive sourcing process are a consequence of market competition, not predetermined goals or mandates. The IRS does not know which option would have resulted in the best cost and redesign because the IRS eliminated the competition and switched to a different process in the middle of this effort.

Recommendations

We recommended the Director, Competitive Sourcing, nominate activities for competitive sourcing only after concluding conditions that are known or can be reasonably expected will not result in removing the activity from competition at a later date. We also recommended the Deputy Commissioner for Operations Support establish guidelines for conducting Business Process Reengineering projects. The guidelines should include steps that should be taken; an estimate of the number of employees that should be involved; and benchmarks for a timeline, estimated benefits, and costs. The guidelines should not impose competitive sourcing disciplines, such as using a firewall and a Requirements Document. Finally, we recommended the Director, Competitive Sourcing, not promote a Business Process Reengineering process with competitive sourcing disciplines as an alternative to competitive sourcing. Future competitive sourcing projects should include competition from commercial vendors.

Response

IRS management agreed with two of our three recommendations. The Director, Office of Competitive Sourcing, completed the development of a nomination model/tool that included the recommended guidance for nominating activities for the Competitive Sourcing Program. In addition, the Office of Competitive Sourcing established a workgroup with personnel from the Procurement function and the Modernization and Information Technology Services organization, as well as an industry expert, to define the processes for conducting business process improvement or reengineering efforts. The workgroup was augmented with subject-matter experts from the Human Capital Office, office of the Chief Financial Officer, and Office of Program Evaluation and Risk Analysis.

IRS management disagreed with our recommendation not to promote its Business Process Reengineering process with competitive sourcing disciplines as an alternative to competitive sourcing. IRS management responded that the IRS has no plans to eliminate competition and will leave open the option of using some of the competitive sourcing best practices for Business Process Reengineering and business process improvement initiatives. Management's complete response to the draft report is included in Appendix IV.



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Office of Audit Comment

IRS management did not include reasons for their disagreement, so we could not determine the basis for their disagreement. The response states there are no plans to eliminate competition (which appears to agree with our recommendation), but it does not indicate that future competitive sourcing initiatives will include competition. Also, it is unclear why management is addressing future business process improvement initiatives for Recommendation 3, which specifically addresses future competitive sourcing projects, not business process improvement initiatives. We continue to believe future competitive sourcing projects should include competition from commercial vendors, and the IRS should not attempt to promote its hybrid approach as a substitute for competitions with private industry.

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



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Abbreviations

FTE	Full-Time Equivalent
IRS	Internal Revenue Service
OMB	Office of Management and Budget
OPERA	Office of Program Evaluation and Risk Analysis



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Background

Competitive sourcing is the process for determining whether a commercial activity¹ will be performed by a public or private source. It is one of five Federal Government-wide initiatives outlined in the President's Management Agenda for improving the management and performance of the Federal Government. Announced in the summer of 2001, the President's Management Agenda states that nearly one-half of all Federal Government employees perform tasks that are readily available in the private sector. The intent of the competitive sourcing initiative is to open the Federal Government to the disciplines of competition. The initiative is expected to consistently generate significant savings and performance improvements.

Office of Management and Budget (OMB) Circular No. A-76, *Performance of Commercial Activities*,² establishes Federal Government policy for the competition of commercial activities. The policy requires classification of all activities performed by Federal Government personnel as either commercial or inherently Governmental.³ Agencies are then required to use a streamlined or standard competition to determine if Federal Government personnel should perform a commercial activity. The Internal Revenue Service (IRS) established an Office of Competitive Sourcing in September 2001.

The IRS classified the Learning and Education activity as a commercial activity and nominated it as a potential candidate for its Fiscal Year 2004 Competitive Sourcing Program. The Learning and Education activity includes components from the Human Capital Office, the Office of Agency-Wide Shared Services, and each of the supported business units.

Beginning in June 2003, the IRS conducted a Business Case Analysis to determine whether competing the Learning and Education activity was likely to yield benefits. The Business Case Analysis team identified 765 Full-Time Equivalents (FTE)⁴ that would be in the scope of a competitive sourcing project. This represented about 27 percent of all Learning and Education activity costs.

The Business Case Analysis also identified an additional 968 FTEs assigned to the business units that contributed to the Learning and Education activity in the IRS. For example, training classes are routinely instructed by business unit personnel. These positions and the other costs incurred

¹ A commercial activity is the process resulting in a product or service that is or could be obtained from a private sector source.

² Issued May 2003.

³ An inherently Governmental activity is one that is so intimately related to the public interest as to mandate performance by Federal Government personnel.

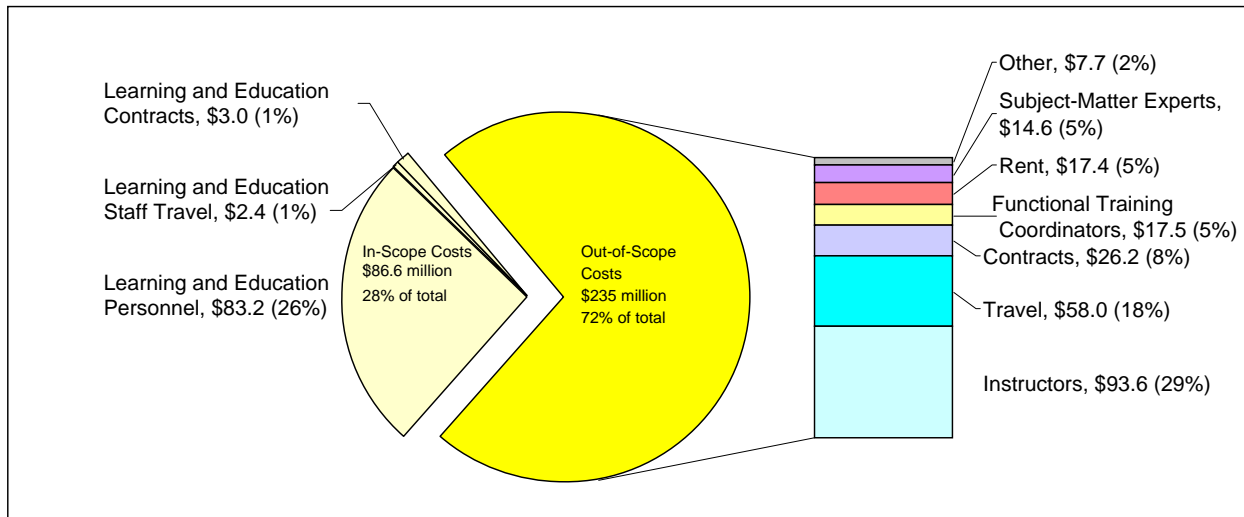
⁴ A measure of labor hours in which 1 FTE is equal to 8 hours multiplied by the number of compensable days in a fiscal year. For Fiscal Year 2004, 1 FTE was equal to 2,096 staff hours.



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by the business units in the delivery of Learning and Education activity services were referred to as “out-of-scope” costs. The out-of-scope costs of approximately \$235 million were significantly higher than the in-scope costs of \$88.6 million and represented 72 percent of the total cost of the Learning and Education activity in the IRS. Figure 1 shows a comparison of the in-scope and out-of-scope costs.

Figure 1: Comparison of In- and Out-of-Scope Costs



Source: Office of Program Evaluation and Risk Analysis (OPERA) presentation to the Strategy and Resource Committee on March 10, 2006.

The Business Case Analysis team defined the current state of the Learning and Education activity, evaluated alternatives to the existing organization, and estimated the costs of maintaining the existing organization or implementing alternative organizations. Alternatives included making improvements in the existing organization and considering proposals from outside vendors. In addition, the team identified and analyzed values and risks and evaluated the impact of values and risks on the costs of the existing and alternative organizations. Figure 2 lists the Learning and Education activity FTEs by business unit for the “in-scope” costs, which were included in the Business Case Analysis and ultimately subjected to the competitive sourcing process.



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Figure 2: Learning and Education Activity FTEs by Business Unit for In-Scope Costs

Type of Work/Office	Number of FTEs
Appeals	12
Agency-Wide Shared Services	84
Career Management and Learning Centers	125
Communications and Liaison	5
Human Capital Office	106
Large and Mid-Size Business Division	48
Modernization and Information Technology Services	38
Small Business/Self-Employed Division	169
National Taxpayer Advocate	10
Tax Exempt and Government Entities Division	24
Wage and Investment Division	144
Total	765

Source: Business Case Analysis.

In April 2005, the IRS decided to suspend the Learning and Education activity competitive sourcing project and conduct a Business Process Reengineering of the activity instead. It was anticipated that this would result in a 40 percent cost savings and be implemented by December 2006. The Human Capital Office had until December 2005 to design a plan to achieve these goals or the Learning and Education activity would revert to the competitive sourcing process. In March 2006, the Strategy and Resource Committee approved the Business Process Reengineering team's redesign of the Learning and Education organization. The solution is expected to save the IRS \$29.9 million (34 percent) of in-scope costs by the first year of implementation. Cost savings are projected to increase to \$32.9 million by the third year, when full implementation is expected.

This review was performed at the IRS National Headquarters in Washington, D.C., in the Human Capital Office and Office of Agency-Wide Shared Services during the period July 2005 through June 2006. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

The Learning and Education Activity Was Not a Good Candidate for Competitive Sourcing

In March 2003, the IRS nominated the Learning and Education activity for its Fiscal Year 2004 Competitive Sourcing Program and followed with a Business Case Analysis to determine if the Learning and Education activity would be a good candidate for competitive sourcing. The Business Case Analysis resulted in a recommendation to compete the Learning and Education activity because competition would yield lower costs while providing the same or more value than the existing organization. In February 2004, the Strategy and Resource Committee, the key decision maker for competitive sourcing in the IRS, agreed with the recommendation and decided to conduct a standard competition of the Learning and Education activity.

In April 2005, the IRS suspended the Learning and Education activity competitive sourcing project. Reasons for suspension included:

- The difficulty in adequately defining the Learning and Education activity level of work and performance metrics⁵ that would enable an outside vendor to deliver Learning and Education activity services that are critical to the core missions of the business units.
- The Learning and Education organization is complex and includes components from every business unit.
- Business unit leaders became concerned that the project was taking too long, resulting in delayed savings and prolonged stress to Learning and Education organization employees who were concerned about their jobs.

Although these are legitimate concerns, they were not caused by any new developments that had occurred since the time the Strategy and Resource Committee had agreed to conduct a standard competition. These concerns should have been considered before the decision was made to nominate the activity; or once the activity had been nominated, the concerns should have been identified during the Business Case Analysis. In addition, some of the concerns are not unique to the Learning and Education activity but should be expected with any competitive sourcing project. The time and costs of the competitive sourcing effort could have been avoided if these concerns had been addressed timely.

⁵ Performance metrics are standards for measuring performance, such as the percentage of students who are satisfied with the quality of the training.



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The IRS did not consider evidence that the Learning and Education activity was not a good candidate for competitive sourcing

The IRS nominates activities for competitive sourcing from its inventory of commercial activities. One of the nominating criteria is that competition of the activity will not negatively affect the mission of the IRS. However, the IRS had previously identified training as a vital component of its overall strategy because it enables the IRS to carry out its mission and overarching business priorities. Based on this, the suitability of the Learning and Education activity as a viable candidate for the Competitive Sourcing Program was questionable from the start. Indeed, business unit leaders later expressed concerns about adequately defining the Learning and Education activity level of work and performance metrics to enable an outside vendor to deliver the Learning and Education activity services that are so important to the IRS mission. Nevertheless, in March 2003, the IRS nominated the Learning and Education activity as a candidate for competitive sourcing.

The complexity of the IRS' Learning and Education organization was cited as one of the reasons to discontinue competition. However, this condition existed at the time the Strategy and Resource Committee approved the decision to compete the activity. When accepting the Business Case Analysis recommendation to proceed with competing the Learning and Education activity, the Strategy and Resource Committee acknowledged the necessity of establishing an oversight group to ensure the input from and concerns of the various business units were addressed. However, at that time, the Strategy and Resource Committee decided to proceed with competing this activity despite the complexity of the organization. The Strategy and Resource Committee recognized that the business units make significant contributions, such as instructors, subject-matter experts, and training coordinators, to the delivery of the Learning and Education activity services. As a result, an Executive Oversight Committee was formed to provide high-level business unit oversight of the development of the Performance Work Statement⁶ to ensure it fully supported critical business unit requirements.

Concerns about the length of time and impact on employees were not unique to the Learning and Education activity competitive sourcing project

Competitive sourcing projects may take a long time because of the requirement to formally announce a competition and evaluate bids. Certain factors can affect the length of a project, such as its complexity and the number of vendor proposals that will need to be evaluated. As part of the Learning and Education Business Case Analysis, the IRS conducted a market survey to identify sources that possessed the expertise, capabilities, and experience necessary to meet the IRS requirements for providing Learning and Education activity services. The IRS received 105 official responses from vendors; it determined 28 vendors appeared to have the capacity to

⁶ The goal of the Performance Work Statement team is to write the part of the formal competitive sourcing solicitation that identifies an agency's requirements.



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perform the mission and had submitted complete responses. The decision to compete the Learning and Education activity was made at the conclusion of the Business Case Analysis.

Revised OMB Circular No. A-76 states that a standard competition shall not exceed 12 months from public announcement to the finish date unless a time limit waiver is granted. If necessary, agencies are permitted to request up to an additional 6 months. The IRS had prior experience with formal competitions that exceeded the 12 months prescribed by the revised OMB Circular No. A-76. For example, the Area Distribution Center⁷ project, which was conducted under the previous version of OMB Circular No. A-76, took approximately 15 months to complete after the public announcement date. The IRS could reasonably expect that it would take at least 12 months to complete the Learning and Education activity competitive sourcing project after the public announcement date and could have anticipated it taking longer, given the high level of vendor interest.

There was also concern that the extended time period for the Learning and Education activity project would prolong employee stress, which is a natural reaction to changes in an organization. Suspending the Learning and Education activity competitive sourcing project and pursuing a Business Process Reengineering solution did not stop changes in the organization. The only way to have alleviated the stress of Learning and Education organization employees would have been to return to the status quo. However, the IRS determined this would not be possible because changes were needed in the Learning and Education activity to improve efficiency.

Recommendation

Recommendation 1: The Director, Competitive Sourcing, should nominate activities for competitive sourcing only after concluding conditions that are known or can be reasonably expected will not result in removing the activity from competition at a later date.

Management's Response: The IRS agreed with this recommendation. The Office of Competitive Sourcing completed development of a nomination model/tool, including this guidance, on August 28, 2006.

The Conversion From Competitive Sourcing to the Hybrid Approach Was Not Efficient

In January 2005, business units' concerns prompted the Strategy and Resource Committee to ask the OPERA to conduct a review of the Learning and Education activity competitive sourcing project. The OPERA developed a decision model that recommends a comparison of the draft Performance Work Statement requirements to the Business Case Analysis alternatives. With the OPERA model, a significant change in projected savings, timeline, or costs—along with the IRS'

⁷ An Area Distribution Center handles public and IRS requests for published IRS products.



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commitment to transformational change—would result in a decision not to proceed with a formal competitive sourcing project and to pursue an internal solution.

The IRS applied this decision model to the Learning and Education activity competitive sourcing project. The OPERA's analysis began in January 2005 and resulted in the Strategy and Resource Committee's vote in April 2005 to suspend the Learning and Education activity competitive sourcing project. The OPERA's analysis showed an implementation date of December 2007 if the IRS proceeded with the competitive sourcing project. By pursuing an internal Business Process Reengineering solution, the IRS expected to complete implementation by December 2006.

The project continued, but the work was no longer subjected to competition with the private sector. The objective of the Business Process Reengineering effort was to realize a 40 percent savings by redefining and redesigning the Learning and Education activity. The design phase of the Learning and Education Business Process Reengineering project was to conclude no later than December 2005, with implementation of the new design by December 2006. The Human Capital Office led the Business Process Reengineering effort, and the Office of Competitive Sourcing provided advice and support. The Human Capital Office adopted an approach that is described as Business Process Reengineering with competitive sourcing disciplines and expectations. The Office of Competitive Sourcing describes the disciplines as defining requirements, performance standards, and metrics and creating a transformational solution designed to meet the long-term needs of the organization. The IRS considered promoting this "hybrid" approach to the OMB as an efficient alternative to traditional competitive sourcing projects. However, if the Business Process Reengineering effort failed to achieve the required objectives, the Learning and Education activity project was to revert to the competitive sourcing process.

The IRS spent 3 years planning and redesigning the Learning and Education organization

In March 2003, the IRS recognized the potential to improve the efficiency of the Learning and Education organization by nominating the activity for competitive sourcing. The Office of Competitive Sourcing then conducted a Business Case Analysis, which confirmed the potential for savings. The IRS began the process of competitive sourcing by starting work on the Performance Work Statement and the Most Efficient Organization;⁸ however, it subsequently migrated to a Business Process Reengineering approach. The final redesign of the Learning and Education organization was not approved until March 2006, which was approximately 3 years after the IRS identified the potential for improvements. IRS management began implementing the redesign in May 2006 and estimates it will take 12 months to 18 months to implement most of the recommended changes to the organization.

⁸ The Most Efficient Organization team assists in the development of the agency's plan that is submitted in response to the formal solicitation.



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IRS officials from the Office of Competitive Sourcing and the Learning and Education organization believe the time spent by the Business Case Analysis, Performance Work Statement, and Most Efficient Organization teams benefited the Business Process Reengineering solution. However, the IRS could not quantify how much of this effort was beneficial to the design and implementation of the new organization. In addition, the IRS does not have benchmark information to measure how this project compares with other Business Process Reengineering efforts. In contrast, the IRS was able to design and implement an entirely new business unit structure based upon the IRS Restructuring and Reform Act of 1998⁹ in less time than it took to redesign the Learning and Education organization. Furthermore, the IRS did not begin to keep track of the costs to conduct the project until October 2004, which was about 19 months after it began.

We believe the IRS could have accelerated the design and approval of the new Learning and Education organization if it had used the Business Process Reengineering approach from the time it recognized the potential for improvement. Because the redesign of the organization is estimated to save the IRS approximately \$30 million annually, any time saved during this process would have resulted in significant cost savings. However, we could not quantify how much time the IRS could have saved because the IRS cost information for the various teams working on the project did not contain details sufficient for us to estimate how much time the IRS could have saved if it had avoided unnecessary competitive sourcing steps and duplication.

The IRS needs a better process for determining how to reengineer its processes and organizations. It does not appear reasonable to spend 3 years and other resources—18 team members, executive oversight, ad hoc team members, business unit contacts, and contractor support—to redesign an organization. If 3 years is not a reasonable amount of time for a Business Process Reengineering effort, the IRS wasted significant resources that could have been used for other priorities. In addition, the IRS will be unable to use this project as a model for future Business Process Reengineering efforts because it did not capture costs or identify where duplication and other competitive sourcing specific efforts could have been avoided.

The time and resources spent on portions of the Learning and Education activity competitive sourcing project were not productive

The redesign of the Learning and Education organization could have been completed and approved sooner if the IRS had proceeded with Business Process Reengineering at the conclusion of the Business Case Analysis instead of making the activity a competitive sourcing project. When planning for a standard competition, the IRS devotes resources to both a Performance Work Statement team and a Most Efficient Organization team. The goal of the Performance Work Statement team is to write the part of the formal competitive sourcing

⁹ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).



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solicitation that identifies an agency's requirements. The Most Efficient Organization team assists in the development of the agency's plan that is submitted in response to that formal solicitation. To ensure fair competition with potential commercial vendors, OMB competitive sourcing rules require that members of the Performance Work Statement team not be members of the Most Efficient Organization team. For the Learning and Education activity competitive sourcing project, the IRS spent approximately \$764,000 for the Performance Work Statement team, plus an additional \$830,000 for the Most Efficient Organization team for salaries, benefits, overhead, and travel. The teams consisted of 18 people. In addition, the IRS spent \$337,316 and \$814,251 for contractor support for the Performance Work Statement and Most Efficient Organization teams, respectively.

A business process reengineering initiative should include defining what is needed from the organization, how to redesign the processes, and how to implement improvements in the structure and operations of the organization to achieve results. These goals are similar to those of the Most Efficient Organization and Performance Work Statement teams. However, unlike in competitive sourcing projects, there is no requirement to separate the two objectives, nor are there restrictions on sharing information. If the IRS had initially made the decision to use the Business Process Reengineering approach, it would not have been necessary to establish 2 separate teams to conduct this work and it is unlikely that the IRS would have assigned 18 people to 2 separate teams. In addition, the Most Efficient Organization and Performance Work Statement teams coexisted for 9 months (October 2004 – June 2005). The IRS also committed additional resources to executive oversight, ad hoc team members, and business unit contacts. Efficiencies could have been gained if the Business Process Reengineering team had begun their work in June 2004 and the same team worked on both developing the requirements and crafting the solution. The efficiencies would have resulted in both time and cost savings to the IRS by reducing:

- Resources needed to conduct the work.
- Duplication of work.
- Time to accomplish the work.
- Contractor costs.

Although these inefficiencies existed, we could not quantify the cost impact to the IRS. The IRS began tracking costs for this project in October 2004. However, the cost information did not include details sufficient for us to evaluate and measure the cost of duplicative efforts. Furthermore, the IRS does not have specific criteria for how to conduct Business Process Reengineering projects, which prevented us from comparing the cost of the Learning and Education activity competitive sourcing project with the estimated cost for a comparable Business Process Reengineering project. Because the IRS has begun tracking costs, we are making no recommendations in this report about this issue.



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The IRS could not efficiently resume the Learning and Education activity competitive sourcing project

To facilitate the design of a new organization, the Business Process Reengineering team was provided with the Requirements Document that was developed by the Performance Work Statement team. The Requirements Document described the IRS' specific needs for its

From "IRS Headlines...and More" for May 2, 2005: "The Human Capital Office will now lead the effort, with the mandate of realizing at least a 40 percent cost savings implemented by December 2006."

Learning and Education activity and would have been provided to prospective vendors as part of a standard competition. By having access to the Requirements Document, the Business Process Reengineering team had an unfair advantage over potential bidders in the event the Business Process Reengineering project failed and the IRS decided to restart the competition. The IRS would have been able to remedy this concern if it had appointed a completely different Most Efficient Organization team. However, the new team would have to restart its analysis of the organization, which would mean the time that the Business Process Reengineering team spent developing the solution had been wasted. In addition, the solution itself could not be used. Furthermore, the team was provided with a specific numeric savings target of 40 percent, which would not be provided to any prospective vendors.

Some of the competitive sourcing disciplines were unnecessary

The IRS imposed certain competitive sourcing disciplines on the Business Process Reengineering team because it wanted the option of resuming the competitive sourcing process. The expectation was that, by using these competitive sourcing disciplines, the Learning and Education activity competitive sourcing project could quickly resume if the Business Process Reengineering effort failed. These disciplines included:

- Maintaining the firewall between the Performance Work Statement and Most Efficient Organization teams. OMB Circular No. A-76 states that, to avoid any appearance of a conflict of interest, members of the Performance Work Statement team shall not be members of the Most Efficient Organization team. A firewall is maintained between the Performance Work Statement team and the Most Efficient Organization team to ensure a conflict does not occur. The firewall precludes the same individuals from serving on both teams and does not allow the teams to share information directly.
- Requiring the Most Efficient Organization team to develop its solution based on a Requirements Document. In a formal competition, the Most Efficient Organization team develops a plan in response to a solicitation. The Performance Work Statement is part of the solicitation. When the decision was made to pursue a Business Process Reengineering solution, the Performance Work Statement or Requirements Document was provided to the Business Process Reengineering team.



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It was not realistic to believe the IRS could quickly restart the competitive sourcing project because of the unfair advantage the Business Process Reengineering team had over potential bidders. As a result, these competitive sourcing disciplines were unnecessary and made the reengineering process more difficult. The firewall inhibited the free flow of information among the most knowledgeable Learning and Education organization personnel for much of the Business Process Reengineering project. In addition, the Business Process Reengineering team was unable to readily share the redesign plans with other IRS activities and obtain buy-in from the business units. We were advised that the firewall requirement was eventually relaxed. Furthermore, the Requirements Document was written for an actual, formal competition; thus, many of the sections did not apply and were not needed for the in-house solution.

Eliminating competition is contradictory to the benefits of competitive sourcing

The IRS advised the OMB about using its hybrid approach as a creative alternative to traditional competitive sourcing. However, the savings and efficiencies created by the competitive sourcing process are a consequence of market competition that does not exist internally within Federal Government agencies. The hybrid solution set an artificial savings goal based on the combined results of Federal Government competitive sourcing studies for a variety of industries. The IRS does not have assurance that its redesign is more efficient than what commercial vendors may have proposed because the IRS eliminated the competition.

The redesign of the Learning and Education activity did not meet the stated goals

Although the Business Process Reengineering solution will save the IRS significant resources, the solution did not achieve the 40 percent savings originally mandated by the Strategy and Resource Committee. The Strategy and Resource Committee expected that the timeline would be expedited significantly by suspending the Learning and Education activity competitive sourcing project and pursuing a Business Process Reengineering solution. However, the Business Process Reengineering design phase of the project was not completed by December 2005. In addition, the Human Capital Office began implementing the solution in May 2006 and estimates that most of the Learning and Education activity will be converted to the new organization in 12 months to 18 months; however, full implementation is not expected to be completed until September 2009, which is almost 3 years past the goal. If the IRS had continued with the competitive sourcing project, it is possible the IRS would have achieved at least the same savings within the same timeline.

Recommendations

Recommendation 2: The Deputy Commissioner for Operations Support should establish guidelines for conducting Business Process Reengineering projects. The guidelines should include steps that should be taken; an estimate of the number of employees that should be involved; and benchmarks for a timeline, estimated benefits, and costs. The guidelines should



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not impose competitive sourcing disciplines, such as using a firewall and a Requirements Document.

Management's Response: The IRS agreed with this recommendation. The IRS considered the Learning and Education Business Process Reengineering study a pilot and acknowledged that guidelines for Business Process Reengineering could be documented. As a result, the Office of Competitive Sourcing established a workgroup with the Procurement function, the Modernization and Information Technology Services organization, and an industry expert under contract to define the processes for conducting business process improvement or reengineering efforts. The workgroup began meeting in May 2006 and was augmented with subject-matter experts from the Human Capital Office, office of the Chief Financial Officer, and OPERA. The IRS expects to complete the guidelines by May 2007.

Recommendation 3: The Director, Competitive Sourcing, should not promote its Business Process Reengineering process with competitive sourcing disciplines as an alternative to competitive sourcing. Future competitive sourcing projects should include competition from commercial vendors.

Management's Response: The IRS disagreed with this recommendation. The IRS stated that there are no plans to eliminate competitions; conversely, the IRS will leave open the option of using some of the competitive sourcing best practices for Business Process Reengineering and business process improvement initiatives.

Office of Audit Comment: IRS management did not include reasons for their disagreement, so we could not determine the basis for their disagreement. The response states there are no plans to eliminate competition (which appears to agree with our recommendation), but it does not indicate that future competitive sourcing initiatives will include competition. Also, it is unclear why management is addressing future business process improvement initiatives for this recommendation. The recommendation specifically addresses future competitive sourcing projects, not business process improvement initiatives. We continue to believe future competitive sourcing projects should include competition from commercial vendors, and the IRS should not attempt to promote its hybrid approach as a substitute for competitions with private industry.



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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether the IRS' decision to remove the Learning and Education activity from the competitive sourcing process was appropriate. To accomplish this objective, we:

- I. Evaluated the reasons for selecting the Learning and Education activity for competitive sourcing and subsequently removing it from the competitive sourcing process.
 - A. Reviewed the Business Case Analysis used to support the decision to compete the Learning and Education activity.
 - B. Reviewed documents showing the progress of the Performance Work Statement and Most Efficient Organization teams.¹
 - C. Reviewed minutes and other relevant documents generated by the governance groups responsible for making decisions about the Learning and Education activity competitive sourcing project.
 - D. Reviewed the OPERA study of FTEs² and time and costs savings that resulted in the decision to remove the Learning and Education activity from the competitive sourcing process.
 - E. Interviewed IRS officials from the Office of Competitive Sourcing, Human Capital Office, Procurement function, OPERA, business units, and Office of the Chief Financial Officer; members of the Most Efficient Organization team; and representatives of governance groups for the Learning and Education activity concerning the decisions surrounding the competitive sourcing process.
 - F. Requested and reviewed advice from the Treasury Inspector General for Tax Administration Office of Chief Counsel on our findings.
- II. Determined whether the goal established for the Business Process Reengineering team³ was reasonable and was met.

¹ The goal of the Performance Work Statement team is to write the part of the formal competitive sourcing solicitation that identifies an agency's requirements. The Most Efficient Organization team assists in the development of the agency's plan that is submitted in response to that formal solicitation.

² A measure of labor hours in which 1 FTE is equal to 8 hours multiplied by the number of compensable days in a fiscal year. For Fiscal Year 2004, 1 FTE was equal to 2,096 staff hours.

³ The Business Process Reengineering team was charged with redesigning the Learning and Education organization.



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- A. Reviewed the Business Process Reengineering team's solution.
- B. Monitored the progress of the Business Process Reengineering team in achieving its objectives by December 2005 and discussed the progress of the team with the team leader, Human Capital Office, Office of Competitive Sourcing, business units, and representatives of the governance groups.
- C. Determined the basis for the 40 percent savings goal and whether it was reasonable that the Business Process Reengineering solution would meet the goal without negatively affecting the Learning and Education organization's ability to perform its mission.
- D. Evaluated the methodology the IRS used in determining the success of the Business Process Reengineering solution.
- E. Determined the cost of the decision to remove the Learning and Education activity from competitive sourcing and pursue a Business Process Reengineering process.



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Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

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

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Appendix III

Report Distribution List

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Appendix IV

Management's Response to the Draft Report



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

RECEIVED

SEP 21 2006

September 21, 2006

MEMORANDUM FOR Michael R. Phillips
Deputy Inspector General for Audit
FROM: *Rebecca Mack Johnson*
Beverly Ortega Babers
Chief Human Capital Officer
SUBJECT: TIGTA Draft Audit Report – The Redesign of the Learning
and Education Activity Involved Unnecessary Delays,
Additional Costs, and Delayed Savings (Audit #200510027)

We agree in principle with the findings of the subject report. We have coordinated this response with the Office of Competitive Sourcing (OCS), which is responsible for implementing the recommendations found in your report.

The Learning and Education study was the first for which the IRS utilized a non-traditional Business Process Improvement (BPI) approach that incorporated some of the best practices of competitive sourcing. We have learned a lot about the effectiveness of this approach; indeed, we are pleased that your report supports the anticipated achievement of 37% cost savings, just shy of our 40% goal.

Throughout the process, the Office of Program Evaluation and Risk Analysis and the Chief Financial Officer were engaged to validate the estimated and actual savings. We also engaged a broad cross section of IRS leadership in this undertaking. We continue to believe that the ultimate result of this service-wide initiative will be an organization that very efficiently provides more effective training and development to the IRS workforce.

If you have any questions, please contact Rebecca Mack Johnson, Director, Leadership and Education Division, at (202) 283-9209 or Raymona Stickell, Director, Office of Competitive Sourcing, at (240) 271-4884.

Attachment

cc: Carl Froehlich
Raymona Stickell
Rebecca Mack Johnson



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Attachment

RECOMMENDATION 1

The Director, Competitive Sourcing, should nominate activities for competitive sourcing only after concluding conditions that are known or can be reasonably expected will not result in removing the activity from competition at a later date.

CORRECTIVE ACTION

The Office of Competitive Sourcing (OCS) completed development of a nomination model/tool including this guidance on August 28, 2006.

IMPLEMENTATION DATE

August 28, 2006

RESPONSIBLE OFFICIAL

Raymona L. Stickell, Director, Office of Competitive Sourcing

RECOMMENDATION 2

The Deputy Commissioner for Operations Support should establish guidelines for conducting Business Process Reengineering projects. The guidelines should include steps that should be taken; an estimate of the number of employees that should be involved; and benchmarks for a timeline, estimated benefits, and costs. The guidelines should not impose competitive sourcing disciplines, such as using a firewall and a Requirements Document.

CORRECTIVE ACTION

IRS agrees. The L&E study was a pilot, and guidelines for Business Process Reengineering could be documented. As a result, OCS established a workgroup with Procurement, MITS, and an industry expert (under contract) to define processes for conducting BPIs or re-engineering efforts to achieve a High Performing Organization designation. The workgroup began meeting in May 2006 and was augmented with subject matter experts from the Human Capital Office (HCO), Chief Financial Officer (CFO), and Office of Program Evaluation and Risk Analysis (OPERA). The IRS model follows industry standards for business process re-engineering which does include substantial upfront investment in requirements development.¹

¹ "In the second generation, during the GE Capital deployment in 1995, a new first phase, *define*, was added, becoming the DMAIC methodology now used in most Six Sigma implementations. In the define phase, data is used to verify customer needs and requirements and to identify the Critical-to-Quality characteristics for customer satisfaction. The define phase guarantees that the Voice of the Customer is central to every Six Sigma project by adding rigor to the front end of the methodology. Thus, Six Sigma has the potential to create processes with maximum efficiency and effectiveness." (What is Six Sigma, Daniel L. Quinn).



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IMPLEMENTATION DATE

May 31, 2007

RESPONSIBLE OFFICIAL

Raymona L. Stickell, Director, Office of Competitive Sourcing

RECOMMENDATION 3

The Director, Competitive Sourcing, should not promote its Business Process Reengineering process with competitive sourcing disciplines as an alternative to competitive sourcing. Future competitive sourcing projects should include competition from commercial vendors.

CORRECTIVE ACTION

IRS disagrees. There are no plans to eliminate competitions; conversely, we will leave open the option of using some of the Competitive Sourcing best practices for BPR/BPI initiatives.

IMPLEMENTATION DATE

Not Applicable

RESPONSIBLE OFFICIAL

Raymona L. Stickell, Director, Office of Competitive Sourcing