

**The Office of Competitive Sourcing Needs to
Improve the Planning, Scheduling, and
Costing of Projects**

August 2004

Reference Number: 2004-10-146

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

Redaction Legend:

7 = Predecisional staff recommendations or suggestions to agency decision makers.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

August 26, 2004

MEMORANDUM FOR CHIEF, AGENCY-WIDE SHARED SERVICES

David R. Deulin

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

SUBJECT: Final Audit Report - The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects (Audit # 200310024)

This report represents the results of our audit to evaluate the effectiveness of the Internal Revenue Service (IRS) competitive sourcing program in planning, scheduling, and costing its projects. Competitive sourcing is one of five Government-wide initiatives outlined in the President's Management Agenda for improving the management and performance of the Federal Government.

In summary, the IRS needs to improve the planning, scheduling, and costing of its projects. When an activity is nominated for the competitive sourcing process, resources necessary to perform a Business Case Analysis to evaluate the potential costs and benefits of competition are committed. However, the IRS does not have adequate procedures to assist in selecting activities to nominate for competitive sourcing. Also, the Office of Competitive Sourcing made significant revisions to original project schedules. As a result, projects went considerably beyond the scheduled dates for completion. Finally, the IRS did not use a reliable method to track and compile the costs of competitive sourcing. As a result, the costs were understated in Fiscal Year 2003 by approximately \$1 million.

We recommended the Chief, Agency-Wide Shared Services (AWSS), develop procedures for nominating activities for a Business Case Analysis. In addition, the Chief, AWSS, should ensure the Office of Competitive Sourcing establishes realistic milestones for competitive sourcing projects by considering relevant factors, responsibilities, and historical time periods for similar tasks and incorporate the milestones into finalized project schedule guidelines. The Chief, AWSS, in coordination with the Chief Financial Officer (CFO), should establish procedures for the reporting of

costs, savings, and other data to the Department of the Treasury and the Congress. The procedures should include the use of the Automated Financial System (AFS)¹ to record and prepare cost information for competitive sourcing.

Management's Response: The Director, Office of Competitive Sourcing, agreed with our recommendations. However, the Director noted disagreement with certain facts in our report and provided additional perspective on the improvements which have been made in the planning, scheduling, and costing of competitive sourcing projects. The Office of Competitive Sourcing considered the Recommendations 1 and 2 to develop procedures for nominating activities and to establish realistic schedule milestones to be fully implemented and will complete corrective action on the two remaining recommendations. Specifically, the Office of Competitive Sourcing, CFO, and budget contacts for the business divisions have been working since May 2003 to ensure competition costs and savings are accurately captured, updated, standardized, and reported regularly in the AFS/Integrated Financial System (IFS). Additional steps have been initiated to document the procedures for AFS/IFS cost tracking. Procedures will include unique AFS/IFS project tracking codes to correspond with the Department of the Treasury and Office of Management and Budget data call requirements.

Office of Audit Comment: We believe the facts in this report are accurate as presented. With respect to Recommendation 1, the Director, Office of Competitive Sourcing, did not differentiate between the nominating phase and the evaluating phase of competitive sourcing. After an activity is nominated for competitive sourcing, it is subjected to a Business Case Analysis, which requires the IRS to evaluate whether an activity is a potential candidate for competitive sourcing. The Office of Competitive Sourcing noted that the Business Case Analyses have been successful and recognized by the Government Accountability Office.² However, our recommendation addresses how activities are nominated, which occurs prior to the Business Case Analyses. The IRS expended resources on several Business Case Analyses that were postponed or cancelled for reasons that could have been identified prior to beginning the Business Case Analyses, such as ensuring the availability of resources. The Office of Competitive Sourcing did not provide documentation on how it applied nominating criteria for Fiscal Years 2002, 2003, and 2004, nor has it revised its procedures to ensure future activities are nominated based on quantifiable criteria.

The Office of Competitive Sourcing considered Recommendation 2 to establish realistic schedule milestones to be fully implemented and listed several steps it takes to establish and adjust the project schedules. It also noted that the IRS completes projects in less time compared to other Federal Government activities. However, we did not offer an opinion on the reasonableness of the time it took the IRS to complete competitive sourcing studies. Our recommendation is to apply lessons learned from past projects to develop more realistic project schedules. The Office of Competitive

¹ The IRS uses the AFS to capture cost information. The AFS requires the creation of unique Project Cost Accounting System codes, which are used to identify project costs. It will be replaced by the Integrated Financial System.

² Formerly the General Accounting Office.

Sourcing has not taken this action. For example, the draft Project Schedule guidelines still recommend 4 months to complete the Performance Work Statement, even though it took 12 months to complete this step for 2 of the 3 competitive sourcing projects we reviewed.

Although we disagree that management's corrective actions fully address Recommendations 1 and 2, we do not intend to elevate our disagreement concerning them to the Department of the Treasury for resolution. Management's complete response to the draft report is included as Appendix VI.

Copies of this report are also being sent to the IRS managers affected by the report 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 Programs), at (202) 622-8500.

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The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

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 Government-wide initiatives outlined in the President's Management Agenda for improving the management and performance of the Federal Government. The President's Management Agenda noted that nearly one-half of all Federal Government employees perform tasks that are readily available in the commercial marketplace—tasks such as data collection, administrative support, and payroll services. Historically, the Federal Government has realized cost savings in a range of 20 to 50 percent when Federal and private sector service providers compete to perform these functions. The competitive sourcing 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*, establishes Federal Government policy for the competition of commercial activities. Agencies are required to follow the policies and procedures outlined in the Circular for competing commercial activities. In May 2003, the OMB published revisions to Circular No. A-76 to improve the competitive sourcing process and to set time periods for completing competitions.

The Internal Revenue Service (IRS) established an Office of Competitive Sourcing in September 2001. This Office centrally manages the competitive sourcing program and has the responsibility of providing oversight to ensure quality, timeliness, consistency, responsiveness, and coordination. In the Fiscal Year (FY) 2002 inventory of activities performed by its employees, the IRS estimated approximately 20 percent (19,600 of 100,700) of its full-time employees perform activities that are commercial in nature.

This review was performed at the Office of Competitive Sourcing in Washington, D.C., during the period September 2003 through June 2004. The audit was

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

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Better Resource Planning Is Needed Before Starting the Competitive Sourcing Process

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.

The Office of Competitive Sourcing developed the following five-step process to support the IRS in using competitive sourcing to produce cost savings and efficiencies:

1. **Planning** – the compilation of the IRS-wide inventory of commercial activities.²
2. **Nominating** – the selection of activities as potential candidates for competition for the upcoming fiscal year.
3. **Evaluating** – the Business Case Analysis to determine the feasibility of subjecting the nominated activities to competition.
4. **Selecting** – based on the Business Case Analysis, the Strategy and Resources Committee decides whether to compete or not compete the activity.
5. **Executing** – if the decision is made to compete the activity, a Performance Work Statement³ is prepared, bids are solicited, and a contract is awarded if a commercial vendor is the most efficient provider. This step also includes the transition phase.

Once an activity is nominated, resources are committed to perform a Business Case Analysis to evaluate the potential costs and benefits of competition. For the 3 projects reviewed, the time used by the IRS to complete the steps leading up to the actual competition was more than 1½ years. Table 1 shows the time used by the IRS for the processes leading up to the competition for the

² As required by the Federal Activities Inventory Reform Act, Pub. L. No. 105-270.

³ The Performance Work Statement identifies the technical, functional, and performance characteristics of the agency's (bureau's) requirements. The Performance Work Statement identifies essential outcomes to be achieved; specifies the agency's required performance standards; and specifies the location, units, quality, and timeliness of the work.

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three projects reviewed. See Appendix V for timeline details for the three projects.

Table 1: Time Spent on Projects Prior to the Competition

Task	Time per Activity (in months)		
	Area Distribution Centers	Campus ⁴ Center Operations	7----- --- -----
Conduct Business Case Analysis/Make Decision	5	5	7-
Assemble Performance Work Statement Team	2	4	7-
Complete Performance Work Statement/Issue Solicitation	12	12	7 ⁵
Total Time for Preliminary Steps	19	21	7--⁶

Source: IRS Office of Competitive Sourcing.

Once the solicitation for bids from competitors is announced, the IRS has 12 more months to complete the competition.⁷ Overall, it can take 3 years or more to complete the entire competitive sourcing process.

Because of the resources committed, nominating an activity for the competitive sourcing program is an important step in the process. The Department of the Treasury, the OMB, and IRS employees are notified of the activities nominated. In its strategic plan, the Office of Competitive Sourcing outlined the following criteria to be considered before activities are nominated as potential competitive sourcing candidates:

- Competition will not negatively affect the mission.

⁴ Campuses are the data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the computing centers for analysis and posting to taxpayer accounts.

⁵ 7-----
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⁶ 7-----.

⁷ OMB Circular No. A-76 (revised in May 2003) states that a standard competition shall not exceed 12 months from public announcement to performance decision date. The time period may be extended by 6 months if the competition is expected to be particularly complex.

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- The activity can be competed as a unit and not a collection of independent positions.
- Activities appear to be readily available and economical in the private sector.
- Competition would not hinder IRS modernization, budget, or workforce planning requirements.
- The potential exists for cost efficiencies and savings.

Other than these general criteria in the strategic plan, procedures have not been completed to guide this process. There are two important factors which the IRS needs to consider before nominating activities for a Business Case Analysis: 1) whether people and other resources are available to complete the competitive sourcing process and 2) how to prioritize projects based on resources and likely savings/improved service.

In FY 2002, the first year it nominated activities for competitive sourcing, the IRS identified the resources it would need to carry out the competitive sourcing process. Competitive sourcing is in process or completed for all of these projects. Table 2 shows the status of the projects that were nominated in FY 2002.

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**Table 2: Status of Activities Nominated for the
Competitive Sourcing Program for FY 2002**

Activity	Number of Full-Time Equivalents (FTE)⁸	Status
Area Distribution Centers	500	Active
Architects and Engineers	10	Completed
Field and Headquarters Mailroom Sites	70	Active
Operation and Maintenance of Delegated Buildings	100	Active
Campus Center Operations	350	Active
Total	1,030	

Source: IRS Office of Competitive Sourcing.

The IRS postponed three of the seven activities nominated for FY 2003. 7-----

-----. Table 3 shows the status of the projects that were nominated in FY 2003.

⁸ 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 FY 2004, 1 FTE is equal to 2,096 staff hours. The chart lists the number of FTEs that are being studied for each activity.

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**Table 4: Status of Activities Nominated for the
Competitive Sourcing Program for FY 2004**

Activity	Number of FTEs	Status
7-----	7--	7-----
7-----	7--	7-----
7-----	7--	7-----
7-----	7--	7-----
7-----	7--	7-----
Total	2,201	

Source: IRS Office of Competitive Sourcing.

For 2 of the 6 activities postponed in FYs 2003 and 2004, the Business Case Analyses had been completed for approximately \$600,000 in contractor costs. In addition, approximately \$180,000 was spent for contractor support for the Performance Work Statement for 1 of the postponed projects. While the postponed projects can be resumed at a later date using much of the work already completed, additional time and resources will likely be necessary to update the information. Moreover, premature nomination of activities can negatively affect morale and job performance.

The Office of Competitive Sourcing posted a draft guide to competitive sourcing on its web site. The guide explains competitive sourcing and describes how to accomplish tasks required for the IRS competitive sourcing process. The guide also includes procedures for the appointment of competition officials, communications with and reviews by functional executive leadership, budget requests, and nondisclosure statements. However, the guide does not include any procedures about nominating activities for a Business Case Analysis. Without procedures for nominating activities, the IRS may commit resources that are not available and may not be nominating the best candidates for the program.

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Recommendation

1. The Chief, Agency-Wide Shared Services, should establish procedures for nominating activities for a Business Case Analysis.

Management's Response: The Office of Competitive Sourcing stated that corrective action was completed on May 17, 2004. It believes guidelines and practices for the project selection process have been established and are being followed. During the project selection process, the IRS answers the following questions:

- Is the function core to the IRS mission?
- How much does the function cost?
- Is there potential to reduce cost and/or improve productivity by competing the function?
- How does the function fit into other current or planned strategic projects?

Based on the responses to these questions along with other factors (analysis of current operations, market research, and the Most Efficient Organization (MEO)¹⁰ design), the IRS calculates and considers economic benefits of each potential alternative and the upfront and recurring investments required to achieve and maintain efficiencies. The IRS makes a decision to compete based on strategic business alignment, investment risks, return on investment, and alignment with the Federal Activity Inventory Reform Act and other President's Management Agenda goals, including Human Capital Initiatives.

Office of Audit Comment: In responding to our report, the Director, Office of Competitive Sourcing, did not differentiate between the nominating phase and the evaluating phase of competitive sourcing. Our recommendation focuses on the second stage of the competitive sourcing life cycle (nomination), as outlined in the IRS Competitive Sourcing Strategic Plan for FYs 2002-2005. The Office of Competitive Sourcing stated

¹⁰ The MEO is the Federal Government's organizational unit that will compete for the work described in the Performance Work Statement.

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it is following the above criteria for project selection; however, much of its discussion appears to be addressing steps taken during the Business Case Analysis, not during the nominating process. In addition, no documentation was available on how the Office of Competitive Sourcing applied the criteria in the nomination stage for FYs 2002, 2003, and 2004, nor have procedures been established to ensure future activities are nominated based on quantifiable criteria. Adequate procedures should ensure appropriate criteria are applied and documented and resources are available to complete the competition.

Significant Revisions Were Made to Original Project Schedules

The schedule for a competitive sourcing project includes many variables that can affect the timeline for completion. The complexity of the project, the availability of internal and external resources, the cooperation of the National Treasury Employees Union (NTEU), and the number and quality of contractor proposals can all affect the schedule for conducting studies. In fact, for the three studies reviewed, these variables significantly affected the original project schedules. As a result, the project completion dates have been extended, which complicates transition planning and delays cost savings.

The Office of Competitive Sourcing develops the project schedules for competitive sourcing studies with input from each project team. For the three competitive sourcing projects reviewed, changes had to be made to the project schedule start and completion dates. Table 5 shows the project planned start dates from the August 2002 project schedules compared with the actual start dates. For purposes of project schedules, the start date is considered the date on which the IRS begins to develop its Performance Work Statement.

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**Table 5: Comparison of the Project Schedule Start Dates
and Actual Start Dates**

Activity	Start date		Months Delayed
	Planned	Actual	
Area Distribution Centers	April 22, 2002	April 22, 2002	—
Campus Center Operations	September 16, 2002	October 28, 2002	1
7----- -----	7-----	7-----	7-

Source: IRS Office of Competitive Sourcing.

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Because contractor support was necessary to begin the project, the start date was delayed until the contractor support could be obtained.

Project schedules also had to be revised to reflect changes to the project completion date. Table 6 shows the changes to the completion dates in the project schedules from the dates originally planned for three ongoing competitive sourcing projects.

Table 6: Revisions to the Completion Dates in Project Schedules

Project	Completion date		Months Delayed
	Planned	Revised	
Area Distribution Centers	September 22, 2003	September 30, 2004	12
Campus Center Operations	February 9, 2004	December 1, 2004	10
7----- -----	7-----	7-----	7- ¹¹

Source: IRS Office of Competitive Sourcing.

The Area Distribution Centers project was the IRS' first competitive sourcing project. This is a large, complex project which involves approximately 1,300 employees.

¹¹ 7-----

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During the process, the NTEU raised issues related to employee rights that the IRS had to address. For example, the IRS had to address NTEU questions related to employees' notification and nondisclosure letters,¹² which caused it to delay the development of the MEO until discussions were held with the NTEU. The schedule had to be revised because the original project schedule did not include sufficient time for these discussions.

In addition, the Procurement function provided the Office of Competitive Sourcing with two possible schedules for the Area Distribution Centers project. The longer of the two schedules included time to hold discussions with bidders,¹³ while the second schedule assumed that discussions would not be necessary. The Office of Competitive Sourcing managed the project using the schedule that did not allow for vendor discussions. For example, in January 2004 the Office of Competitive Sourcing briefed the Director, Media and Publications, Distribution Division, that the contract would be awarded in April 2004, which is the schedule date without vendor discussions. The briefing did not include the possibility that the award date could be delayed until July 2004 if discussions were necessary. However, in March 2004, the Procurement function determined that vendor discussions would be necessary, and the award date was delayed.

The Office of Competitive Sourcing also underestimated the time necessary to develop a Performance Work Statement. For the Area Distribution Centers and the Campus Center Operations projects, the Office of Competitive Sourcing scheduled 5 months and 7 months, respectively, to complete the Performance Work Statement. However, the completion of the Performance Work Statement took approximately 12 months for both projects. 7-----

¹² The nondisclosure letter addresses an employee's access to sensitive procurement data and the requirement to protect that data.

¹³ Discussions with prospective vendors are sometimes necessary to clarify issues and give the bidders an opportunity to revise their proposals.

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----- . In addition, the Office of Competitive Sourcing underestimated the time necessary to complete the independent review of the MEO proposal.

Future project schedules should take into account the time actually required to complete these tasks. Project delays can affect employees and the cost to complete the project and can postpone cost savings. While some of these delays may not have been avoidable, consideration of these potential issues should be included in the project schedules. Instead of targeting the most optimistic dates, project schedules should plan for the most probable dates, so managers are aware of the likely time periods and can plan for them accordingly.

The Office of Competitive Sourcing developed draft guidelines for competitive sourcing project schedules. The purpose of having project schedules is to enable the Competitive Sourcing Project Manager and the Office of Competitive Sourcing to monitor and evaluate the progress of the projects. However, the project schedule guidelines are not complete and do not always consider the IRS' experience with ongoing projects. For example, although both the Area Distribution Centers and Campus Center Operations projects took 12 months to complete the Performance Work Statements, the January 2004 guidelines designate 4 months to complete future Performance Work Statements. The IRS needs to update and improve its scheduling for competitive sourcing studies to recognize the lessons learned from its ongoing projects.

Recommendation

2. The Chief, Agency-Wide Shared Services, should ensure the Office of Competitive Sourcing establishes realistic milestones for competitive sourcing projects by considering relevant factors, responsibilities, and historical time periods for similar tasks and incorporate the milestones into finalized project schedule guidelines.

Management's Response: The Office of Competitive Sourcing stated that corrective action was completed on June 17, 2004. It is following project management disciplines, including planning and scheduling and

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incorporating lessons learned for competitive sourcing competitions. The Office of Competitive Sourcing stated it has also taken steps to support compressing of timelines by:

- Sharing lessons learned at monthly and biweekly meetings.
- Expanding information on its web site.
- Obtaining expert contractor support for project acceleration.
- Providing training.
- Maintaining knowledge transfer from the Business Case Analysis phase to the Performance Work Statement phase by keeping the same project leader to assist teams in meeting the “stretch schedule goals.”

The Office of Competitive Sourcing stated it would continue to refine and condense the project schedules.

Office of Audit Comment: The draft guidelines for Project Schedules in the IRS Guide to Competitive Sourcing do not appear to address lessons learned. As we noted, the Office of Competitive Sourcing acknowledges that it takes 12 months to complete a Performance Work Statement. However, the draft guidelines suggest a 4-month timeline for the Performance Work Statement. While the IRS may be informally sharing information and lessons learned, the Office of Competitive Sourcing needs to formalize this process and incorporate the results into its written guidelines.

The Method for Compiling the Costs of Competitive Sourcing Is Not Accurate or Reliable

In August 2001, the Acting Chief Financial Officer (CFO) for the Department of the Treasury issued a memorandum to all Department of the Treasury bureaus requiring the collection of costs and savings resulting from compliance with OMB Circular No. A-76. The purpose of collecting these costs is to determine the point at which the savings exceed the costs, identify additional funds needed, and identify potential areas for reducing costs. Data collection was to be implemented in whatever manner was most efficient for each bureau. In January 2004, the Consolidated

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Appropriations Act, FY 2004,¹⁴ was signed into law. The Act includes a Government-wide requirement for each agency to report to the Congress on its competitive sourcing activities, including the costs and savings, for the prior fiscal year.

The IRS began compiling and submitting reports on its competitive sourcing costs in FY 2002. The IRS reports the following quarterly costs to the Department of the Treasury:

- Cost of managing the competitive sourcing program – this includes the administrative duties of the Office of Competitive Sourcing and all work associated with the Business Case Analysis.
- Cost of conducting competitions – this includes all work conducted by the business units subsequent to the decision to compete the activity.

However, the IRS does not have adequate procedures to ensure the costs it reports to the Department of the Treasury are accurate and reliable. The IRS has a cost accounting system¹⁵ to collect costs; however, it is not using its system to collect all of its costs. Inadequate procedures contributed to the IRS underreporting costs to the Department of the Treasury by \$1 million for FY 2003. This was due to an error in consolidating quarterly costs. The Office of the CFO corrected the error after we brought it to their attention. The costs for FYs 2002 and 2003 are shown in Table 7.

¹⁴ Consolidated Appropriations Act, FY 2004, Pub. L. No. 108-199.

¹⁵ The IRS uses the Automated Financial System (AFS) to capture cost information. The AFS requires the creation of unique Project Cost Accounting System codes, which are used to identify project costs.

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Table 7: Costs of the IRS Competitive Sourcing Program

Task	Cost (in millions)	
	FY 2002	FY 2003 ¹⁶
Managing the program	3.8	4.9
Conducting competitions	1.8	5.4
Total	\$5.6	\$10.3

Source: IRS Office of the CFO.

For FY 2002, the Office of the CFO identified these costs by asking the IRS divisions to provide information on costs for salary, travel, and training related to competitive sourcing and by asking the contractor to provide the costs billed to the IRS for the fiscal year. In FY 2003, the Office of the CFO began capturing salary, travel, and training costs by using its cost accounting system. However, the Office of the CFO did not use the system to capture and report the contractor costs. Instead, it asked each contractor to provide this information each quarter. In the beginning of FY 2002, only one contractor was working on competitive sourcing initiatives. In FY 2003, 9 contractors worked on various aspects of the competitive sourcing program and accounted for \$4.8 million (47 percent) of the \$10.3 million, which increases the importance of recording this information on the IRS cost accounting system as costs are incurred. Proper use of the IRS cost accounting system would eliminate the need to manually compile these costs.

In the future, the IRS will also be expected to report on savings resulting from competitions, which will be calculated by comparing the previous cost of performing the activity with Federal Government resources with the price of the winning contractor or Federal Government team offer. As of March 2004, there had been no savings; the IRS standard competitions were still in process and no awards had been announced. According to the Office of the CFO, savings are expected to begin in FY 2005.

¹⁶ The IRS originally reported \$4.2 million for managing the program and \$5.1 million for conducting competitions, for a total of \$9.3 million. The costs in this table represent the costs reported after the IRS made a correction.

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Recommendations

The Chief, Agency-Wide Shared Services, and the CFO should:

3. Use the Automated Financial System (AFS)¹⁷ to record and prepare cost information for competitive sourcing.
4. Establish written procedures for reporting costs, savings, and other required competitive sourcing data to the Department of the Treasury and to the Congress.

Management's Response: The Office of Competitive Sourcing, CFO, and budget contacts for the business divisions have been working since May 2003 to ensure competition costs and savings are accurately captured, updated, standardized, and reported regularly in the AFS/Integrated Financial System (IFS). Additional steps have been initiated to document the procedures for AFS/IFS cost tracking. Procedures will include unique AFS/IFS project tracking codes to correspond with the Department of the Treasury Department and Office of Management and Budget data call requirements.

¹⁷ The AFS will be replaced by the Integrated Financial System.

Detailed Objective, Scope, and Methodology

The overall objective of our review was to evaluate the effectiveness of the Internal Revenue Service (IRS) competitive sourcing program in planning, scheduling, and costing its projects. To accomplish our objective, we:

- I. Assessed the process the IRS developed for selecting and competing commercial activities.¹
 - A. Reviewed the IRS competitive sourcing plan, minutes of the Competitive Sourcing Coordination Group, and other documents related to the IRS competitive sourcing program.
 - B. Obtained criteria established by the Office of Management and Budget (OMB) and the Department of the Treasury for developing a competitive sourcing plan and compared the IRS competitive sourcing program plan with the criteria.
 - C. Discussed the competitive sourcing process with the Director and staff of the Office of Competitive Sourcing and with project leaders, team leaders, and team participants in the Wage and Investment (W&I) Division, Modernization and Information Technology Services (MITS) organization, and Agency-Wide Shared Services (AWSS) organization.
 - D. Selected a judgmental sample of three of the eight projects undergoing a full competitive sourcing study from the W&I Division, MITS organization, and AWSS organization; reviewed the steps taken to select the activities for competition; and evaluated the process. We judgmentally selected the sample to obtain one project from each of the above divisions.
- II. Reviewed the steps the IRS has taken to meet the standards established for the President's Management Agenda competitive sourcing initiative.
 - A. Identified the President's Management Agenda standards and goals and compared IRS performance with the standards and goals.
 - B. Discussed the President's Management Agenda competitive sourcing initiative with the Director and staff of the Office of Competitive Sourcing.
- III. Assessed the method used by the IRS for tracking costs related to the competitive sourcing program to determine whether IRS reported costs were accurate.
 - A. Obtained the Department of the Treasury's criteria for tracking costs and compared the IRS methodology for tracking costs with the criteria.

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

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- B. Discussed the methodology for tracking competitive sourcing programming costs with representatives of the Chief Financial Officer organization.
 - C. Reviewed documentation related to costs.
- IV. Reviewed the IRS plans to comply with OMB Circular No. A-76, *Performance of Commercial Activities*, including transition issues.

Major Contributors to This Report

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

Michael E. McKenney, Director

Carl L. Aley, Audit Manager

Joan R. Floyd, Lead Auditor

Susan A. Price, Senior Auditor

Michael J. Della Ripa, Auditor

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
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Outcome Measures

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

Type and Value of Outcome Measure:

- Reliability of Information – Actual; \$1 million understatement in costs of the competitive sourcing program reported to the Department of the Treasury for Fiscal Year 2003 (see page 13).

Methodology Used to Measure the Reported Benefit:

We reviewed the consolidated and quarterly cost reports the IRS sent to the Department of the Treasury for Fiscal Years 2002 and 2003. We also reviewed the process for assembling the reports and determined that inadequate procedures contributed to the understatement.

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Appendix V

**Timeline of Major Events for
Three Activities Reviewed**

Area Distribution Centers

Date	Event
September 2001	Business Case Analysis (BCA) team began its work.
February 22, 2002	Results of the BCA were presented to the Competitive Sourcing Executive Steering Committee. The Committee approved the recommendation to conduct a competition.
April 2002	Performance Work Statement (PWS) team began its work.
November 2002	Management Plan team informally began its work.
November 13, 2002	Request for Information and the draft PWS were issued.
December 13, 2002	Comments to the draft PWS were due and received.
February 2003	Management Plan team formally began its work.
April 25, 2003	Request for Proposal or solicitation was issued.
September 5, 2003	Original due date for proposals that was established in the solicitation.
September 17, 2003	Independent Review Officer startup meeting was held.
November 18, 2003	Independent Review Officer certified the Internal Revenue Service's (IRS) cost comparison form.
November 25, 2003	Revised due date for proposals that was changed by amendments to the solicitation. Also the received date for proposals and the date the IRS' bid was sealed.
April 2004	The award decision was expected.
August 2004	The revised date for the award decision.

**The Office of Competitive Sourcing Needs to Improve
the Planning, Scheduling, and Costing of Projects**

Campus¹ Center Operations

Date	Event
January 2002	The BCA team began its work.
June 17, 2002	Results of the BCA were presented to the Competitive Sourcing Executive Steering Committee. The Committee approved the recommendation to conduct a competition.
October 2002	The PWS team began its work.
April 28, 2003	Request for Information and the draft PWS were issued.
May 12, 2003	Comments to the draft were due and received.
June 2003	Most Efficient Organization (MEO) ² team began its work.
October 1, 2003	Request for Proposal or solicitation was issued.
January 29, 2004	Original due date for proposals that was established in the solicitation.
February 26, 2004	Revised due date for proposals that was changed by an amendment to the solicitation. Also the received date for proposals.
July – September 2004	The performance decision is expected.

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¹ Campuses are the data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the computing centers for analysis and posting to taxpayer accounts.

² The MEO is the Federal Government's organizational unit that will compete for the work described in the PWS.

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Appendix VI

Management's Response to the Draft Report



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

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MEMORANDUM FOR GORDON C. MILBOURN III
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT
FROM: *Raymona L. Stickell*
Raymona L. Stickell
Director Office of Competitive Sourcing
SUBJECT: Draft Audit Report – The Office of Competitive Sourcing Needs
to Improve the Planning, Scheduling, and Costing of Projects
(Audit # 200310024)

I appreciate the opportunity to provide a written response to the subject audit report. Members from our respective offices met on June 9, 2004, to discuss issues and concerns with the "discussion draft". While some clarifications have been made, there are still a number of factually incorrect statements, which should be corrected before the final report is issued. Additionally, before the final report is released, I ask that information regarding projects that have not been publicly released through the draft Performance Work Statement or Request for Proposal be redacted.

Since establishing our program in 2001, significant improvements have been made in the planning, scheduling, and costing competitive sourcing (CS) projects. In fact, the General Accounting Office¹ recognized our program for its discipline and rigor in selecting CS candidate activities. We have made revisions to original project schedules throughout the project life cycle as additional information was created or gleaned from lessons learned and best practices. As an example, over a year ago, we expanded the milestone action plan to include detail level entries to monitor schedules and mitigate due date slippages. CS worked extensively with Strategic Human Resources² to create the first comprehensive Reduction-in-Force timeline and associated action items. This expanded action plan is not only used for CS projects but by other activities engaged in re-engineering efforts.

In September 2002, existing and subsequent project milestone plans were updated to reflect the 18 months lead-time required for NTEU negotiations and based on experience from the Area Distribution Center (ADC) initiative the lead-time was modified to 12 months, without compromising program implementation. Through bi-weekly meetings with CS teams, monthly coordination meetings with CS Program Leaders and support organizations (i.e., CFO, Communications and Liaison, General Legal

¹ GAO Report 04-367, "Competitive Sourcing, Greater Emphasis Needed on Increasing Efficiency and Improving Performance," dated May 2004.

² Now reorganized as the Chief, Human Capital Officer reporting to the Deputy Commissioner for Operations Support.

The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

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Services, Human Capital, Procurement, etc.) we monitor schedules, identify issues and barriers, and share lessons learned. Additionally, a standardized project timeline and milestones template is maintained to create "stretch goals" for each project team. The CS Intranet site is populated with lessons learned, templates, project management tools, informational documents such as the IRS Project Managers Guide and the Federal Acquisition Council Guide to CS, and relevant support links to assist project teams.

IRS will complete two large complex studies, ADC and Campus Operations, in less than two and a half years. Similar studies at the Department of Defense are completed, on average, within 3 1/2 years.³ Our program is well managed and flexible to accommodate change or corrections. When a costing error was identified on the quarterly report to Treasury; our CFO quickly corrected the error without creating project delays.

Attached is our response to your recommendations. We have implemented two of your recommendations and, as such, they are closed. Recommendations 3 and 4 are scheduled for closure in early FY 2005 and I ask that they be combined in the published report and in the JAMES tracking system.⁴ My rationale for combining the two is that the corrective actions to resolve them are interconnected.

If you have any questions, please contact me at (202) 927-7550. For audit follow-up matters, please call Greg Rehak at (202) 622-3702.

Attachment

³ Data is based on a recently released OMB Report on Competitive Sourcing Results, FY 2003.

⁴ Treasury's audit follow-up tracking system is the Joint Audit Management Enterprise System (JAMES).

The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

ATTACHMENT

RECOMMENDATION 1:

The Chief, Agency-Wide Shared Services, should establish procedures for nominating activities for competitive sourcing.

CORRECTIVE ACTION:

Guidelines and practices are being followed as captured in GAO-04-367 Report, Competitive Sourcing, Greater Emphasis Needed on Increasing Efficiency and Improving Performance. During project selection process IRS answers the following questions:

- Is the function core to the IRS mission;
- how much does the function cost;
- is there potential to reduce cost and/or improve productivity by competing the function; and
- how does the function fit into other current or planned strategic projects?

Based on the responses to these questions along with other factors (analyses of current operations, market research, and a notional MEO design) IRS calculates and considers economic benefits of each potential alternative and the upfront and recurring investments required to achieve and maintain efficiencies. IRS makes a decision to compete based on strategic business alignment, investment risks, return on investment and alignment with the FAIR Act and other PMA goals including Human Capital initiatives.

COMPLETED: May 17, 2004.

RESPONSIBLE OFFICIAL:

Director Office of Competitive Sourcing OS:A:OCS

CORRECTIVE ACTION MONITORING PLAN:

The Office of Competitive Sourcing will continue to incorporate lessons learned and best practices to further refine guidance and procedures.

The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

RECOMMENDATION 2:

The Chief, Agency-Wide Shared Services, should ensure that the Office of Competitive Sourcing establishes realistic milestones for competitive sourcing projects by considering relevant factors, responsibilities and historical time periods for similar tasks and incorporate the milestones into finalized project schedule guidelines

CORRECTIVE ACTION:

OCS is following project management disciplines; including planning and scheduling and incorporating lessons learned/past experience for CS competitions. OCS has taken steps to support compressing the timelines by:

- sharing lessons learned at monthly and bi-weekly team meetings,
- expanding information on the OCS web site,
- obtaining expert contractor support for project acceleration,
- providing training and
- maintaining knowledge transfer from BCA to PWS phase by keeping the same project leader to assist teams in meeting the stretch schedule goals.

These actions will ensure that OCS continues to refine and condense the project schedules.

COMPLETED: June 17, 2004.

RESPONSIBLE OFFICIAL:

Director Office of Competitive Sourcing OS:A:OCS

CORRECTIVE ACTION MONITORING PLAN:

The Office of Competitive Sourcing will continue to incorporate lessons learned and best practices to further refine and condense project schedules.

The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

RECOMMENDATION 3:

The Chief, Agency-Wide Shared Services, and the CFO should use the Automated Financial System to record and prepare cost information for competitive sourcing.

CORRECTIVE ACTION:

OCS, CFO and embedded Business Division budget contacts have been working since May 2003 to ensure that competition costs and savings are accurately captured, updated, standardized, and reported regularly in AFS/IFS. The data capture includes transition costs for voluntary early retirement and separation incentive payments, if approved. OCS enters a funding request in the Requisition Tracking System for all CS support contracts. Additional steps have been initiated to document the procedures for AFS/IFS cost tracking. Procedures will include a unique AFS/IFS project tracking codes to correspond with the Department of Treasury and Office of Management and Budget data call requirements.

IMPLEMENTATION DATE: December 1, 2004

RESPONSIBLE OFFICIAL:

Director Office of Competitive Sourcing OS:A:OCS

CORRECTIVE ACTION MONITORING PLAN:

The IRS OCS will conduct monthly progress meetings with CFO and Business Division budget contacts.

The Office of Competitive Sourcing Needs to Improve the Planning, Scheduling, and Costing of Projects

RECOMMENDATION 4:

The Chief, Agency-Wide Shared Services, and the CFO should establish written procedures for reporting costs, savings, and other required competitive sourcing data to the Department of the Treasury and to the Congress

CORRECTIVE ACTION:

OCS, CFO and embedded Business Division budget contacts have been working since May 2003 to ensure that competition costs and savings are accurately captured, updated, standardized, and reported regularly in AFS/IFS. The data capture includes transition costs for voluntary early retirement and separation incentive payments, if approved. OCS enters a funding request in the Requisition Tracking System for all CS support contracts. Additional steps have been initiated to document the procedures for AFS/IFS cost tracking. Procedures will include unique AFS/IFS project tracking codes to correspond with the Department of Treasury and Office of Management and Budget data call requirements.

IMPLEMENTATION DATE: December 1, 2004

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