

**Improvements Are Needed in the Invoice  
Review Process for the Business Systems  
Modernization Contract**

**June 2004**

**Reference Number: 2004-10-117**

**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.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

June 29, 2004

MEMORANDUM FOR CHIEF, AGENCY-WIDE SHARED SERVICES

*Gordon C. Milbourn III*

FROM: Gordon C. Milbourn III  
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract (Audit #200310019)

This report presents the results of our review of the Business Systems Modernization (BSM) contract. The overall objective of this review was to determine whether the Internal Revenue Service (IRS) is properly reviewing and certifying invoices for the BSM contract to ensure all charges are accurate and supported.

Because contract expenditures represent a significant outlay of IRS funds, the Treasury Inspector General for Tax Administration (TIGTA) has made a commitment to perform audits of these expenditures. We initiated this audit to review the process the IRS has in place to certify invoices for the BSM contract and ensure charges on the invoices are accurate and supported.

In summary, the IRS' process for reviewing and certifying invoices for this contract does not ensure all charges are accurate and supported. We found the contractor's documentation was not adequate to support all the charges invoiced.

According to the IRS Request Tracking System, as of September 2003, the IRS had approved payment of approximately \$750 million for the BSM contract. Using a judgmental sample of 4 invoices from 1 judgmentally selected task order, we requested supporting documentation from the IRS and the contractor<sup>1</sup> to verify approximately \$17.6 million in direct charges claimed on the invoices. As a result of our analysis, we

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<sup>1</sup> We initially requested supporting documentation for the direct charges from the IRS. To complete the review, we needed to request additional information from the contractor to support the direct charges. Direct costs are those that can be identified specifically with a contract.

identified approximately \$9.5 million<sup>2</sup> (approximately 54 percent) in direct charges for which neither the IRS nor the contractor provided any supporting documentation, the supporting documentation did not adequately support the charge, or the charge was unallowable. A minimal amount, approximately \$1,400, is attributed to unallowable costs.

Because we were unable to verify all the direct charges contained in our sample of four invoices, there is no assurance the contractor billed the IRS accurately. Additionally, without an effective process to ensure charges included on the invoices are accurate and supported, the IRS is at risk of wasting Federal Government funds.

We recommended the Director, Office of Procurement, seek recovery of the \$9.5 million in unsupported charges unless the contractor provides acceptable support for those charges. Additionally, the Director, Office of Procurement, should initiate a program to review a representative sample of invoices submitted since the inception of the contract and ensure charges paid are accurate and supported. Further, the Director, Office of Procurement, should institute a policy of performing invoice reviews, which includes obtaining supporting documentation from the contractor for the charges included on an invoice, to ensure charges are accurate and supported before payment is made.

Management's Response: Office of Procurement management responded that they agree the documentation we reviewed did not, in some cases, adequately justify all charges. However, subsequent to the audit, the IRS did assemble documentation that demonstrates the contractor is accurately billing the IRS. In view of this, the Office of Procurement believes its review process ensures charges are accurate and supported.

The Office of Procurement requested and received documentation from the contractor to support the charges questioned. The Office of Procurement will continue to review supporting documentation and will seek recovery of any unsupported charges, if applicable. Office of Procurement management does not believe further corrective action is necessary in reviewing the invoice charges. They believe the standard contract closeout audits, performed for cost-reimbursement contract actions, will accomplish the same objective as the recommendation, without the need for a separate program. Additionally, the Office of Procurement has an existing policy for performing invoice reviews, which includes obtaining supporting documentation to ensure charges are accurate and supported before payment is made. While the audit team experienced difficulty in obtaining documentation from the contractor for the review, the contractor has committed to provide any documentation necessary to support the costs referenced in the report, as well as any future requests for supporting documentation. Management's complete response to the draft report is included as Appendix V.

Office of Audit Comment: Subsequent to the issuance of the draft report, we met with the contractor and the IRS. The contractor agreed to provide us and the IRS with all supporting documentation to verify the \$9.5 million in questioned costs. After our review

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<sup>2</sup> Subsequent to the issuance of the draft report, the contractor provided documentation to support all but approximately \$52,200 of the \$9.5 million we originally questioned.

of the additional documentation, we were able to verify all but approximately \$52,200 of the \$9.5 million we originally questioned. The \$52,200 consists of \$27,650 in unsupported charges and \$24,515 in unreasonable or unallowable charges. The contractor should continue to work with the IRS to provide additional support for the \$27,650 in unsupported charges. However, if the contractor is unable to provide supporting documentation, the IRS should seek recovery of any outstanding unsupported charges and the \$24,515 in unreasonable or unallowable charges.

The contractor initially did not provide sufficient documentation to support the charges on the four invoices we selected for our review. However, after the draft report was issued to the IRS, the contractor cooperated and provided the appropriate documentation to support the invoices. The contractor's delays in providing the necessary documentation prevented us from completing this audit timely. To assure that its billings are adequately justified, and to facilitate timely, independent review by TIGTA auditors, we believe the IRS should strengthen its invoice review process by routinely requesting and reviewing a sample of supporting documents.

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 Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations), at (202) 622-8500.

**Improvements Are Needed in the Invoice Review Process for the  
Business Systems Modernization Contract**

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## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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### Background

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In December 1998, the Internal Revenue Service (IRS) awarded an indefinite-delivery/indefinite-quantity<sup>1</sup> task order contract to provide for the design and development of an information system that allows the IRS to effectively and efficiently process tax return information, provide customer service, and maintain accurate financial records. This effort, known as Business Systems Modernization (BSM), is a partnership between the contractor and the IRS. The contract is estimated to span 15 years at a cost of \$8 billion. According to the IRS Request Tracking System, as of September 2003, the IRS had approved payment of approximately \$750 million for the BSM contract.

The Federal Acquisition Regulation (FAR)<sup>2</sup> stipulates that a contractor is responsible for accounting for costs appropriately and for maintaining records, including supporting documentation, adequate to demonstrate that costs claimed have been incurred. The FAR also provides that costs shall be allowed to the extent they are reasonable, allocable, and allowable under the FAR.

Because contract expenditures represent a significant outlay of IRS funds, the Treasury Inspector General for Tax Administration (TIGTA) has made a commitment to perform audits of these expenditures. We initiated this audit to review the process the IRS has in place to certify invoices for the BSM contract and ensure charges on the invoices are accurate and supported.

The timeliness of the audit was impaired due to significant delays in obtaining access to the contractor's supporting documentation. Although we eventually received some records from the contractor, the records provided as of January 30, 2004, did not adequately support a significant amount of direct charges as described later in this report. Accordingly, we provided the IRS with a detailed listing of the unsupported charges in anticipation that the contractor would potentially provide additional documents in support of these charges.

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<sup>1</sup> In an indefinite-delivery/indefinite-quantity contract, the time of delivery is not specified but is established during performance, and the exact quantity to be ordered is unknown but is specified within minimum and maximum limits.

<sup>2</sup> 48 C.F.R. pt 1-53 (2002).

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The audit work was performed during the period March 2003 through January 2004 in the BSM Office within the Modernization and Information Technology Services function in New Carrollton, Maryland, and in the Procurement directorate within the Agency-Wide Shared Services office in Oxon Hill, Maryland. In addition, we interviewed the contractor's accounting employees and reviewed contractor records in New Carrollton, Maryland.

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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### Documentation Was Not Adequate to Support All of the Invoiced Costs

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The IRS' process for reviewing and certifying invoices for this contract does not ensure all charges are accurate and supported. We found the contractor's documentation was not adequate to support all the charges invoiced.

Because of the size and complexity of the BSM contract, our review focused on the Customer Account Data Engine (CADE) project.<sup>3</sup> We selected the CADE because of the importance and high visibility of the project to the IRS and tax administration. We analyzed the invoices submitted from October 2000 through April 2003 and the associated task orders for the CADE project. Using a judgmental sample of four invoices from one judgmentally selected task order, we requested supporting documentation from the IRS and the contractor<sup>4</sup> to verify all the direct charges<sup>5</sup> included on the invoices, including employee labor hours, travel expenses, subcontractor costs (labor hour and other direct costs (ODC)/travel), and Internal Working Order (IWO)<sup>6</sup> labor and travel expenses. We identified

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<sup>3</sup> The CADE will provide data storage for tax account and return information and perform tax administration.

<sup>4</sup> We initially requested supporting documentation for the direct charges from the IRS. To complete the review, we needed to request additional information from the contractor to support the direct charges.

<sup>5</sup> Direct costs are those that can be identified specifically with a contract.

<sup>6</sup> IWO charges are for work completed by contractor employees outside of the usual Federal/Civil Sector Division of the contract.

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approximately \$9.5 million<sup>7</sup> (approximately 54 percent) of the \$17.6 million in direct invoiced charges for which neither the IRS nor the contractor provided any supporting documentation, the documentation provided did not adequately support the charge, or the cost was unallowable. Nearly all the unsupported charges related to subcontractor labor, subcontractor ODC/travel, and IWO labor and travel expenses. A minimal amount, approximately \$1,400, was attributed to unallowable costs.

The following are examples of specific invoice charges for which the contractor did not provide support or the support provided was inadequate:

- One of the invoices included charges of approximately \$2.7 million for subcontractor labor. The contractor provided no supporting documentation for these charges.
- One of the invoices included a charge of approximately \$2.8 million for subcontractor ODC/travel. The contractor provided a subcontractor invoice as support for the charge; however, the contractor provided checks payable to the subcontractor totaling only \$1.9 million. Additionally, we could not attribute the \$1.9 million in checks to the subcontractor invoice (i.e., there were no cross-references linking the checks to the invoice).
- The invoices included charges of approximately \$860,000 and \$97,000 for IWO labor and IWO travel, respectively. The documentation provided to support these charges was an invoice from the contractor's IWO group with an attached list of employees, their hours, and associated travel expenses. We did not believe this documentation was adequate to support these charges. The contractor did not provide any documentation from its timekeeping system to support the labor hours,

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<sup>7</sup> Subsequent to the issuance of the draft report, the contractor provided documentation to support all but approximately \$52,200 of the \$9.5 million we originally questioned.



## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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nor were any receipts provided for the travel expenses.

- Two of the invoices included charges for the fixed fee.<sup>8</sup> The contractor did not provide any support for the fee.

Table 1 summarizes the questioned charges identified during our review, using the categories as shown on the invoice.

**Table 1: Schedule of Questioned Charges**

Questioned Activity	Questioned Charges
Subcontractor Labor	\$3 million
Subcontractor ODC/Travel	\$5 million
IWO Labor	\$860,000
IWO Travel	\$97,000
Civil Group Travel	\$1,400
Tech Pubs Allocation	\$28,000
Other ODC	\$12,000
Fixed Fee	\$518,000
<b>Total</b>	<b>\$9.5 million</b>

*Source: TIGTA analysis of four invoices submitted to the IRS.*

The IRS has an agreement in place with the contractor outlining the invoice review process. The agreement provides that the Contracting Officer and Contracting Officer Technical Representative (COTR) will review the invoices and submit any requests for necessary supporting documentation to the contractor within 7 calendar days of receipt of the invoice. The agreement also outlines COTR invoice review responsibilities. These responsibilities include ensuring all costs are commensurate with the task order, verifying compliance with special contract terms and conditions, verifying indirect billing rates, and verifying mathematical accuracy.

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<sup>8</sup> The fixed fee is the fee agreed upon for the performance of a cost-plus-fixed-fee contract.

## **Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract**

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The IRS does not routinely receive supporting documentation for invoices submitted by the contractor. According to IRS personnel, to verify an invoice, the COTR forwards the invoice to the Acquisition Project Manager (APM) to review the charges on the invoice. If the APM raises questions regarding any charge, the COTR requests the supporting documentation for the questioned charge and a determination is made as to whether the charge is valid. If no charges are questioned, the invoice is paid in full.

The IRS review process identified issues and withheld monies from three of the four invoices included in our sample. Specifically, the IRS withheld the following amounts:

- For 1 invoice, \$77,000 was withheld because the amount billed exceeded the funds allotted to the contract. According to the COTR, \$77,000 was paid to the contractor over several subsequent invoices.
- For another invoice, \$313,000 of the fixed fee was withheld because the amount was billed in error. This amount has not been paid to the contractor. On the same invoice, \$80,000 was withheld because the amount billed exceeded the funds allotted to the contract. The \$80,000 has not been paid.
- On the third invoice, only \$72,000 of the \$1.1 million has been paid to the contractor. The remaining amount is being withheld because this invoice was for change requests and the work has not been completed.

Additionally, the Defense Contract Audit Agency (DCAA) performed various audits of this contractor.<sup>9</sup> Since September 2000, the DCAA has reported deficiencies with the contractor's budget and planning system, the billing system, and the indirect and ODC system, including related internal control policies and procedures. Because of the size and complexity of the invoices and the system inadequacies reported by the DCAA, we believe a more thorough review of the invoices needs to be performed to ensure all charges

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<sup>9</sup> We coordinated with the DCAA to ensure our audit of specific invoices did not duplicate its efforts.

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are accurate, supported, and allowable. These reviews should include obtaining documentation from the contractor to support charges contained on the invoices.

As previously mentioned, the FAR provides that a contractor is responsible for accounting for costs appropriately and for maintaining records, including supporting documentation, adequate to demonstrate that costs claimed have been incurred. Because we were unable to verify the above costs, there is no assurance the contractor billed the IRS accurately. Additionally, without an effective process to ensure charges included on invoices are accurate and supported, the IRS is at risk of wasting Federal Government funds.

### **Unallowable charges**

We identified approximately \$1,400 of unallowable expenses<sup>10</sup> in our judgmental sample of 4 invoices. These charges were for meals provided at meetings or conferences to contractor, subcontractor, and/or IRS employees. Additionally, \$671 of the \$1,400 was billed and paid for on 2 separate invoices included in our review. Therefore, the IRS paid for the expense twice. IRS personnel explained they approved these charges because the contractor believed that, by allowing attendees to leave the meeting or conference for lunch, key points in the presentations would be missed.

According to the Principles of Federal Appropriations Law,<sup>11</sup> appropriated funds are not available to pay subsistence or to provide free food to Federal Government employees at their official duty stations. Appropriation law extends the prohibition to non-Government personnel. The Principles of Federal Appropriations Law further state,

*Just as the entertainment of government personnel is generally unauthorized, the entertainment of non-government personnel is equally impermissible. The basic rule is*

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<sup>10</sup> An unallowable expense is a cost incurred by the contractor that is not chargeable to Federal Government contracts.

<sup>11</sup> Principles of Federal Appropriations Law, Second Edition, published by the General Accounting Office.

## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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*the same regardless [of] who is being fed or entertained; appropriated funds are not available for entertainment, including free food except under specific authority.*

Additionally, the FAR provides that the costs of amusement, diversions, social activities, and any directly associated costs, such as tickets to shows or sporting events, meals, lodging, rentals, transportation, and gratuities, are unallowable.

In August 2003, the Office of Procurement issued an Office of Modernization Acquisition Directive that stipulates payment to contractors for free food/entertainment or refreshments for Federal Government, contractor, and/or subcontractor employees would be unallowable unless the reimbursement meets an exception authorized under law. We believe the charges discussed above should not have been allowed; however, the IRS took the appropriate steps in issuing a directive that prohibits the allowance of these charges in the future. Notwithstanding the directive and the earlier decision to allow these prior charges, the IRS at a minimum should recover the \$671 in duplicate charges.

### Recommendations

The Director, Office of Procurement, should:

1. Seek recovery of the \$9.5 million unless the contractor provides acceptable support for those charges.

Management's Response: The Office of Procurement requested and received documentation from the contractor to support the costs questioned. The Office of Procurement will continue to review the supporting documentation and will seek recovery of any unsupported charges, if applicable.

Office of Audit Comment: Subsequent to the issuance of the draft report, we met with the contractor and the IRS. The contractor agreed to provide us and the IRS with all supporting documentation to verify the \$9.5 million in questioned charges. After our review of the additional documentation, we were able to verify all but approximately \$52,200 of the \$9.5 million we originally questioned.

## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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For the \$52,200 still questioned, the contractor either did not provide documentation to support the charge, the charge was unallowable, or the charge seemed unreasonable. We identified additional unallowable costs of \$1,465 in other ODCs. These charges were for meals provided at meetings. Additionally, we identified approximately \$21,700 in travel charges that we consider unreasonable. These include overcharges of meals and incidental expenses, corporate apartments for employees where an employee was at the temporary duty station for only 10 days during the month, and charges for incidental expenses, which included food.

Table 2 summarizes the questioned charges still outstanding using the categories as shown on the invoice.

**Table 2: Schedule of Questioned Charges Outstanding**

Questioned Activity	Unsupported Charges	Unreasonable/ Unallowable Charges
Subcontractor Labor	\$5,759.16	
IWO Travel	\$21,551.43	\$21,707.94
Civil Group Travel	\$339.58	
Other ODCs		\$2,807.23
<b>Total</b>	<b>\$27,650.17</b>	<b>\$24,515.17</b>

*Source: TIGTA analysis of supporting documentation for four invoices submitted to the IRS.*

The contractor should continue to work with the IRS to provide additional support for the outstanding unsupported charges of \$27,650. However, if the contractor is unable to provide sufficient documentation, the IRS should seek recovery of the outstanding unsupported charges and the \$24,515 in unreasonable or unallowable charges.

2. Initiate a program to review a representative sample of invoices submitted since the inception of the contract and ensure charges paid are accurate and supported. This may include requesting DCAA audit assistance.

Management's Response: The Office of Procurement believes standard contract closeout audits, performed for cost-reimbursement contract actions, will accomplish the

## **Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract**

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same objective as the recommendation, without the need for a separate program.

3. Institute a policy of performing invoice reviews, which includes obtaining supporting documentation from the contractor for the charges included on an invoice, to ensure charges are accurate and supported before payment is made.

Management's Response: The Office of Procurement has an existing policy for performing invoice reviews, which includes obtaining supporting documentation to ensure charges are accurate and supported before payment is made. While the audit team experienced difficulty obtaining documentation from the contractor for the review, the contractor has committed to provide any documentation necessary to support the charges referenced in the report, as well as any future requests for supporting documentation.

Office of Audit Comment: The contractor initially did not provide sufficient documentation to support the charges on the four invoices we selected for our review. However, after the draft report was issued to the IRS, the contractor cooperated and provided the appropriate documentation to support the invoices. The contractor's delay in providing the necessary documentation prevented us from completing the audit timely. To assure that its billings are adequately justified, and to facilitate timely, independent review by TIGTA auditors, we continue to believe the IRS should strengthen its invoice review process by routinely requesting and reviewing a sample of supporting documents.

## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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### Appendix I

#### Detailed Objective, Scope, and Methodology

The overall objective of this audit was to determine whether the Internal Revenue Service (IRS) is properly reviewing and certifying invoices for the Business Systems Modernization (BSM) contract to ensure all charges are accurate and supported. To accomplish our objective, we:

- I. Determined the methodology the IRS has in place to verify invoices before certifying payment to the contractor.
- II. Determined whether the charges included on the invoices submitted by the contractor were supported and allowable.
  - A. Prepared a sampling plan and judgmentally selected a sample of invoices. A judgmental sample was used because we did not plan to project the results to the universe. Because of the size and complexity of the BSM contract, our review focused on the Customer Account Data Engine (CADE) project.<sup>1</sup> We selected the CADE because of the importance and high visibility of the project. We analyzed the invoices submitted from October 2000 through April 2003 and the associated task orders for the CADE project. Three cost-reimbursable task orders<sup>2</sup> were issued, with 27 invoices, totaling approximately \$36 million, submitted as of April 2003. We judgmentally selected one task order, task order 73, from which to select our judgmental sample of invoices. We selected a sample of 4 of the 12 invoices for task order 73 to verify all the direct costs,<sup>3</sup> including labor hours, travel expenses (e.g., airfare, hotel, mileage) and subcontractor charges, and reviewed the contractor's supporting documentation. Our sample covered approximately \$15.7 million<sup>4</sup> (56 percent) of the total amount invoiced for the task order selected (approximately \$28 million).
  - B. For the invoices included in our sample, obtained supporting documentation from the contractor and verified all direct charges on the invoices.
    1. Verified the mathematical accuracy of each invoice and any supporting documentation provided.

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<sup>1</sup> The CADE will provide data storage for tax account and tax return information and perform tax administration.

<sup>2</sup> Cost-reimbursable task orders provide payment to the contractor for allowable incurred costs.

<sup>3</sup> Direct costs are those that can be identified specifically with a contract.

<sup>4</sup> Although the total amount of the invoices was \$15.7 million, the amount of direct charges verified on the 4 invoices was approximately \$17.6 million. Two of the four invoices included significant amounts of adjustment for excess funding. We verified all the direct charges without consideration of the excess funding adjustments.

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2. Prepared a schedule of charges, including the labor category, labor rate, and hours charged; traced the charges to supporting documentation; and determined whether the charges were appropriate.
  3. Traced travel costs included on the invoices to supporting documentation (e.g., airline/hotel receipts) and determined whether the charges were appropriate.
- C. Determined whether unsupported, questioned, or disallowed charges were re-billed on a subsequent invoice and whether the IRS certified these charges for payment.



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Business Systems Modernization Contract**

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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)

John R. Wright, Director

Debra Gregory, Audit Manager

Terrey Haley, Senior Auditor

Rosemarie Maribello, Senior Auditor

Rita Woody, Senior Auditor

Niurka Thomas, Auditor

**Improvements Are Needed in the Invoice Review Process for the  
Business Systems Modernization Contract**

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**Appendix III**

**Report Distribution List**

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
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    Director, Office of Procurement OS:A:P

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**Appendix IV**

**Outcome Measures**

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

Type and Value of Outcome Measure:

- Cost Savings, Questioned Costs – Potential; \$52,165.34 (see page 2).
- Cost Savings, Questioned Costs (Unsupported portion of the questioned costs) – Potential; \$27,650.17 (see page 2).

Methodology Used to Measure the Reported Benefit:

To determine the outstanding questioned costs, we reviewed the additional documentation provided by the contractor to support the \$9.5 million in costs originally questioned. We identified \$27,650.17 in costs for which the contractor did not provide support. Additionally, we identified \$21,707.94 in what we consider to be unreasonable and therefore unallowable costs and \$2,807.23 in unallowable costs.

**Improvements Are Needed in the Invoice Review Process for the  
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Appendix V

**Management's Response to the Draft Report**



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

**RECEIVED**

May 14, 2004

**MAY 14 2004**

MEMORANDUM FOR GORDON C. MILBOURN III  
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: David A. Grant *David A. Grant*  
Director, Procurement

SUBJECT: Draft Audit Report – Inadequate Invoice Review Process Results  
in Significant Unsupported Costs for the Business Systems  
Modernization Contract (Audit #200310019)

We appreciate the opportunity to respond to the subject audit report. The report provides your assessment of whether the IRS is properly reviewing and certifying invoices for the Business Systems Modernization (BSM) contract. The objective of your audit was to determine whether our invoice review process ensures all charges under the BSM contract are accurate and supported. We agree the documentation you reviewed did not, in some cases, adequately justify all charges; however, subsequent to your audit, we have been able to assemble documentation that demonstrates the contractor is accurately billing the IRS. In view of this, we recommend that you amend your finding that the contractor's documentation is inadequate to support invoiced costs to reflect this positive outcome. This also supports a finding that our review process does ensure charges are accurate and supported.

The audit focused on four invoices submitted for one of 119 task orders we have issued under the BSM contract. We understand the audit team experienced difficulty obtaining documentation from the contractor, which prevented the team from performing a complete assessment of the support for the selected invoice sample. Specifically, the audit team was unable to verify \$9.5 million of \$17.6 million in direct costs under the contract.

After receiving the report, we met with the contractor to discuss the findings. The contractor was notably alarmed by the findings and committed to produce any documentation necessary to support the costs referenced in the report, as well as any future requests for supporting documentation. The extension in response time you granted enabled us to obtain support from the contractor for \$9.5 million in unsupported costs. In the short time available, we reviewed documentation for \$6 million of the \$9.5 million and verified 99% of the costs. Our continuing review indicates the outcome will be the same for the balance of the unexamined documentation and substantially allays the concerns detailed in the report.

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Your report recommends that we initiate a program to review invoices from the inception of the contract. This recommendation is predicated on the audit team not receiving sufficient data to support the \$9.5 million invoiced costs. Since our subsequent review verified the contractor can produce the requisite documentation to support the invoices, we believe our current review procedures are adequate. The same premise holds true for your recommendation that we establish an invoice review policy. We continue to believe our existing procedure for performing invoice reviews, Program Office Directive (POD) 2, adequately ensures charges are accurate and supported before payment is made. Your audit team has a copy of this directive, which establishes procedures and supporting data requirements that are substantially the same as those prescribed by the Government expert, the Defense Contract Audit Agency (DCAA).

Given the significance of the IRS Modernization Program, we recognize the need for a comprehensive and productive process for review and payment of Cost Reimbursement and Time and Materials invoices under the BSM contract. In addition to following the POD 2 procedures, the Contracting Officer, Contracting Officer's Technical Representative and Acquisition Project Manager review all invoices to ensure costs are allowable and acceptable. As additional insurance, DCAA provides ongoing audits of the contractor, which alert us to problem areas.

The report cites two areas of measurable benefits resulting from the audit. As detailed above, we have verified approximately \$6 million of the unsupported costs and will complete our review of the remaining documentation by June 1, 2004. We agree with the \$1,400 in unallowable costs; however, the contractor deducted this cost on a subsequent invoice. The attachment provides our specific response to the report's recommendations.

In light of the positive outcome of our review of the contractor's supporting invoice documentation, we suggest you reconsider issuing this audit report as currently drafted. At a minimum, we request that you change the title of the report to reflect that the BSM contract invoices paid by the IRS are accurate and supported.

If you have any questions, please call me at (202) 622-8480 or Fred Martin, Director, Office of Modernization Acquisition, at (202) 283-1202.

Attachment

cc: Assistant Deputy Commissioner Operations Support  
Chief, Agency-Wide Shared Services  
Management Controls Coordinator OS:A:F

## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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### ATTACHMENT

#### RECOMMENDATION 1:

The Director, Office of Procurement, should seek recovery of the \$9.5 million unless the contractor provides acceptable support for those costs.

#### CORRECTIVE ACTION:

We requested and received supporting documentation from the contractor for all but approximately \$60,000 of the \$9.5 million. The TIGTA audit manager we consulted concurred the documentation provided is acceptable. The contractor has committed to provide the support for the remaining \$60,000. We are continuing our review to verify that the documentation demonstrates the \$9.5 million is allowable and supported. To date, we have completed reviewing the support for 2 of the 4 invoices audited by TIGTA. The two invoices represent \$6 million of the \$9.5 million unallowable and unsupported costs. So far, the IRS review has confirmed:

- 99% of the TIGTA questioned cost was appropriately charged and paid.
- \$1,400 in unallowable costs identified in the report were credited under a subsequent invoice (Invoice 7).

Procurement will continue reviewing the supporting documentation and will seek recovery of any unsupported costs, if applicable.

#### IMPLEMENTATION DATE:

PROPOSED June 1, 2004

#### RESPONSIBLE OFFICIAL:

Director, Procurement OS:A:P

#### CORRECTIVE ACTION MONITORING PLAN:

The Office of Modernization Acquisition (OS:A:P:M) will conduct weekly status meetings until the review of all supporting documentation is completed.

## **Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract**

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2

**RECOMMENDATION 2:**

The Director, Office of Procurement, should initiate a program to review a representative sample of invoices submitted since the inception of the contract and ensure charges paid are accurate and supported. This may include requesting Defense Contract Audit Agency (DCAA) audit assistance.

**CORRECTIVE ACTION:**

We believe standard contract close-out audits, performed for cost-reimbursement contract actions pursuant to Federal Acquisition Regulation 52.216-7, will accomplish the same objective, without the need for a separate program. In addition, Procurement has an existing policy, Program Office Directive (POD) 2, for performing invoice reviews that includes obtaining supporting documentation to ensure changes are accurate and supported before payment is made. The procedures prescribed and the data requested by POD 2 are substantially the same as those prescribed by the Government expert, DCAA, in its Contract Audit Manual, Section 6-1008.

**IMPLEMENTATION DATE:**

Not Applicable

**RESPONSIBLE OFFICIAL:**

Director, Procurement OS:A:P

**CORRECTIVE ACTION MONITORING PLAN:**

Not Applicable

## Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract

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3

**RECOMMENDATION 3:**

The Director, Office of Procurement, should institute a policy of performing invoice reviews, which includes obtaining supporting documentation from the contractor for the charges included on an invoice, to ensure charges are accurate and supported before payment is made.

**CORRECTIVE ACTION:**

The Office of Procurement has an existing policy, Program Office Directive (POD) 2, for performing invoice reviews, which includes obtaining supporting documentation to ensure charges are accurate and supported before payment is made. The procedures prescribed and the data requested by POD 2 are substantially the same as those prescribed by the Government expert, the Defense Contract Audit Agency (DCAA), in its DCAA Contract Audit Manual, Section 6-1008.

While the audit team experienced difficulty obtaining documentation from the contractor for the review, the contractor has committed to provide any documentation necessary to support the costs referenced in the report as well as any future requests for supporting documentation. Therefore, no corrective action is required.

**IMPLEMENTATION DATE:**

Not Applicable

**RESPONSIBLE OFFICIAL:**

Director, Procurement OS:A:P

**CORRECTIVE ACTION MONITORING PLAN:**

Not Applicable