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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$Cal) project. Pursuant to Government Code, Section 15849.22(e), the California State Auditor (state auditor) is required to independently monitor the FI$Cal project throughout its development, as deemed appropriate by the state auditor. FI$Cal is a business transformation project for state government in the areas of budgeting, accounting, procurement, and cash management and it is based on a commercial-off-the-shelf software package with minimal modifications. The independent monitoring includes, but is not limited to, monitoring the contracts for independent project oversight (IPO) and independent verification and validation (IV&V) services, assessing whether concerns about the project raised by the IPO and IV&V contractors are appropriately addressed by the FI$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. We are required to report on the project's status at least annually and this is the eighth report we have issued since we began our monitoring in 2007, but our first report since the project began the design, development, and implementation (DDI) phase in June 2012. During the DDI phase, the project intends to deploy FI$Cal in five waves, with more departments and functionality added with each wave. The final wave of FI$Cal has a go-live date of July 2016.

In our last status update, dated April 26, 2012, we reported that the project completed its procurement phase by selecting Accenture plc as its systems integrator, with a five-year contract of $213 million. We also provided our review of selected information from the project's fourth Special Project Report (SPR), which it released on March 1, 2012, including the project's revised cost estimate of $616.8 million[1] and the project's proposed pay-as-you-go funding method. In addition, we summarized the project's projected benefits, its revised project schedule and implementation approach, and its envisioned risks and assumptions.

Since we issued our April 2012 report, the project was appropriated $89 million in the fiscal year 2012–13 budget and has reported spending $4.7 million of its appropriation through October 2012. The project asserts it will spend the majority of the remaining appropriation during fiscal year 2012–13. According to the project executive, the project will prepare a month-to-month spending plan for the remainder of the current fiscal year and thereafter, will put one together each fiscal year. The project indicates that spending is uneven during the fiscal year because the more significant payments to the system integrator have not yet occurred. Through October 2012 the project reported having spent $82 million in total since the FI$Cal project began. This letter report provides updates on our oversight activities,

[1] In the project's second SPR issued in November 2007, the cost of FI$Cal was estimated to be approximately $1.6 billion spread over 12 years.

the project's relatively inactive tracking of risks and issues since early 2012, its continuing challenges in recruiting and retaining staff, its schedule progress, and an update on the project's data conversion and change management activities.

State Auditor's Monitoring and Project Oversight Activities

As part of our monitoring activities during the DDI phase, we continue to attend monthly oversight meetings, quarterly steering committee meetings, and steering committee executive working group (working group) meetings. The working group meetings are intended to provide a place for the project executives to talk freely and openly about emerging project risks and problems before they are ready to be formally presented to the steering committee. According to the project director, beginning with the September 2012 meeting, the members of the working group decided to meet quarterly rather than monthly.[2] Further, the working group will meet on an as-needed basis between the quarterly meetings.

In our past updates, we communicated a concern about the California Technology Agency's (CTA) plan to provide the IPO services for the project even though the secretary of the CTA (technology secretary) serves as a voting member of the project's steering committee.[3] We were concerned that this arrangement—the CTA providing the IPO services and the technology secretary 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. In June 2012 the steering committee voted, at the CTA's suggestion, to remove the technology secretary as a voting member. We believe that this change will help assure that the project oversight is unbiased and independent. The CTA plans to continue to provide IPO services for the project, and chose not to transition the IPO role to a private contractor, as it previously planned. Currently, the CTA has dedicated one full-time staff person to provide IPO services. Given the size and scope of this project, we are uncertain if this staffing is sufficient and will monitor to ensure this level of oversight is appropriate.

There was a disruption in IV&V services during the initial stage of the project's DDI phase. Consequently, the project lacked a timely independent assessment of the system integrator's early work products during this time. As we pointed out in our October 2009 status update, the CTA took on the responsibility of contracting for a consultant to perform the IV&V services for the FI$Cal project and engaged Eclipse Solutions for this purpose. Although its contract with Eclipse Solutions was not scheduled to end until January 2013, between June 22, 2012 and August 7, 2012, the project had no IV&V services in place. This disruption in IV&V services occurred because the contract with Eclipse Solutions ran out of funds and there was a delay in procuring a contract for IV&V services during the project's DDI phase. In August 2012 the CTA amended the contract with Eclipse Solutions to add funds so that Eclipse Solutions could continue to provide IV&V services until the new procurement for IV&V services was completed, although the team consisted of the equivalent of two full-time positions, rather than the three IV&V staff under the original contract. The contract end date remained January 2013.

This disruption in services resulted in the IV&V consultant completing only one report over a 19-week period because not only was there a six-week lapse in IV&V services, but once Eclipse Solutions was reengaged on the project it was busy catching up on reviewing contract deliverables, which further delayed its reporting. While CTA and the project deserve credit for taking steps to minimize the effect

[2] The working group is composed of the steering committee members, including the project sponsor, designees representing the CTA, the State Controller's Office, the State Treasurer's Office, and the Department of General Services.

[3] Prior to 2011 the CTA was called the Office of the State Chief Information Officer and the technology secretary was called the State Chief Information Officer.

of the disruption, this lapse in IV&V services came at a critical time when the system integrator was developing and submitting its planning documents for the DDI phase to the project. As a result, the project lost an opportunity to benefit from a timely, independent assessment of early deliverables from the system integrator. Once it was reengaged, the IV&V consultant provided comments on the system integrator's deliverables that were in the project's review and acceptance process or had already completed the process.

In mid-November 2012 Eclipse Solutions fully resumed IV&V services under a new contract that calls for two full-time staff and a full-time project manager. In December 2012 Eclipse assigned one additional staff to its team at no cost to the State, as the contract allows, for a total of four staff. This level of staffing is a significant increase from the staffing level during the period between July and mid-November 2012, when the IV&V team had the equivalent of two full-time staff on the team. The IPO noted in its October 2012 report that, due to the fact that the new IV&V contract will be paid for by the project, there is the potential that the IV&V findings under the new contract could be more restrained. The IPO reported that it will monitor the quality of services provided under the new contract.

The Project's Tracking of Risks and Issues Has Been Relatively Inactive Since the Design, Development, and Implementation Phase Began

The IPO and IV&V consultant track and regularly report on the risks and issues relating to FI$Cal, as defined in the text box. However, the IV&V consultant reported in November 2012 that the project's process for reporting risks and issues has been relatively inactive since early 2012 with only two new risks being introduced into the process during the previous 250 days. The IV&V consultant recommended that the project revive the proactive risk management practices employed during the procurement phase and that it include the system integrator's staff during the project's periodic meetings to discuss risks and issues. Furthermore, in November 2011 the project reported to the working group five "high-priority" issues that were outstanding beyond 90 days, all of which were related to project staffing and data management. However, in the next steering committee meeting, in February 2012, the project reported that there were no high-priority issues outstanding. In response to our inquiry, the project indicated to us that it had previously addressed the five issues and incorporated any outstanding concerns into a new high-priority risk it is tracking. The project also indicated it provided a document describing mitigation activities related to these five issues to the steering committee, but was unable to provide the document to us. However, some of the mitigation activities the project identified as necessary to address these issues remained incomplete and were incorporated into the new high-priority risk. For example, the procurement of data management services was captured as a mitigation strategy for the new high-priority risk and remains incomplete as of December 2012. We will follow up with IPO regarding the project's risk tracking activities.

> **Definition of Risks and Issues**
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> Risks: Uncertain conditions or events that, should they occur, will negatively impact the project.
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> Issues: Unanswered questions and differences of opinion.
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> Source: California Technology Agency's *Project Management Methodology Reference Manual*.

In December 2012 the project opened a new risk recognizing that it was not identifying and managing risks and issues within its documented process, resulting in an increased potential for negative impacts later in the project. The project developed several action items to mitigate this risk and has completed two of them. However, if the project does not proactively identify risks and issues and report when and how it intends to address them, particularly high-priority matters, the project's stakeholders lose an opportunity to provide input on these risks and issues. In fact, CTA's guidance indicates that as projects resolve issues it is important to document and broadly communicate the resolution to appropriate stakeholders and team members to keep those affected by the resolution informed.

Although the Project Has Shown Some Improvement, It Continues to Experience Staffing Difficulties

Although the project has been funded for fiscal year 2012–13, we are still concerned that the FI$Cal project may have difficulty attracting and retaining qualified staff, as the vacancy rate for its full-time positions remains high. As of November 2012, the IPO reported that 49 of the project's 221 full-time authorized positions (22 percent) were vacant. These figures represent a modest improvement to those we previously reported for December 2011. At that time, 52 of the project's 161 full-time budgeted positions (32 percent) were vacant. In the last year, the project has received authorization for 60 new positions and has increased its overall staffing from 109 to 172, an increase of 63 staff. According to the November 2012 IPO report, operating at an approximate 75 percent staffing level cannot be sustained without affecting the schedule and quality of the project. The IPO recommended that the project continually monitor the hours that staff work, and if key staff are working excess hours on a sustained basis, the project should try to provide them with additional resources in an effort to avoid burnout and to retain them.

Additionally, both the IPO and the IV&V consultant have expressed concern over the project's ability to recruit individuals from the State Restriction of Appointments (SROA) list with the skills required. The SROA process is an alternative to layoff that allows the California Department of Human Resources (CalHR) to restrict state agencies' hiring so as to give employees in jeopardy of layoff an opportunity to retain state employment. If there is an SROA list for a given employment class, state agencies must determine if the individuals on the SROA list are either unqualified or not interested in the position before they may hire from another employment list to fill an open position. The project executive indicates this process is time consuming. Moreover, according to the November 2012 IPO report, the project is concerned that it may not be able to find candidates with the necessary skills on the SROA list. Although the IV&V consultant had previously recommended that the project request a blanket exemption from the SROA process, in July 2012 the CalHR rejected the project's request. According to the IPO, the project is continuing to actively recruit for positions. The project indicates that it needs individuals with unique skills and experience, such as knowledge of the enterprise software used by the system integrator, which makes recruiting qualified candidates more challenging.

Furthermore, the project has continued to experience turnover in key management positions. In October 2012 both the administration deputy director and the technology deputy director left the project. The project hired a new administration deputy director in mid-December 2012 and another state department has loaned the project a staff person to serve as the interim technology deputy director through January 2013. The IPO reported that a lack of strong, permanent leadership in these two key areas could affect overall project quality.

In contrast to the staffing difficulties that the project continues to face, as of November 2012 the IPO reported that the system integrator is staffed at over 150 percent of the planned level (about 68 full-time equivalent positions compared to a planned level of 45 positions). The IPO indicated that the system integrator decided to engage staff earlier in the project to work on critical tasks and to begin work on future planned tasks resulting in it staffing at a higher level than it originally planned.

Although the Project Is Generally Meeting Near Term Milestones, Its Overall Progress Is Difficult to Assess Until a Long-Term Schedule Is in Place

In November 2012 the project approved the system integrator's proposed long-term schedule. The project schedule illustrates the timing of the various tasks needed to complete FI$Cal. The project and the system integrator will use the schedule to monitor the progress of tasks and to report on the overall status in completing FI$Cal. Since the project began the DDI phase it has operated with an interim schedule, which identified short-term tasks that the project needed to focus on between July 2012 and December 2012. According to the IPO, the project has completed and approved all major tasks and milestones in accordance with the interim schedule. However, the IPO noted that the interim schedule has not provided the project with the level of schedule performance monitoring and reporting that the long-term schedule is expected to provide.

Because the CTA considers FI$Cal to be a high criticality project, it requires the project to report progress on a monthly basis. Under the interim schedule, the project has been reporting its progress to CTA on various tasks. In addition, the project has reported overall progress based on how much it has spent compared to the overall budget reported in its fourth SPR rather than the work completed during the DDI phase. The total amount spent includes the project's costs during the procurement phase. Based on this methodology, the project has been reporting that it is roughly 18 percent complete based on its total expenditures to date as a percentage of the project's estimated one-time development costs. However, the project's expenditures are not necessarily reflective of the project's progress or the amount of work it has completed. For example, although certain activities such as project management and oversight services, as well as hardware and software purchases, are necessary for the project, expenditures in these areas are not reflective of the project's progress in completing tasks that directly result in the implementation of FI$Cal. According to the project director, the project will be able to more precisely report on its progress during the DDI phase starting in January 2013 when it has the long-term project schedule in place. At that time, the project director stated that the project will be able to report the percentage of completion based on actual deliverables that the system integrator has completed and the project's progress using baseline completion dates compared to actual completion dates. However, until this process is in place, the extent of the FI$Cal project's progress towards completion is based on a measure that may not be a best indicator of progress.

Data Management Issues Remain Unresolved While It Is Too Early to Assess the Effectiveness of the Project's Change Management Efforts at This Time

The project continues to work toward completing two critical activities—data management and organizational change management. As we reported in January 2012, data management is a significant component of the FI$Cal project, but has suffered as a result of staffing constraints. Data management encompasses creating an inventory of data to be converted, preparing the data for conversion, and then converting the data to the new FI$Cal system. Since then, the project has made some progress, but it remains a risk area. The IPO reported that in April 2012 the project completed its legacy systems inventory, which identified and documented electronic and manual business systems that state departments currently use and are expected to transition to FI$Cal. According to the November 2012 IPO report, the project estimates that statewide 2,200 legacy applications need to be converted to FI$Cal and the project will need to ensure that an additional 3,400 interfaces are able to exchange data with FI$Cal. In March 2012 the project initiated the legacy systems and data analysis subproject. Among others, the objectives of this critical subproject are to validate the information gathered by the legacy systems inventory, identify requirements for cleaning up data that is incorrect or incomplete, and assist

Departments Implementing FI$Cal During the Pre-Wave and Wave 1

Pre-Wave* (July 2013)

- Agricultural Labor Relations Board
- Office of Environmental Health Hazard Assessment
- Department of Aging (including Commission on Aging)
- California Arts Council
- Department of Fair Employment & Housing

Wave 1† (July 2014)

- Alcoholic Beverage Control Appeals Board
- California Alternative Energy & Advanced Transportation Financing Authority
- California Citizens Compensation Commission
- California Debt and Investment Advisory Commission
- California Debt Limit Allocation Committee
- California Educational Facilities Authority
- California Health Facilities Financing
- California Industrial Development Financing Advisory Commission
- California Pollution Control Financing Authority
- California Postsecondary Education Commission
- California School Finance Authority
- California State Summer School for the Arts
- California Tax Credit Allocation Committee
- California Urban Waterfront Area Restoration Financing Authority
- Department of Alcoholic Beverage Control
- Department of Justice
- Department of General Services–Contracted Fiscal Services
- Fair Employment and Housing Commission
- San Francisco Bay Conservation and Development Commission
- Scholarshare Investment Board
- State Board of Equalization
- State Controller's Office
- State Treasurer's Office
- Department of Finance

Sources: FI$Cal's fourth Special Project Report, the October 2012 Independent Project Oversight report, and a July 2012 FI$Cal Forum presentation.

* Pre-Wave implements requisition and purchase order functionality, including the vendor master file, for the five Pre-Wave departments, establishes a statewide chart of accounts and budget structure, and reengineers business processes.

† Wave 1 implements FI$Cal as the primary departmental accounting, procurement, and budgeting system for the Pre-Wave and Wave 1 departments, and FI$Cal becomes the system of record for budget data for the Department of Finance.

departments with data clean-up activities. Due to the complexity and effort required for data conversion, the IPO has recommended the project bring in data conversion experts with a proven track record to assist the data conversion efforts. As we reported in January 2012, the project cancelled the procurement for a data management contractor in June 2011 because it considered the bids to be inadequate and by November 2011 it had drafted a request for offers for a new procurement. However, the IPO reported in November 2012 the procurement for these services has been delayed, which may affect the project's effort to complete data conversion and system interfaces.

Similarly, the project's organizational change management effort is also a critical activity. As we reported in January 2012, the IV&V consultant cautioned that organizational change management challenges that departments face might prove to be FI$Cal's largest impediment to success. The project's change management office is responsible for preparing each department for the changes necessary to successfully integrate with FI$Cal and to develop an infrastructure that facilitates ongoing communications and activities between FI$Cal and State departments. The IPO reported that the project hired a change management contractor in March 2012. The project has begun performing readiness assessments, with the assistance of the change management contractor, and is conducting sessions focused on reengineering business processes with Pre-Wave and Wave 1 departments. The text box shows the departments and the FI$Cal functionality that will be implemented in these two waves. The readiness assessments are to determine whether department staff are aware of FI$Cal, understand its impact, and are committed to implementing it when the Pre-Wave departments go live in July 2013. Further, the assessments will be used to help the project determine the activities needed to bring those departments up to full readiness before they go live with FI$Cal. The project director indicates that the results of these readiness assessments for the Pre-Wave departments are due in mid-December 2012 and will be subject to the project's established review process before being accepted. Both the IPO and IV&V consultant plan to continue to monitor the project's progress on its activities for data management and change management.

Status of Legislative Recommendations From the April 2012 Report

In our April 2012 report we made three recommendations for the Legislature to consider related to tracking of costs for state department subject matter expert staff, monitoring the projected benefits of FI$Cal, and reporting the cost and reasons for any significant and unanticipated customizations that the project makes to the FI$Cal software. The text box lists these recommendations. We are unaware of any legislative action to address our recommendations; however, we believe these recommendations are still valid.

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,

Elaine M. Howle

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State Auditor

Recommendations for the Legislature to Consider if It Decides to Approve Funding for the FI$Cal Project

- To ensure that the cost to implement FI$Cal accurately reflects the effort needed, the Legislature should require the project to track the cost of department subject matter expert staff and include this cost in the total cost for FI$Cal.
- To monitor the benefits that FI$Cal is projected to provide based on the Hackett study, the Legislature should require the project to track projected benefits and to report annually on the total benefits achieved, any changes in total projected benefits, and actual project benefits as compared to actual and projected FI$Cal costs.
- The Legislature should require the project to report annually on the cost and reasons for any significant customizations it makes to the software that were not anticipated at the onset of FI$Cal implementation.

Source: State Auditor's report 2012-039, April 2012.