

United States General Accounting Office

GAO

Report to the Chairman, Committee on
Government Operations, House of
Representatives

January 1990

IRS AUTOMATION

Procurement Practices Need Strengthening





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

Information Management and
Technology Division

B-236918

January 12, 1990

The Honorable John Conyers, Jr.
Chairman, Committee on Government
Operations
House of Representatives

Dear Mr. Chairman:

This report responds to your July 24, 1989, request that we review several procurements under the automated data processing (ADP) acquisition program of the Internal Revenue Service (IRS). In subsequent meetings with your office, we agreed that we would review four specific issues. Those issues and our findings are summarized below.

Results in Brief

Issue #1: Are the procedures being used by the IRS to award a contract noncompetitively to Vanguard Technologies Corporation for ADP support services for the Electronic Filing System¹ appropriate?

Response: No. In this estimated \$1.7 million project, planned for award in late January 1990, IRS has circumvented provisions of the Competition in Contracting Act (41 U.S.C. 253 et seq.) designed to maximize competition in government contracting. In an attempt to ensure that changes to the Electronic Filing System would be completed in time for the 1990 filing season, IRS has improperly permitted Vanguard to proceed with work since May 1989 (1) without a written contract; (2) before contacting other potential offerors; and (3) before obtaining all necessary approvals within IRS and the Department of the Treasury.

Issue #2: Is IRS' July 1989 agreement to pay \$15,000 to Vanguard Corporation in return for Vanguard withdrawing a bid protest before the General Services Board of Contract Appeals on a \$500 million award for ADP support services appropriate?

Response: No. In our view, the agreement is inappropriate because IRS has no reasonable basis on which to conclude that it had violated a statute, regulation, or delegation of procurement authority in eliminating

¹The Electronic Filing System automates the receipt of individual tax returns filed electronically by tax return preparers. The Electronic Filing System is one of several projects included in the multibillion dollar IRS Tax System Modernization program. See *ADP Modernization: IRS' Progress on the Electronic Filing System* (GAO/IMTEC-88-40, July 13, 1988), and *ADP Modernization: IRS Needs to Assess Design Alternatives for Its Electronic Filing System* (GAO/IMTEC-89-33, May 5, 1989).

and is essential for proper operation of the Electronic Filing System for the 1990 filing season. Any work that is not currently under way should be limited to that which can be performed only by Vanguard.

We also recommend that the Commissioner (1) determine fully the nature and extent of the weaknesses in IRS' ADP procurement process and assess whether the corrective actions planned by IRS will correct these weaknesses, and (2) report the deficiencies identified in this report to the President and Congress as material internal control weaknesses under the Federal Managers' Financial Integrity Act.

Irregularities in Procuring ADP Services for Electronic Filing System

IRS plans to noncompetitively award a contract for a project estimated at \$1.7 million to Vanguard; this contract is for ADP services to enhance and maintain the nationwide expansion of the Electronic Filing System. The Electronic Filing System is one of several projects included in the multi-billion dollar Tax System Modernization program. The contract will serve two distinct requirements. First, the contract is to enhance existing software to process individual and business returns for the 1990 filing season. Second, the contract is to include a program to allow electronic submission of employee plans returns.²

IRS plans to award the contract with less than full and open competition on the basis of unusual and compelling urgency by the end of January 1990. The Competition in Contracting Act and Part 6 of the Federal Acquisition Regulation, which implements the act, permits agencies to contract with less than full and open competition when the agency's need is of such unusual or compelling urgency that the government would be seriously injured unless the agency is permitted to limit the number of sources from which it solicits bids or proposals. According to IRS' justifications supporting this procurement as well as IRS officials' statements, the software changes to the Electronic Filing System must be incorporated for the 1990 tax filing season and Vanguard's prior experience working on this software made them the only contractor able to meet the deadlines for implementing changes to the system for the 1990 filing season. Although IRS believes that it was faced with circumstances that called for using less than full and open competition, when this procurement approach is used, all pertinent laws and regulations still need to be followed.

²Employee plans are deferred compensation arrangements established by employers to provide income after retirement. Once a plan meets certain IRS standards, an employer can deduct plan contributions. Earnings on the contributions are exempt from tax, and employees are not taxed on contributions or earnings until a distribution is made, usually at retirement.

this authorization from Treasury until late June 1989, 2 months after Vanguard had begun work. This authorization, originally granted for \$745,000, was increased to \$1,745,000 in September 1989. Electronic Filing System Office officials and the Chief, Office of Tax Systems Acquisition said the estimated cost of the procurement more than doubled because the original cost underestimated the number of hours Vanguard would require to perform the tasks in the statement of work. As of December 31, 1989, Vanguard's proposal was still being evaluated by IRS.

IRS officials admitted that they had no specific authority to allow Vanguard to proceed without a written contract. They said that they plan to take a number of actions to correct the weaknesses in their procurement activities, including hiring additional personnel and reorganizing the procurement organization. They also said that oral contracts will not be used in the future.

The Federal Managers' Financial Integrity Act (31 U.S.C. 3512 (b) and (c)), requires agencies to establish systems of internal controls for ensuring that obligations and costs comply with applicable law, and to annually report material weaknesses in these controls and the status of corrective actions until they are corrected. Material weaknesses are weaknesses of sufficient importance to warrant the attention of the President and the Congress. For example, material weaknesses could significantly impair the fulfillment of an agency mission or significantly weaken safeguards against the loss or waste of funds, property, or other assets. Failure to follow established procurement law, regulation, or other procurement procedures is a material internal control weakness because it skirts the internal controls intended to ensure prudent use of the government's resources as laid out in these requirements. IRS' circumvention of the Federal Acquisition Regulation regarding the Vanguard contract is a material weakness which should be reported under the provisions of the Financial Integrity Act.

In our view, IRS did not have a reasonable basis to conclude that such a violation had occurred. Part 15 of the Federal Acquisition Regulation provides that an offer should be included in the competitive range if it has a substantial chance for award. IRS' solicitation for this contract provided that award would be made based on the proposal offering the best overall value to the government and that technical factors would be weighted as substantially more important than price. There was a wide disparity between the technical scores of Vanguard and OAO, with OAO's proposal receiving a near-perfect score; also, OAO's proposed price was significantly lower than Vanguard's. The board found that even if IRS had included Vanguard's proposal in the competitive range and conducted discussions with the firm in those areas where it would have been permissible to do so, it would have been "extraordinarily unlikely" that Vanguard would have surpassed OAO's technical score. To receive the award, Vanguard also would have had to make "enormous price reductions."

We agree with the board that "the likelihood of discussions leading to an award to Vanguard appear[ed] negligible," and we therefore see no reasonable basis for a conclusion by IRS that there was a significant risk of Vanguard successfully challenging its exclusion from the competitive range. It is therefore our view that the \$15,000 settlement is inappropriate.

Services Ordered From Vanguard Under Contract TIR-85-0289 Were Within Scope

In July 1985, IRS awarded a contract (TIR-85-0289) to Vanguard for ADP support services. This was a requirements contract with a maximum value of \$50 million under which IRS issued delivery orders to perform specific ADP services. The services to be performed included requirements definition, systems analysis and design, software development, testing, maintenance, program and project management, and a variety of miscellaneous ADP functions such as training, data entry, and technical writing. As of September 1989, a total of 202 delivery orders had been issued under this contract: 33 orders were in progress, 135 had been completed, and 34 orders had been cancelled. The total cost of active and completed delivery orders was \$49.5 million.

We compared the scope section of the contract to the statements of work for 26 delivery orders. These included all 22 delivery orders issued that were valued over \$500,000 and the four most recently issued orders. We found all were within the scope of the contract. The delivery orders we reviewed were for ADP services supporting a broad range of IRS programs

The ICS request for proposals was issued on October 25, 1988, and the closing date was August 28, 1989. The TMAC request for proposals was issued January 4, 1989, and the closing date was September 18, 1989. As of December 1989, IRS was reviewing the proposals submitted by offerors for both procurements. The Chief of IRS' Office of Tax Systems Acquisition said that, as of November 1989, no protests concerning either request for proposal had been lodged. He estimated that the ICS contract will be awarded in August 1990, and that the TMAC contract will be awarded in September 1990.

ICS and TMAC Requests for Proposals Permitted Full and Open Competition

The Federal Acquisition Regulation and the Federal Information Management Regulation generally require federal agencies to use specifications in requests for proposals that will promote full and open competition. In our review of the technical specifications for ICS, we found three requirements for compatibility with vendor-specific hardware and communications protocols. Our comparable review of TMAC disclosed five specifications that called for vendor-specific software, compatibility with specific equipment, or that otherwise appeared to limit competition. Our review of these technical specifications showed, however, that they appear to be justified by the agency's needs and therefore did not unduly limit competition. In addition, the technical specifications could be satisfied by many vendors. More detailed information on these technical specifications and our analysis is included in Appendix I.

Scope and Methodology

To obtain the information presented in this report, we interviewed IRS headquarters officials, attorneys representing Vanguard Technologies Corporation in Washington, D.C., and officials of OAO Corporation in Greenbelt, Maryland. We reviewed documents used by IRS attorneys to support the General Services Administration Board of Contract Appeals hearing process, as well as other documentation, including requests for proposals, for the acquisitions discussed. We also reviewed about \$33 million of the \$50 million in task orders performed under the 1985 ADP support services contract between IRS and Vanguard to determine whether the work performed was within the scope of the contract. We selected for review all task orders valued at more than \$500,000 as well as the four most recently issued lower value task orders. We conducted our review from August 1989 through December 1989, in accordance with generally accepted government auditing standards.

**Appendix I
Analysis of Technical Specifications in the
Integrated Collection System and Treasury
Multiuser Acquisition Contract Requests
for Proposals**

3. The primary operating system for each different binary-compatible computer family offered shall meet the Portable Operating System Interface for Computer Environments (POSIX) requirements at contract award. The results of running the National Institute of Standards and Technology POSIX Federal Information Processing Standards Conformance Test must be provided, including a statement by the offeror showing the date that the operating system was tested. It must have been tested on at least one of the hardware configurations being offered.
4. The proprietary Oracle and Informix data base management system software shall be proposed.
5. Network adaptor cards to provide connectivity with existing personal computers to the proposed Local Area Networks. The three cards required for IRS' existing personal computers are IBM PC or PC/XT compatible, IBM XT/286 or AT compatible, and IBM PS/2 or Tandy compatible.

As with the ICS requirements discussed above, we found none that did not appear justified by the agency's needs and that could not be met by many vendors. The 32-bit architecture requirement is necessary to meet IRS' performance needs, and can be met by most vendors in the marketplace. Similarly, the specified swivel capability is standard and most vendors can meet this requirement or could add a commercially available swivel base to the display at a nominal cost. The operating system testing requirement means only that proposals must adhere to government POSIX standards. The proprietary data base management software is currently in use by IRS for a variety of applications and IRS plans to operate these applications on the new equipment. In this respect, this proprietary data base management software will operate on most vendors' equipment. Finally, the network adapter cards are necessary to permit connectivity with existing equipment, and most local area networks have this capability.

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Analysis of Technical Specifications in the Integrated Collection System and Treasury Multiuser Acquisition Contract Requests for Proposals

To determine whether the technical specifications in the requests for proposals for the Integrated Collection System (ICS) and the Treasury Multiuser Acquisition Contract (TMAC) would promote full and open competition, we reviewed the technical specifications in the statements of work (Section C) of both requests for proposals. We identified those specifications that called for vendor-specific or compatible hardware or software or that otherwise appeared to restrict competition and analyzed them to determine if they were justified and allowed for competition.

The potentially restrictive technical specifications we identified in the ICS request for proposals are:

1. Tape units that shall be fully media compatible with existing IBM model 3420-8 tape drives.
2. Cartridge tape units that shall be functionally equivalent to the IBM model 3480 cartridge tape unit.
3. The capability for interfacing with retained equipment, including the Rockwell Automatic Call Distributor and IBM model 3179 and 3101 terminals.

We found nothing in these specifications that did not appear justified by the agency's needs. The first two specifications called for potential vendors to propose equipment that could read existing magnetic tape files. The third specification was justified because it required a capability to interface with existing equipment that is to be retained. Further, the majority of hardware manufacturers in business today support software capable of reading and writing magnetic tape that is fully compatible with IBM tape units and support the protocols necessary for interfacing with the devices specified in these specifications.

Potentially restrictive technical specifications we identified in the TMAC request for proposals are:

1. A minimum 32-bit processor and a minimum 32-bit data path for the multiuser computer system architecture.
2. Terminal screens capable of swiveling a minimum of 180 degrees.

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Abbreviations

ADP	Automated Data Processing
GAO	General Accounting Office
IMTEC	Information Management and Technology Division
ICS	Integrated Collection System
IRS	Internal Revenue Service
POSIX	Portable Operating System Interface for Computer Environments
TMAC	Treasury Multiuser Acquisition Contract

We discussed the facts presented in this report with IRS officials during the course of our work and have incorporated their views where appropriate. We did not obtain official agency comments on a draft of this report.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to the Secretary of the Treasury, the Commissioner of Internal Revenue, and other interested parties, and will make copies available to others upon request. This report was prepared under the direction of Mr. Howard G. Rhile, Director, General Government Information Systems, who can be reached at (202) 275-3455. Other major contributors are listed in appendix II.

Sincerely yours,

A handwritten signature in cursive script that reads "Ralph V. Carlone".

Ralph V. Carlone
Assistant Comptroller General

and activities such as the Electronic Filing System, a facilities management system, and the Integrated Collection System.⁴ Services provided included systems design, software development, data entry services, testing, and training.

ICS and TMAC Requests for Proposals Comply With Federal Acquisition Regulation

The ICS and TMAC requests for proposals comply with Federal Acquisition Regulation and Federal Information Resources Management Regulation requirements concerning full and open competition.

Description of ICS and TMAC

Under ICS, IRS plans to buy 21 mainframe computer systems and associated peripheral equipment, more than 10,000 portable and over 6,000 non-portable workstations, software, and systems engineering and training support. The hardware, software, and support services are intended to (1) increase collection of delinquent tax returns and revenues, (2) improve voluntary compliance with the federal tax filing and payment requirements, (3) provide more timely access to and updating of taxpayer information, and (4) increase the efficiency of collection employees. For this procurement, the General Services Administration has delegated procurement authority of \$458 million.

TMAC will supply ADP equipment and services, as required, to all Treasury organizations nationwide. Treasury has given IRS responsibility for managing this procurement. Treasury estimates it will obtain 3,220 multiuser computers, 7,000 terminals, and 49,538 workstations, together with associated software over 5 years. The contract will also provide configuration management, training, and maintenance support of this equipment for up to 7 years. The contract will provide an option for acquiring microcomputers and multiuser systems and associated software for numerous projects including the Automated Examination System, Automated Taxpayer Services System, and the Automation of Criminal Investigation. The General Services Administration has delegated procurement authority of \$1.866 billion to Treasury for this contract.

⁴The Integrated Collection System is intended to fully automate IRS' collection of unpaid accounts and obtaining of delinquent returns. Further, the system is planned to support the analysis of why accounts become delinquent and why returns are not filed.

IRS' Agreement to Pay Vanguard \$15,000 Is Inappropriate

On April 26, 1989, Vanguard protested to the IRS that the agency had improperly excluded it from the competitive range³ for award of a \$500 million contract for ADP support services. IRS denied the protest on June 14, 1989, and the contract was awarded on the same day to another offeror, OAO Corporation. Vanguard then filed a similar protest on June 23, 1989, with the General Services Board of Contract Appeals. According to IRS officials, after an additional review of the work of the panel that had evaluated Vanguard's technical proposal, IRS concluded that it could have cleared up certain discrepancies in Vanguard's proposal and included Vanguard in the competitive range. IRS attorneys and other officials familiar with the case told us that the agency also had doubts that it would prevail in the protest before the board. As a result, on July 19, 1989, IRS entered into a settlement agreement with Vanguard.

The IRS-Vanguard settlement agreement provided that IRS would terminate the ADP support services contract it had signed with the OAO Corporation in June 1989, and admit Vanguard to the competitive range. In addition, IRS agreed to pay \$15,000 to Vanguard. As of January 10, 1990, IRS had not made the payment. Upon learning of the agreement, OAO filed a protest with the board seeking to have the agreement overturned. In September 1989, the board ruled that IRS' original actions eliminating Vanguard from the competitive range and awarding the contract to OAO were reasonable. The board directed that the agency continue its contract with OAO.

According to IRS officials, the \$15,000 payment constitutes reimbursement for attorneys' fees incurred by Vanguard. Attorneys' fees generally are not payable by the government in the absence of specific statutory authority. However, the Brooks Act permits the General Services Board of Contract Appeals to award protest costs, including attorneys' fees, when it determines that a challenged agency action violated a statute or regulation or the conditions of a delegation of procurement authority (40 U.S.C. 759(h)(5)(C)(i)). Whether this authority extends to agencies settling protests filed under the act is an open question. In any case, even if the Brooks Act authority applied here, the standard for award of costs under the act, a finding that a challenged agency action violated a statute or regulation or the conditions of any delegation of procurement authority, has not been satisfied.

³The Federal Acquisition Regulation provides that a competitive range is determined by the contracting officer based on the evaluation factors in the solicitation. The competitive range includes all proposals with a reasonable chance for award.

Contractor Given Oral Authorization to Proceed

In October 1989, officials of the Electronic Filing System Office told us that although no written contract had been signed with Vanguard, Vanguard employees began performing services on May 1, 1989. According to the Chief of the Office of Tax Systems Acquisition, he orally authorized Vanguard to begin work because (1) the Electronic Filing Systems Office was late in providing an adequate statement of work, and (2) it was necessary to meet the schedules to implement the Electronic Filing System on a nationwide basis for the 1990 tax filing season.

In our view, IRS improperly permitted Vanguard to proceed with work. The Federal Acquisition Regulation does not provide for the use of oral contracts except in limited circumstances—such as small purchases from imprest funds—that do not apply here. In this case, the contracting officer was not authorized to allow Vanguard to proceed without a written contract.

Other Procurement Requirements Were Not Met Until After Contractor Started Work

Vanguard began work before IRS (1) contacted other potential offerors, (2) had all necessary IRS approvals to contract with less than full and open competition, and (3) received procurement authorization from the Department of the Treasury.

The Competition in Contracting Act requires that before contracting without full and open competition because of urgency, the agency shall solicit offers from as many sources as is practicable under the circumstances. We found that IRS contacted two other potential vendors, but this was not done until July 1989, and Vanguard began work on May 1, 1989.

In an attempt to keep the Electronic Filing System changes on schedule, IRS permitted Vanguard to begin work on May 1, 1989, before getting the necessary approvals. The two justifications supporting the decision to contract with less than full and open competition were not certified by the contracting officer until May 31 and July 13, 1989, respectively, and did not receive the required approval from IRS' Deputy Assistant Commissioner, Human Resources Management and Support, until June 8 and July 19, 1989, respectively.

Finally, our review disclosed that IRS did not meet the Department of the Treasury requirements for a timely request for a procurement authorization. According to the Chief, Office of Tax Systems Acquisition, all noncompetitive procurements over \$100,000 must be approved by the Department of the Treasury. However, IRS did not request and receive

Vanguard from the competition. Although IRS agreed to make this payment, no payment had been made as of January 10, 1990.

Issue #3: Are services provided by Vanguard under a prior ADP support services contract (TIR-85-0289) within the contract's scope?

Response: Yes. We reviewed 26 of the 202 delivery orders that IRS issued under this 1985 contract. These 26 orders accounted for about 66 percent of the contract costs. Our review included (1) all 22 orders where each order was worth over \$500,000, as well as (2) the four most recent delivery orders. We found all were within the scope of the contract.

Issue #4: Did the requests for proposals for the Treasury Multiuser Acquisition Contract (TMAC) and Integrated Collection System (ICS) procurements permit full and open competition?

Response: Yes. Our review showed that both requests for proposals were in compliance with the Federal Acquisition Regulation and appeared to permit full and open competition.

Conclusions and Recommendations

IRS' disregard for established procurement policies and procedures in procuring ADP services for the Electronic Filing System and settling the protest before the General Services Board of Contract Appeals indicates a lack of effective internal controls over ADP procurements. These deficiencies take on added significance in light of IRS' plans to procure billions of dollars worth of ADP equipment and services over the next few years in support of programs such as its Tax System Modernization. In carrying out these procurements, it is essential that IRS have internal controls to assure that procurement law, regulations, and practices designed to protect the government's interest and maximize competition will be followed. IRS recognizes the need to improve its procurement activities and is taking steps to address some of the problems we identified.

We recommend that the Commissioner require IRS' contracting officials to take immediate steps to bring its procurement of ADP services for the Electronic Filing System in line with proper procurement practices. Specifically, the IRS should determine, in accordance with the Competition in Contracting Act, whether it has adequate justification for a sole source award to Vanguard and whether the circumstances warrant the execution of a written contract with Vanguard. Any contract with Vanguard should be limited to work that is completed, or is soon to be completed,

