

August 2001

INTERNAL REVENUE
SERVICE

Results of Review of
IRS Spending for
Business Systems
Modernization



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Abbreviations

CSC	Computer Sciences Corporation
IRS	Internal Revenue Service
IS	Information Systems
ITIA	Information Technology Investment Account
TIGTA	Treasury Inspector General for Tax Administration



United States General Accounting Office
Washington, D.C. 20548

August 17, 2001

The Honorable Byron L. Dorgan
Chairman
The Honorable Ben Nighthorse Campbell
Ranking Minority Member
Subcommittee on Treasury and General Government
Committee on Appropriations
United States Senate

The Honorable Ernest J. Istook, Jr.
Chairman, Subcommittee on Treasury,
Postal Service and General Government
Committee on Appropriations
House of Representatives

The Internal Revenue Service (IRS) received appropriations in fiscal years 1998 and 1999 of about \$506 million for information technology investments to pay for its business systems modernization costs. According to its fiscal year 1998 and 1999 appropriations, IRS may not obligate funds in the Information Technology Investment Account (ITIA) until it satisfies certain conditions, including submitting to Congress an expenditure plan that has been approved by Treasury and the Office of Management and Budget. In fiscal years 1999 and 2000, approved plans provided for expenditure of approximately \$249 million of ITIA appropriations.¹ IRS also receives appropriations each year for Information Systems (IS) to pay for its expenses related to data processing and telecommunications support, including developmental information systems and operational information systems. The IS appropriation is also available for limited purposes related to IRS' business systems modernization efforts.² In addition, IRS receives appropriations each year for Tax Law Enforcement and Processing, Assistance, and Management to pay for the cost of these programs, which includes the costs associated with IRS employees who may be involved in the business systems modernization effort.

¹In fiscal year 2001, an additional \$328.1 million of ITIA funds received congressional approval for expenditure.

²Conference and committee reports accompanying IRS' appropriations acts support the availability of IS funds for limited purposes related to the business systems modernization effort, such as modernization management, modernization support, and modernization program infrastructure.

Pursuant to your requests, we reviewed IRS expenditures relating to its business systems modernization. Our objectives were to (1) determine whether IRS used ITIA appropriations only to fund its business systems modernization costs, (2) determine the extent to which IRS used appropriations other than ITIA to fund its business systems modernization costs, and (3) review internal controls over ITIA. To accomplish these objectives, we reviewed IRS' expenditures for fiscal years 1999 and 2000 from its ITIA and other appropriations. We also reviewed IRS' internal controls over ITIA-related expenditures and reviewed related audit reports.

We briefed your offices on May 31, 2001 (the Subcommittee on Treasury, Postal Service and General Government, House Committee on Appropriations), and June 12, 2001 (the Subcommittee on Treasury and General Government, Senate Committee on Appropriations), on the results of our review. This report transmits our briefing slides and summarizes the main points presented in the briefing. The full briefing is reprinted in appendix I.

In summary, we found

- IRS obligated and expended available ITIA appropriations in fiscal years 1999 and 2000 to pay for external³ business systems modernization costs. In fiscal years 1999 and 2000, IRS expended about \$12.8 million and \$120.2 million, respectively, of ITIA appropriations and, as of September 30, 2000, had an additional \$66 million of ITIA appropriations obligated for its external business systems modernization costs. IRS' use of ITIA appropriations appears to be for purposes consistent with the fiscal year 1998 and 1999 appropriations acts⁴ and within the \$249 million in approved ITIA expenditure plans.
- IRS used its IS appropriations and other appropriations to fund both internal⁵ and external business systems modernization costs. IRS paid its internal business systems modernization costs from the IS; Tax Law Enforcement; and Processing, Assistance, and Management appropriations. However, the amount of these costs is unknown

³External costs refer to amounts paid to IRS contractors for business systems modernization efforts.

⁴Public Laws 105-61 and 105-277, respectively.

⁵Internal costs include payroll costs for IRS employees and any related support costs (such as travel for IRS employees) associated with IRS' business systems modernization efforts.

because IRS did not have a cost accounting system in place to track its internal costs for business systems modernization. IRS initiated actions in fiscal year 2000 to begin tracking its internal costs associated with specific projects through the use of project accounting codes in conjunction with its time and attendance reporting. However, these actions were not fully implemented during the time of our review.

- In addition, IRS used its IS appropriations to fund some external business systems modernization costs. In fiscal years 1999 and 2000, IRS expended \$48.6 million of IS appropriations to pay for external business systems modernization costs. Also during this period, IRS expended an additional \$9.3 million of IS appropriations for both modernization and nonmodernization costs but could not distinguish between the two.
- There were no instances that we identified in which IRS' internal controls failed to assure that expenditures against ITIA appropriations were for business systems modernization. However, we recently reported⁶ that, despite important progress, IRS has yet to fully implement the capabilities needed to effectively manage the business systems modernization program. In addition, the Treasury Inspector General for Tax Administration (TIGTA) reported that internal controls for managing IRS' business systems modernization efforts were inadequate before the Business Systems Modernization Office began operations in July 2000 but have since been improved.

Scope and Methodology

To accomplish our objectives, we reviewed (1) all expenditures IRS charged in fiscal years 1999 and 2000 against its ITIA appropriations, (2) all expenditures in fiscal years 1999 and 2000 to Computer Sciences Corporation (CSC), MITRE Corporation, and TRW, and expenditures in the first 9 months of fiscal year 2000 to selected other vendors⁷ that IRS charged to its IS appropriations, (3) all expenditures in fiscal year 1999 and expenditures in the first 9 months of fiscal year 2000 to CSC, MITRE, and TRW that IRS charged to its other appropriations, (4) internal controls over expenditures, and (5) reports issued by the TIGTA related to contract management controls.

⁶*IRS Modernization: Continued Improvement in Management Capability Needed to Support Long-Term Transformation* (GAO-01-700T, May 8, 2001).

⁷We selected Booz, Allen and Hamilton; Grumman Data Systems; and Management Systems Designers because of their prior assistance to IRS in its organizational restructuring and modernization efforts.

We performed our work at IRS' Administrative Services Center in Beckley, W.V., and at IRS offices in the Washington, D.C., area. We performed our work from August 2000 through May 2001 in accordance with U.S. generally accepted government auditing standards.

Agency Comments

In commenting on a draft of our report, IRS generally agreed with our findings and stated that it is making steady progress in managing its business systems modernization program. This includes establishing a technical framework to guide all business systems modernization project developments, fully implementing rigorous configuration management practices, and establishing a key executive position to manage and control IRS' technology investment spending. The complete text of IRS' comments is reprinted in appendix II.

We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate Committee on Appropriations; Senate Committee on Finance; Senate Committee on Governmental Affairs; Senate Committee on the Budget; Subcommittee on Taxation and IRS Oversight, Senate Committee on Finance; and Subcommittee on Oversight of Government Management, Restructuring, and the District of Columbia, Senate Committee on Governmental Affairs. We are also sending copies of this report to the Chairmen and Ranking Minority Members of the House Committee on Appropriations; House Committee on Ways and Means; House Committee on Government Reform; House Committee on the Budget; Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations, House Committee on Government Reform; and Subcommittee on Oversight, House Committee on Ways and Means, and to the Chairman of the Subcommittee on Foreign Operations, Export Financing and Related Programs, House Committee on Appropriations, and the Ranking Minority Member of the Subcommittee on Treasury, Postal Service and General Government, House Committee on Appropriations. In addition, we are sending copies of this report to the Chairman and Vice-Chairman of the Joint Committee on Taxation, the Commissioner of Internal Revenue, the Secretary of the Treasury, the Director of the Office of Management and Budget, the Chairman of the IRS Oversight Board, and other interested parties. Copies will be made available to others upon request.

This report was prepared under the direction of Steven J. Sebastian, Acting Director, who can be reached at (202) 512-9521. He can also be reached at

sebastians@gao.gov. If I can be of further assistance, please call me at (202) 512-2600. Key contributors to this report are listed in appendix III.

A handwritten signature in black ink, reading "Jeffrey C. Steinhoff". The signature is written in a cursive style with a large initial "J" and a distinct "C" before the last name.

Jeffrey C. Steinhoff
Managing Director
Financial Management and Assurance

Briefing to Senate and House Subcommittee Staffs



Financial Management and
Assurance

Review of IRS Expenditures for Business Systems Modernization

Briefing to Staffs of
the Subcommittee on Treasury
and General Government,
Senate Committee on Appropriations

June 12, 2001

and

the Subcommittee on Treasury, Postal Service,
and General Government,
House Committee on Appropriations

May 31, 2001

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Briefing Overview

- Introduction
- Objectives
- Scope and Methodology
- Background
- Results in Brief
- Results
- Conclusions



Introduction

- This is a briefing on the results of our review of IRS' expenditures, in fiscal years 1999 and 2000, for its business systems modernization efforts.
- IRS received, in fiscal years 1998 and 1999, appropriations for information technology investments to pay for IRS' business systems modernization costs. According to IRS' fiscal years 1998 and 1999 appropriations, IRS may not obligate funds in the Information Technology Investment Account (ITIA) until certain conditions are satisfied, including congressional approval of its expenditure plan.



Introduction

- IRS also receives annual appropriations each year for Information Systems (IS) to pay for its expenses related to data processing and telecommunications support, including developmental information systems and operational information systems. The appropriation is available for limited purposes related to IRS' business systems modernization efforts.
- GAO was requested to review IRS expenditures relating to business systems modernization.



Objectives

- Our objectives were to
 - Determine whether IRS used ITIA appropriations only to fund its business systems modernization costs;
 - Determine the extent to which IRS used appropriations other than ITIA to fund its business systems modernization costs; and
 - Review internal controls over ITIA.



Scope and Methodology

- To accomplish our objectives, we
 - Reviewed all expenditures IRS charged in FY 1999 and FY 2000 against its ITIA appropriations;
 - Reviewed all expenditures in FY 1999 and FY 2000 to Computer Sciences Corporation (CSC), MITRE Corporation, and TRW, and expenditures in the first 9 months of FY 2000 to selected other vendors¹ that IRS charged to its IS appropriations;
 - Reviewed all expenditures in FY 1999 and expenditures in the first 9 months of FY 2000 to CSC, MITRE, and TRW that IRS charged to its other IRS appropriations;

¹We selected Booz, Allen and Hamilton, Grumman Data Systems, and Management Systems Designers because of their prior assistance to IRS in its organizational restructuring and modernization efforts.



Scope and Methodology

- Reviewed internal controls over expenditures; and
- Reviewed Treasury Inspector General for Tax Administration (TIGTA) reports on contract management controls.
- Performed our work at IRS' Administrative Services Center in Beckley, W.V., and at IRS offices in the Washington, D.C. area.
- We performed our work from August 2000 through May 2001 in accordance with U.S. generally accepted government auditing standards.



Background

- IRS' external² business systems modernization costs are currently funded by two separate appropriations.
 - Appropriations for ITIA
 - Appropriations for IS
- IRS' internal³ business systems modernization costs are funded by the IS, Tax Law Enforcement (TLE), and Processing Assistance and Management (PAM) appropriations.

²External costs refer to amounts paid to IRS contractors for business systems modernization efforts.

³Internal costs include payroll costs for IRS employees and any related support costs (such as travel for IRS employees) associated with IRS' business systems modernization efforts.



Background

- Funds in the ITIA are for necessary expenses for business systems modernization as described in the Modernization Blueprint.⁴ The obligation of ITIA funds is prohibited until certain statutory conditions are satisfied.
- Before ITIA funds are available for obligation, IRS must submit to the Congress for approval a plan for expenditure that, among other things, has been reviewed and approved by Treasury and OMB, and has been reviewed by GAO.

⁴ This blueprint is a target enterprise systems architecture that describes in general terms the future systems environment needed to satisfy the business requirements, and a general sequencing plan for transitioning from IRS' current systems environment to its future systems environment.



Background

- ITIA authorized funding was as follows:
 - **ITIA Funds Appropriated - \$505.7 million**
 - 1998 Appropriations Act – \$325 million
(Available from 9-1-98 to 9-30-00)
 - Of this amount, \$30.3 million was rescinded by
Public Law 105-174.
 - 1999 Appropriations Act – \$211 million
(Available from 9-30-99 to 9-30-02)



Background

- **ITIA Funds Approved in Fiscal Years 1999 and 2000 for Expenditure - \$249.3 million⁵**
 - Congressional Approvals Received in FY 1999 – \$35.1 million
 - Congressional Approvals Received in FY 2000 – \$214.2 million

⁵In FY 2001, an additional \$328.1 million of ITIA funds received congressional approval for expenditure.



Background

- Funds in the IS account are for necessary expenses for data processing and telecommunications support for IRS activities, including both developmental information systems and operational information systems.
- The use of these funds is prohibited for the award of or initiation of a Prime Systems Integration Services (PRIME) contract to implement the Modernization Blueprint. However, these funds are available for developing the request for proposals (RFP) for the PRIME contract and for limited purposes related to the business systems modernization effort.



Background

- Various Conference and Committee Reports support the availability of IS funds for limited purposes related to the business systems modernization effort. For example
 - For fiscal year 1998, \$32.1 million of IS funds were available for modernization management and modernization support through September 30, 1999. For example, IS funds were available for modernization support to continue efforts to implement the Modernization Blueprint and to complete the necessary details.⁶
 - In fiscal year 1999, \$68.7 million of IS funds were available for the modernization program infrastructure through September 30, 2000.⁷

⁶House of Representatives Conference Report 105-284, dated September 29, 1997.

⁷House of Representatives Conference Report 105-825, dated October 19, 1998.



Background

- In December 1998, IRS awarded its PRIME contract to Computer Sciences Corporation (CSC).
- Under the PRIME contract, CSC performs work and coordinates and oversees the work of various subcontractors that are involved in IRS' business systems modernization effort.
- IRS pays for costs incurred under the PRIME contract and other contracts related to business systems modernization, and any related equipment costs, from its ITIA funds.
- IRS' practice is not to charge internal IRS costs to the ITIA appropriation.



Results in Brief

- ITIA appropriations expended and obligated in FY 1999 and FY 2000 to pay for IRS' external business systems modernization costs appear to be for purposes consistent with
 - FY 1998 and FY 1999 Appropriations Acts,⁸ and
 - Approved ITIA expenditure plans.

⁸Public Laws 105-61 and 105-277, respectively.



Results in Brief

- Information Systems (IS) and other appropriations were also used to fund IRS' business systems modernization costs.
 - IS appropriations also funded external business systems modernization costs.
 - IRS paid its internal costs from IS and other appropriations but the amount is unknown.



Results in Brief

- We found no instances where IRS' internal controls failed to assure that expenditures against ITIA appropriations were for business systems modernization.
- We recently reported⁹ that, despite important progress, IRS has yet to fully implement the capabilities needed to effectively manage the business systems modernization program.
- The TIGTA reported that internal controls for managing IRS' business systems modernization efforts were inadequate before the Business Systems Modernization Office (BSMO) began operations in July 2000 but have since been improved.

⁹ *IRS Modernization: Continued Improvement in Management Capability Needed to Support Long-Term Transformation* (GAO-01-700T, May 8, 2001).



Results

- **ITIA Appropriations Were Expended for Business Systems Modernization**
 - IRS expended about \$12.8 million of ITIA appropriations in fiscal year 1999 and \$120.2 million in fiscal year 2000 for its external business systems modernization costs.
 - IRS also had another \$66 million of ITIA appropriations obligated as of 9/30/00.



Results

- **IS and Other IRS Appropriations Were Also Used to Fund Business Systems Modernization**
 - IRS used \$48.6 million of IS appropriations to pay for its external business systems modernization costs.
 - IRS expended \$33.9 million of IS appropriations in fiscal years 1999 and 2000 for external business systems modernization costs relating to its integrated support contract (ISC) with TRW.
 - IRS initially considered work under the ISC contract not to be business systems modernization costs to be funded from ITIA appropriations.



Results

- In March 2000 IRS determined that some ISC work was business systems modernization-related and began funding it under ITIA.
- IRS expended \$14.7 million of IS appropriations in fiscal years 1999 and 2000 for other external business systems modernization costs.
- IRS expended an additional \$9.3 million of IS appropriations for both modernization and non-modernization costs but could not clearly distinguish between the two.



Results

- **Obligations Changed From IS to ITIA Appropriation**
 - IRS initially charged \$7.4 million of obligations to IS appropriations for business systems modernization costs and later changed them to ITIA appropriations. In general:
 - IRS obligated funds under IS appropriations in June 1999.
 - IRS accepted services in July and August 1999.



Results

- IRS deobligated the funding under IS and reobligated the funds under ITIA appropriations in September 1999.
- IRS expended funds from ITIA appropriations from October through December 1999.



Results

- **Some IS Appropriations Were Expended in Error**
 - According to IRS officials, IRS charged 4 payments totaling about \$963,000 to IS appropriations in error.
 - Obligation information in IRS' records identified IS appropriations as the funding source instead of ITIA appropriations.
 - Accounting staff was unaware of the intent to use ITIA appropriations instead of IS.
 - IRS subsequently corrected the error for 2 of the payments totaling \$542,000.



Results

- **IRS' Internal Costs Were Paid From IS and Other IRS Appropriations But the Amount Is Unknown**
 - IRS' internal costs for business systems modernization are paid from various appropriations but have not been tracked.
 - IRS did not have a cost accounting system in place to track its internal costs for business systems modernization.
 - Consequently, the full cost of IRS' business systems modernization efforts cannot be reasonably determined.



Results

- In FY 2000, IRS initiated actions to begin tracking its internal costs associated with specific projects through the use of project accounting codes in conjunction with its time and attendance (T&A) reporting.
 - In March 2000¹⁰ the Business Systems Modernization Executive issued guidelines for tracking obligations and commitments that can be directly linked to business systems modernization.
 - In July 2000, the Deputy Chief Financial Officer for Finance issued a memorandum requesting all staff working on projects to charge their time to appropriate project accounting codes when preparing their T&A reports.

¹⁰A year later, in March 2001, the Associate Commissioner, Business Systems Modernization, and Deputy CFO for Strategic Planning and Budgeting issued updated guidance.



Results

• Internal Controls

- IRS' internal controls to manage and safeguard ITIA expenditures are implemented through BSMO which provides oversight, coordination, and approval for the use of ITIA appropriations.
- BSMO began operations under an executive director in July 2000.
- Prior to BSMO, the Enterprise Program Management Office (EPMO) provided oversight of systems modernization efforts and reported to the Chief Information Officer who had final approval within IRS for the use of both ITIA and IS appropriations.



Results

- **GAO Tested Internal Controls**

- GAO tested certain controls during its audit of IRS' FY 2000 financial statements and its review of ITIA transactions and found no instances where IRS' controls failed to assure that
 - IRS had a valid obligation and had received goods or services before making payment to vendors for ITIA-related expenses.
 - Projects charged to ITIA appropriations matched approved expenditure plans.



Results

- **GAO Recently Reported on IRS Business Systems Modernization Controls**
 - GAO has reported¹¹ that IRS has made important progress in managing its business systems modernization program.
 - However, IRS has yet to fully implement the controls and capabilities needed to effectively manage the business systems modernization program.
 - Work on certain key aspects of business systems modernization was slower than anticipated.
 - Modernization projects were proceeding past critical milestones without certain essential management controls.

¹¹ *IRS Modernization: Continued Improvement in Management Capability Needed to Support Long-Term Transformation* (GAO-01-700T, May 8, 2001).



Results

- **TIGTA Tested Modernization Management Controls**
 - TIGTA conducted audits of IRS' systems modernization efforts and found that management controls have improved.
 - During October 1999 through March 2000 (prior to the emergence of BSMO), TIGTA reviewed IRS' systems modernization oversight and reported that related management controls were inadequate.



Results

- During June through August 2000 (after the emergence of BSMO), TIGTA again reviewed IRS' systems modernization oversight and reported that IRS was making progress in building program management capabilities.



Conclusions

- ITIA appropriations were used for external costs associated with IRS' business systems modernization efforts.
- IS appropriations have also funded limited external costs associated with IRS' business systems modernization efforts.
- There were no instances identified in which IRS' controls over expenditures from ITIA during fiscal years 1999 and 2000 failed to provide assurance that funds were obligated and expended for business systems modernization costs. However, GAO and TIGTA reports continue to note the need for further improvement in management controls over business systems modernization.

Comments From the Internal Revenue Service



COMMISSIONER

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

August 3, 2001

Mr. Steven J. Sebastian
Acting Director, Financial
Management and Assurance
U.S. General Accounting Office
441 G Street N.W.
Washington, D.C. 20548

Dear Mr. Sebastian:

Thank you for the opportunity to respond to your draft report titled, "Internal Revenue Service: Results of Review of IRS Spending for Business Systems Modernization." As one of the largest public sector financial management institutions, fiscal management and integrity are cornerstones to the mission of the Internal Revenue Service.

We are very pleased the GAO validated that:

- The IRS is spending Information Technology and Investment Account (ITIA) for Business Systems Modernization as directed by Congress
- The IRS is making progress in building program management capabilities

The IRS is making steady and solid progress managing the program and delivering tangible benefits to the taxpayer. Since your audit, I reported to the Congress our important progress in management capabilities. I detail our accomplishments below.

Enterprise Architecture Guides All Business Systems Modernization (BSM) Project Developments

We are confident the Enterprise Architecture (EA) Versions (1.0), issued December 2000, and Version (1.1), issued June 2001, established the necessary technical framework as a foundation on which we will build all BSM projects. While we expect to update the EA periodically to keep it current and effective, it is sufficiently robust to provide guidance to BSM projects now underway.

In addition, to ensure accountability and consistency of BSM Projects to the EA, we created the 2002 Release Architecture. This release architecture identifies the configuration items we can trace to the EA and allocate to specific

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modernization projects. We now require architectural certification for every project before exiting Milestone 3. This certification will ensure compliance with the EA. The reviews prior to certification evaluate each project on:

- Design consistency with the technical reference model in the EA
- Compliance with architectural standards
- Systems interfaces as defined in the EA
- Compliance with architectural security and privacy requirements
- Alignment of the Systems Design with the transition strategy
- Modifications from the EA requiring waivers or architecture change requests

In addition, the Systems Engineering Board provides ongoing engineering leadership and guidance. The Customer Account Data Engine (CADE) Project is the first to receive this formal architectural certification, which we now require for all BSM projects. This is a significant achievement for the project, the program and for the IRS.

Configuration Management Is Now Fully Implemented

We made significant progress implementing rigorous configuration management practices in all our many modernization projects. With assistance from MITRE, we assessed the PRIME configuration management program last January. We implemented several key improvements in June 2001; our improvements include:

- Assigning unique identifiers for configuration items
- Establishing baselines for deliverables and placing them under control of data management and approval processes
- Placing the Enterprise Life Cycle Process Asset Library, our documented methodology, under configuration management control

In addition, we established a process for managing changes to architectural baselines. Modifications require change requests (CR), including an impact analysis citing functional, cost, and schedule impacts. The Business Systems Modernization Office and PRIME Configuration Control Boards (CCBs) then approve these change requests. These boards have been operational since September 2000, and we chartered them with fully defined roles and responsibilities in February 2001. We also established control practices and tools to assist the CCBs in change management. These practices and tools include:

- A change request tracking system to control changes to the baseline configuration items
- A deliverables database repository, which houses the official baseline documentation

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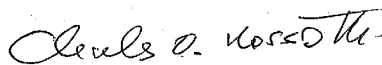
- Analytical tools to assess the impact of configuration changes to the EA and project plan baselines

Finally, the Deputy Commissioner for Modernization and the Chief Information Officer added a key executive position to his organization to provide additional financial expertise and rigorous oversight to manage and control our technology investment spending.

While our achievements are important, we are committed to aggressively managing the risks, cost and schedule changes associated with such a large and complex program.

Thank you for your guidance and the work of your staff. If you have any questions or need additional information, please call me or John Reece, Deputy Commissioner for Modernization & Chief Information Officer at (202) 622-6800.

Sincerely,



Charles O. Rossotti

GAO Contact and Staff Acknowledgments

GAO Contact

Joan Hawkins, (202) 512-8433

Acknowledgments

In addition to the person named above, other key contributors to this report were John Davis, David Fisher, Mickie Gray, and Julia Ziegler.

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