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The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
State Capitol  
Sacramento, California 95814

Dear Governor and Legislative Leaders:

This letter report provides an update on recent events related to the Financial Information System for California (FI\$Cal) project. Pursuant to Government Code, Section 15849.22(f), the State Auditor's Office (state auditor) is required to independently monitor the FI\$Cal project throughout the development of the FI\$Cal system, as deemed appropriate by the state auditor. The independent monitoring shall include, but is not limited to, monitoring the contracts for independent project oversight (IPO) and independent verification and validation (IV&V) services, assessing whether concerns about the project raised by the IPO and IV&V contractors are addressed by the FI\$Cal steering committee and the FI\$Cal project office within the Department of Finance or its successor entity, and assessing whether the FI\$Cal project is progressing timely and within budget.

In our October 2009 status update, we communicated two concerns related to the FI\$Cal project and provided an update on a recent decision related to a change in the project's procurement approach. First, we reported that the Office of the State Chief Information Officer (OCIO) plans to provide the IPO services for the project. Specifically, in March 2009, the FI\$Cal project's steering committee gave its approval for the state's chief information officer (CIO) to be a voting member of the steering committee. In addition, the OCIO had informed us that it intends to have its own staff provide the IPO services rather than contract with an outside consultant. We are concerned that this arrangement—the OCIO providing the IPO services and the CIO being a voting member of the steering committee—might, either in fact or appearance, create a conflict that undermines the purpose of the IPO, which is to provide an independent, unbiased perspective. It is our understanding that, at the time of this report, the OCIO plans to continue with this arrangement and has hired an employee to perform the IPO services.

Second, we reported our concern that the project currently lacks long-term funding. The FI\$Cal project stated that, because of the State's economic situation and a law that prohibits the use of bonds to finance a budget deficit, it is unable to rely on the sale of bonds to fund the project as it initially planned. As a result, the project indicated that it was exploring various funding options, such as using special funds that receive revenue from sources other than the General Fund and federal funds or obtaining loans from vendors to finance vendor costs. Given the level of uncertainty surrounding its future funding, we communicated our concern that the FI\$Cal project may have difficulty attracting and retaining qualified staff. Finally, we provided an update on the steering committee's approval to select three bidders instead of two to perform the "fit-gap" analysis during the project's first stage of procuring a system integrator.<sup>1</sup>

<sup>1</sup> The purpose of the "fit-gap" analysis is to have the bidders develop detailed technical and cost proposals for the project, which would become the basis for software and system integrator bids.

The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
January 7, 2010  
Page 2

At this time, we believe it is appropriate to provide a brief summary of the events that have occurred since our October 2009 status update including the steering committee's approval of a third Special Project Report (SPR), the project's tentative selection of state entities for first wave implementation, and its selection of a contractor to perform some activities to prepare for the fit-gap analysis.

In November 2009 the steering committee approved its third SPR related to the FI\$Cal project. Unlike its previous SPR, which describes the project's activities over its 12-year implementation schedule, the current SPR focuses primarily on the project's two stages of procurement, which include the completion of the fit-gap analysis and the awarding of the software and system integrator contract in December 2011. The current SPR does not update the estimate of the project's total costs, which was reported at \$1.6 billion over 12 years in the second SPR. Instead, according to the third SPR, the project plans to re-estimate its overall costs and to address its long-term funding and financing plans in its next SPR. In particular, the FI\$Cal project indicated that it will complete a fourth SPR and, as required by a trailer bill to the Budget Act of 2009, submit a written report to the Legislature on its selection of the winning system integrator before it awards the contract. Thus, for purposes of this third SPR, the project is only estimating costs through December 31, 2011, or through the awarding of the system integrator contract. According to the third SPR's project funding plan, the project estimates it needs about \$72 million in total for fiscal year 2010–11 and through December 2011. However, the project also indicated in this SPR that it will address the source of this funding as part of the 2010–11 Governor's Budget, which was not yet available at the time of this report. Nevertheless, although the project is developing a plan to address its funding needs through December 2011, we continue to believe that the uncertainty surrounding the long-term funding of the project may hamper the project's ability to attract and retain qualified staff.

**State entities selected for first wave implementation:**

- Agricultural Labor Relations Board
- Board of Equalization
- California Arts Council (Summer School for the Arts)
- California Postsecondary Education Commission
- Department of Aging (Commission on Aging)
- Department of Alcoholic Beverage Control (Alcoholic Beverage Control Appeals Board)
- Department of Fair Employment and Housing
- Department of Justice
- Office of Environmental Health Hazard Assessment
- San Francisco Bay Conservation and Development Commission

Further, the project explains in the third SPR that, as part of the fit-gap analysis, each bidder will include a detailed implementation plan and all costs required to carry out the plan. According to the project, this step will limit the factors that result in cost overruns, such as bidders misunderstanding business and data conversion requirements. Additionally, the SPR describes the revised implementation approach that limits the first wave implementation, or "wave 1," to core accounting functions to avoid the risks and complexity of installing the full functionality of the software. Core accounting includes functions such as general ledger, accounts payable, and cash management. Further, the steering committee recently approved 10 state entities, proposed by the FI\$Cal project, as those where the core accounting functions will be implemented first. These state entities are shown in the textbox. According to the FI\$Cal project, it identified eight of these state entities as potential wave 1 entities based, in part,

The Governor of California  
President pro Tempore of the Senate  
Speaker of the Assembly  
January 7, 2010  
Page 3

on their level of complexity and willingness to accept change. The project also indicated that it proposed the Department of Justice and the Board of Equalization as wave 1 entities because of their failing accounting systems and willingness to participate. However, the project also emphasized that the entities it selected for wave 1 may change depending on the results of the fit-gap analysis developed by the three winning bidders.

Finally, to prepare for the fit-gap analysis, the project awarded a \$1.3 million contract to Cambria Solutions, Inc. in December 2009 for the purpose of documenting the current business processes and systems of 44 state entities, including four selected for wave 1. The FI\$Cal project indicated that it focused on selecting a minimum number of entities that its contractor could study, which accurately characterize the state's financial management processes as well as the information technology applications and systems that support these processes. According to the contract, materials from this engagement will be used to train the system integrators during the fit-gap phase of the project. The project anticipates its contractor will complete this work by September 2010, which is about the same time it expects to award the fit-gap contract to the three winning bidders.

We will continue to monitor and report on these topics in addition to others that come to our attention, at a minimum, before January 10 each year.

Respectfully submitted,



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