

IRS knew risk before refunds

New computer unable to flag taxpayer frauds

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USA Today

At least two months before the IRS mistakenly began paying an estimated \$200 million in fraudulent or erroneous 2006 tax refunds, the agency was warned about potentially

"catastrophic" problems in a new computer being developed to avert such a blunder.

A *USA Today* examination of the IRS Electronic Fraud Detection System project found the previously unpublicized November 2005 warning, along with other warnings and new details of missteps that culminated in one of the most costly and embarrassing episodes in the tax agency's recent history.

As the peak of the 2006 tax

season approached last spring, the IRS discovered that a planned upgrade of the agency computer that red-flags potentially fraudulent tax refunds had failed. The discovery came after the IRS had shut down the older computer. The failure forced the agency to continue processing 2006 tax returns, and issuing refunds, without its first line of electronic defense against fraud.

USA Today's review found that the IRS lacks a compre-

hensive plan to recover the \$200 million, which the agency said represents far less than 1 percent of all 2006 tax refunds. That means most fraudulent filers who got federal checks in 2006 will likely never be caught.

Today, as the 2007 tax season looms, the IRS is restarting



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the older computer, because the nearly \$21 million planned successor still isn't operable.

"I would say it is one of the more significant disappointments of my tenure," IRS Commissioner Mark Everson said in a recent interview. The blame, he said, "lies both within the IRS and at the contractor," because both "totally misjudged the complexity and the difficulty of this system."

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The IRS managed to identify and stop some fraudulent 2006 tax returns without the computer. But Senate Finance Committee Chairman Charles Grassley, R-Iowa, says the agency's failure to see beyond rosy projections on the computer project and act on the warnings had hurt millions of Americans.

'Going to get off'

"There's a lot of fraudulent tax returns that are filed ... and for at least last year, they're all going to get off scot-free," Grassley said. "And it's not just that they're getting off scot-free — it's that the honest taxpayers become the suckers."

The Electronic Fraud Detection System is the IRS' second-largest repository of taxpayer data.

Every tax return that claims a refund is run through the computer, which is designed to flag potentially suspicious claims for additional review under the agency's Questionable Refund Program.

The IRS decided to upgrade the 6-year-old computer in 2001 to keep pace with new refund fraud schemes and to enable investigators to use the system via the Internet.

Nine companies bid on the upgrade, the IRS said. DynCorp, a computer firm based in Reston, Va., won. In 2003, California-headquartered Com-

puter Sciences Corp. acquired DynCorp, and became the main contractor.

The IRS planned to switch to the upgraded computer in time for the 2005 tax season. But multiple problems arose, delaying the planned start-up to early 2006.

IRS officials said the agency's own personnel and CSC representatives repeatedly voiced confidence the new computer would start on schedule. During a Jan. 17 meeting at Everson's Washington office, IRS Deputy Commissioner John Dalrymple said, CSC projected a mid-February start date.

The timing was crucial, Dalrymple said, because the IRS had shut down the older computer months earlier. By autumn 2005, he said, it couldn't be restarted for 2006.

Missed deadline

But the promised February date came and went. By late March or early April, "it was clear to us that we were not going to be able to bring the Web-based system up at all," Dalrymple said.

Everson said he and other top IRS officials relied on repeated assurances in which the agency's managers on the computer project and CSC personnel said the new computer would be up and running as scheduled.

However, internal IRS documents obtained by *USA Today*,

including a \$400,000 post-failure assessment of the project, show the agency received multiple warnings about serious problems.

In a Nov. 10, 2005, memo, CSC personnel who worked on the project outlined "10 most critical EFDS (Electronic Fraud Detection System) risks" they said had to be resolved by the company and the IRS "before they become catastrophic." The problems included:

- "Extremely slow" communication between IRS computers and those used by CSC. The problems, chronic since June 21, made the communication so slow that at times, it's like using a "dial-up connection from home" that requires "2-3 minutes to do even the simplest of task, such as sending an e-mail."

Unless the problem was addressed, the memo warned, the IRS risked "putting the entire EFDS project in jeopardy."

- Repeated delays in setting up a large Oracle-manufactured computer network capable of handling massive volumes of data. Failure to rectify the problem by Dec. 9, 2005, the memo warned, raised the prospect that the new IRS computer "may not be ready to go into production" as scheduled.

- Computer servers that the contractor used for data conversion shut down frequently, halting work. The company wasn't alerted to a weekend

shutdown on Oct. 15, 2005, until two days later.

CSC has not been fined or sanctioned by the IRS, and continues to work on restarting the older Electronic Fraud Detection System. The firm declined to discuss specifics of either the warning memo or the project.

James Sheaffer, president of the firm's federal contracts sector, issued a statement that said: "We are contractually obligated to address any current or anticipated issues or problems that could, in our best judgment, interfere with our scheduled performance. That is exactly what we were doing in the '10 critical issues' document."

Dalrymple said the problems in the memo had all been addressed before top IRS officials learned the new computer would not start on time and did not "have anything to do with what the problem was with the root cause of the failure."

The key problem, which Dalrymple said was only determined during a March 2006, test, was that the new computer "couldn't load a full day's worth of data in one day. And when you can't do that ... you just fall further and further behind."

Yet, the IRS' post-failure assessment, obtained by *USA Today* under the Freedom of Information Act, found that some of the problems in the CSC warning memo "contributed to the delay" of the project.