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June 16, 2005

MEMORANDUM

TO: Representative Henry "Kiki" Saavedra, Chair
and members of the Audit, Computers and Capital Outlay Subcommittee

FROM: Aurora B. Sánchez, IT Performance Auditor
Legislative Finance Committee

SUBJECT: Audit of Unemployment Insurance (UI) Claims Computer System

EXECUTIVE SUMMARY

In March 2005, the Legislative Finance Committee (LFC) audit staff was asked to audit the Labor Department's (Department) UI Claims Project. The purpose of this particular audit is to determine the progress of this project since March 2004 toward full implementation of an integrated system. It was not intended to duplicate work already done. However, to ensure that past problems do not continue to plague this project, it was necessary to review the history, identify what went wrong and compare it to current practices. Understanding what transpired between May 2001 and March 2004 can provide the Department with valuable lessons that it can apply so that it can successfully complete and deploy into production the integrated UI Claims System.

The objectives of this audit were to determine:

- If the Department employed and is employing the best practices in the development of the UI Claims System;
- The current status of the "FIX" project, including on schedule and within budget;
- If the UI Claims System was received within the time allotted and within the budget allowed;
- If the UI Claims System assists in meeting the Department's strategic business objectives and information technology (IT) goals;
- If Department technical staff received or will receive appropriate training in applicable technology and sufficient knowledge transfer to maintain and support the UI Claims System
- If users have been sufficiently trained or if there are plans to train users; and
- If the Department ensured the UI Claims System has sufficient security to safeguard employer and employee data.

Department Summary Response. One aspect of the New Mexico Department of Labor (NMDOL) mission is to promote economic development and education by matching the needs of employers with the skills of the job seekers. However, when the clients are unemployed, the goal is to provide temporary benefits.

The NMDOL Unemployment Insurance Claims (UI) Reengineered system was designed to automate the processes used by the department to provide unemployment insurance benefits to the citizens of New Mexico. The processes consist of processing unemployment insurance claims, adjudication of cases, payments of benefits and other related functions. To achieve this goal the department put in place an aggressive project plan with anticipated results of a new UI claims application that is:

- available 24 X 7 utilizing state-of-the-art technology
- integrated with call center for taking client calls
- integrated with web capabilities giving clients access via the Internet

The NMDOL is committed to ensuring the UI claims system meets implementation expectations in order to provide required services to its clients. The legacy system currently carries the major burden for this program. However, the department is working diligently to bring the new system into full production. The project staff has developed a controlled, effective and standard process for monitoring progress. More importantly, the department is now controlling the project.

The New Mexico Department of Labor is pleased to respond to the Legislative Finance Committee (LFC) review of the unemployment insurance claims computer system. The department does not completely disagree in principal with LFC's Audit Finding. The department previously identified many of the issues raised in the LFC Findings and has taken proactive steps to rectify. The following responses will help explain some of the past issues and more specifically, will address how the department is working to proceed positively and expeditiously to bring the system into full production.

Problem Definition. The NMDOL UI Claims System project was placed on hold on in May, 2004, and has not proceeded to full system test and cutover due to the following:

1) Only 20% (Phase I) of the UI Claims system is in production. The remaining 80% (Phase II) of the system is still in test/development and not fully operational due to outstanding defects.
2) The NMDOL IT staff was not adequately trained and knowledgeable to operate and maintain the upgraded UI Claims System.

UI Claims "FIX" Project. NMDOL proposed the UI Claims FIX Project to address and complete the UI Reengineering Project to department requirements and to address deficiencies of the previous halted implementation. The scope of the UI Claims FIX Project is to:

- Complete system testing and implement to original requirements with assistance from external resources
- Complete the Reengineered UI Claims System to production and fully integrate with IVR

No Current Contract for Development Services and Knowledge Transfer. Currently, there is no development contract in place to put into production an estimated 80 percent of the functionality that is not fully tested and provide much needed knowledge transfer even though the Department has been in negotiations for several months. Without the contract, it is doubtful that the UI Claim System can be implemented by the October 2005 deadline.

Recommendation. Sign the new contract to complete the estimated 80 percent missing functionality as soon as possible. Fully define deliverables before entering into any contract. Ensure the term of the contract is sufficiently long to complete the functionality, fully test the completed and integrated system, train technical and user staff and successfully move the system into production.

Establish a baseline for what the system to be delivered should contain and closely monitor changes to that baseline. Functionality based on legislative changes or receipt of federal grants should not be the basis for adding to the scope of work, extending time or increasing compensation. Once the core system is in production, other functionality can be added based on legislative changes or federal grant requirements.

Institute a process for accepting changes that will substantially alter the cost of and time to deliver the system. Document modifications or enhancements based on legislative changes or new grant requirements so that those can be addressed immediately after the core system is successfully and fully in production.

Accept deliverables only if complete and functioning as intended and deliverables should never accept "conditionally". Base the time to begin the warranty period on full implementation of the system not on receipt of particular deliverables. Never reduce the percentage of the retainage. If there are delays in entering into a contract with the developer, the Department should use the time to fill vacant technical positions, address any data migration issues and provide technical training on new technologies.

Department Response. On October 29, 2004, NMDOL Secretary Conroy Chino and TCS-America Vice –President Dr. Shyam Johari, signed a letter of agreement. The agreement included TCS' agreement to perform seven functions for compensation not to exceed $300,000. The described functions represent full implementation of the UI re-engineering system, including training and knowledge transfer to NMDOL employees, and a new warranty period.

NMDOL has aggressively negotiated with TCS-America and on Thursday, June 9, 2005 presented a signed contract to TCS Vice-President Dr. Shyam Johari for his signature. The submitted contract includes the following attachments:

1. Letter of Agreement
2. Service Level Agreement
3. Project Schedule
4. Deliverables and Acceptance Matrix

dedicate one full-time IT staff person to the SHARE project (replacement of the statewide accounting, human resource and procurement system), thus requiring an already burdened IT staff to assume additional duties.

Recommendation. Advertise and fill the current technical vacancies quickly with staff proficient in the technology being used for the UI Claims System. If the positions prove difficult to fill, consider contractors with an option to hire if the individual turns out to be a good fit.

Consider extending the deadline for implementation to no earlier than December 2005. If the positions cannot be filled or a contract for technical services cannot be signed in a timely manner, require the project manager to reanalyze the project taking into consideration all known constraints to determine if a date later than December 2005 is not more realistic to achieve project success.

Department Response. NMDOL agrees that the project is currently understaffed, the extent of which is difficult to determine. A hiring freeze was put into place by the state Chief Information Office. Six vacancies were not filled immediately when the hiring freeze was removed, however other state IT initiatives caused delays with hiring – such as the committee approval process required for IT staff and the State Personnel Office information requirement to distinguish between infrastructure vs. non-infrastructure positions.
The department has posted the jobs and interviewed several candidates to fill positions. One has been hired and two others identified. In addition, the department has contracted for the services of an expert programmer who is a RUP/Rational configuration management specialist.

Insufficient Technical Training on New Technologies. Technical staff must be knowledgeable about the technologies used for the UI Claims System so that they can provide accurate, complete and timely support after the system is in production. During development, technical staff must be knowledgeable about the technologies so that they can assist with and oversee the building of the system.

Approximately 18 percent of technical courses required to fully support the UI Claims System have been completed. The technology services division has formulated a training plan for the UI Claims "FIX" project, but not all staff that will work on the development and continued support have received the training necessary to enable them to maintain and support the system when it goes into production because the Department did not have sufficient funds to allocate toward all its training needed. In FY05, the Department spent approximately $198.0 to train eleven of its technical employees. As of June 2005, technical staff has not received training in Rational, the development tool used on this project.

If the Department cannot provide the training necessary, it will have to completely rely on contractors to develop and support this mission critical system.

Recommendation. Set aside FY06 funds to provide at least the necessary basic training for technical development and support staff. Request training quotes from training service providers and from IBM, possibly using the Education Pack, and determine, based on dollars available,

- Recommendation, including the date the recommendation needs to be implemented.

Issues or items to report on include, but are not limited to: the status of contract negotiations, budget and expenditure information, hiring and training of technical staff to provide project and ongoing support, changes to the UI Program, reporting requirements to external entities, expectations by the Department, USDOL, the OCIO, etc.

For example, if the Department cannot fill technical positions, executive management should not simply be informed that the project will be delayed. It should also be informed why the hiring was delayed, the length of the delay, impact to the final implementation date, corrective action options, recommendation and date executive management should take action.

Department Response. NMDOL will follow the recommendations of the LFC of providing weekly project status reports to executive management that contain complete status information from all responsible parties about all aspects of the project, including contracting, budget and expenditures, staffing, training, and testing. NMDOL has improved its format for reporting and addressing risks. This improved format provides additional information for each risk, its impact, and target dates for mitigating or resolving. This Risk Tracking and Status Report will be updated weekly and provided to Executive Management with weekly Project Status reports.

No Executive Steering Committee. A project executive steering committee is the key body within the governance structure which is responsible for the business issues associated with the project that are essential to the outputs and the attainment of project outcomes. This includes approving the budgetary strategy, defining and realizing benefits, monitoring risks, quality and timelines, making policy and resource allocation decisions, and assessing requests for changes to the scope of the project. Successful projects require executive level involvement so that the business vision is articulated and the project is managed toward attaining that vision.

Although the project manager is not part of the steering committee, the steering committee does empower the project manager to undertake the project. It is also the committee's responsibility to ensure that the project manager receives all the assistance and resources required from the various business units in order to successfully deliver the project as mandated.

Although the project manager and the deputy CIO do meet with the Secretary and other Department management, the Department has not formed a formal steering committee to provide the needed governance structure to the UI Claims Project.

Recommendation. Establish a formal executive steering committee consisting of the Secretary, Deputy Secretary for Programs, ASD Director, CIO, and the UI Director. It can also include one or two individuals from outside of the agency.

Ensure the executive steering committee receives the project status reports before regularly scheduled meetings so that each member has a chance to review the items or issues presented. The members can then decide which resolution or mitigation option will work best for the project and the Department if the project manager has escalated the decision to the executive steering committee.

be included in the written reports. The validated spreadsheet can also be used to report current and consistent financial data to the OCIO each month.

Ensure that the accounting system selected for the SHARE project will have the capability of tracking project budget and expenditures to provide accurate and timely information to the Department's management and oversight authorities.

Department Response. The NMDOL agrees with this finding. The department's financial system was the legacy system called FARS. The Department budget analyst, in April 2004, recommended setting up specific fund ledgers and one cost center to track project budget and expenditures because the project was difficult to track. However, shortly thereafter, in July 2004, the Department was required to transfer to the state's Central Accounting System and continues to account for its finances on both systems. Both the FARS and Central Accounting System are legacy mainframe systems with limited ability for financial reporting. This inadequacy is one reason why the Department is implementing the SHARE system. The SHARE project is the statewide initiative to replace the Central Accounting System with a modern human resources, accounting and reporting system. The SHARE system's functionality is vastly superior to the legacy systems.

In the FARS system, cost centers are defined as organizational units and expenditures are accounted by "fund ledgers". The Department set up specific fund ledgers in each division to capture project costs in the FARS system as well as the Central Accounting System as recommended by the budget analyst. Neither the FARS nor the Central Accounting System contains the ability to automatically track the project as a "cost center". The Department will continue to rely on Excel spreadsheets to track past and current project costs until the SHARE project is implemented. The time expended by the budget analyst was required to have a detailed reconciliation of all costs to include all staff charges as well as vendor payments and other non-personal services costs.

During the 2005 legislative session, the Department requested and was appropriated $3.5M towards the SHARE system with the intent of developing the Projects and Grants modules of the PeopleSoft software to enable the Department to track the grants and projects at the level of detail required.

The total UI Claims Project obligations from April 1, 2004 to April 30, 2005 are $1,224,794. Projected expenditures for FY06 are $750,000. The Project has sufficient revenue to pay for current expenditures and to completion. The worksheet reflecting the obligations and projected expenditures from April 1, 2004 through April 30, 2005 were provided to the LFC auditor on June 13, 2005.

A Budget Analyst from the Budget Bureau of the Administrative Services Division has been assigned as a formal member of the UI Claims FIX Project Team. The analyst will provide monthly financial status reports to the Executive Steering committee and Tomas Rodriguez, Project Sponsor, for inclusion with the UI Claims FIX Project status reports. The reports will contain appropriated Budget and Expenditures (actual and projected) by category and line item

professional project management services for Advanced Planning via a pricing agreement

- The project did not start in January 2005 as planned due to three delays: 1)Version issue, 2) Data Migration Error Correction, and 3) No signed contract with TCS.

NMDOL identified additional funding and amended the project management professional services contract in the interests of continuity.

NMDOL has engaged an IV&V contractor for $80,000. The contract will not be amended. NMDOL identified $80,000 it had available for IV&V Services. NMDOL sought informal bids from Northrup Grumman, Kemtah, RESPEC, POD, Inc. NMDOL did receive proposals for extensive and comprehensive IV&V at a cost beyond the budget NMDOL had available. NMDOL reached an agreement with Northrup Grumman for IV&V services with a scope, term and cost that is within the $80,000 amount that NMDOL has available. NMDOL has no plans to amend this services agreement.

In the Spring of 2001, the Department signed a contract for "the full development, testing and implementation" of the replacement system with a completion date of December 31, 2001. The Department reported it received $7.2 million in federal funds to re-engineer, develop, test and implement the UI Claims System and would be requesting another $1.6 million (which it subsequently received), and would have to be spent by December 31, 2001, which was the end of the grant period.

Two months after the contract with the developer had been signed it was amended. Over the span of 24 months the contract was amended twelve times to extend the time to implement the fully integrated system, increase the compensation to the contractor, or change the scope of work. The numerous contract amendments to the firm fixed price contract of $3.6 million entered into in May 2001 to develop the UI Claims system resulted in:

- Total increases of $6.3 million, which represents 71 percent of the total project increases;
- Erosion of protective clauses, such as reduction of the retainage percentage from 10 percent to 5 percent;
- Accepting deliverables even though contract milestones had not been met;
- Changing system acceptance from full to conditional;
- Delivery of an estimated 20 percent of a production-ready system instead of a complete and fully integrated system;
- Extension of time two and one-half years beyond the initial implementation date;
- Changes in scope of work based on legislative changes or new grant requirements that were beyond the scope of the request for proposal; and
- Adding time and materials option to a firm fixed price contract.

In late 2003, the Department accepted the system and paid all but $425.0 to the development contractor based on the previous project team's recommendation none of whom are currently on the project. After further review of the system by the "FIX" project team, it discovered that even though all but $425.0 had been paid to the contractor, eighty percent of the required processes, which are shown in the table below, were incomplete.

developed. It is unclear what the USDOL representative was reviewing or what representations were made to cause him to issue such a report when the system was over budget, behind schedule and incomplete.

The Department's management relied on positive reports from Department project staff and from the USDOL to either continue the project or to make payments to the development contractor even though it had not received a complete production-ready system.

Project status reports were not accurate in that project deadlines were continually extended making it appear as though the project was on schedule. The development contractor's compensation was continuously increased and revenue available for the project was increased based on additional federal grants received or transfers from other federal sources making it appear that the project was within budget. However project milestones related to the delivery of code or data migration were not met.

Although the individual assigned as project manager did have extensive knowledge about the UI Program, he did not have project management skills. "Project managers must be competent in the five process groups (initiating, planning, executing, controlling and closing) and in nine knowledge areas (project integration management, project scope management, project time management, project cost management, project quality management, project human resource management, project communications management, project risk management and project procurement management)." Additionally, project managers should be dedicated to the project and not juggling other duties.

Finally in March 2004, with only an estimated 20 percent of the UI Claims System in production and nearly 100 percent of the payments made to the contractor, the Department halted the project in an attempt to determine the status of the project and identify strategies toward successful completion. By March 2004, the project was grossly over budget and several years behind schedule. In September 2004, the Department reported to the IT Commission that:

- the IT Staff was never trained in new technology,
- there had been no knowledge transfer from the vendor,
- the Department had an insufficient number of FTE to support the system,
- the warranty had expired, and
- the Department had only 20 percent of the system in production.

The Department CIO attributed the project's troubles to: lack of dedicated project management, unclear deliverables, no control over statement of work, no communication or risk assessment plans, no change control process and no consistent use of acceptance testing and modeling tools.

The Department requested three independent reviews of the UI Claims Project.

- disposition of the team; and
- sponsor's commitment and time.

Using the implementation date in the original contract, December 31, 2001, and the reported federal appropriations received, $8.8 million, as a baseline, this project is approximately $8.9 million over budget and three and one-half years behind schedule.

The Department is currently attempting to get the project back on track so that it can finally receive a fully complete and integrated system.

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