Secretary of State

State of Oregon

DEPARTMENT OF ADMINISTRATIVE SERVICES
Information Resources Management Division Review

Audits Division

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OFFICE OF THE
SECRETARY OF STATE

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Secretary of State

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Auditing for a Better Oregon

The Honorable John Kitzhaber, M.D.
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This report includes our evaluation of selected activities of the Department of Administrative Services, Information Resources Management Division. During the audit, we evaluated the agency's processes for providing enterprise-wide policies and procedures governing information technology, controls over its system development projects, and processes for establishing customer rates to recover the costs of providing services.

The department has not provided adequate guidance and direction to other state agencies to govern the state's information technology resources. Similarly, the division did not have adequate controls to manage its own system development projects. Finally, the division's processes for charging its customers should be improved. The report includes recommendations to improve the division's management of these issues.

The Department of Administrative Services generally agrees with our recommendations.

OREGON AUDITS DIVISION

John N. Lattimer
Director

Fieldwork Completion Date:
April 26, 2001

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SUMMARY

AUDIT PURPOSE

In September 2000, the Audits Division concluded a risk assessment of the Department of Administrative Services' (department) Information Resources Management Division (division). The purpose of this audit was to provide additional insight regarding some of the most important issues that we identified during that assessment. The audit had the following three objectives:

- Determine whether the department has established adequate direction to govern the state's information technology resources.
- Determine whether the division has sufficient policies and procedures to manage its information system development.
- Determine whether the division's business processes provide a reasonable basis for charging its customers.

BACKGROUND AND INTRODUCTION

The Governor and Legislature directed the department to play a pivotal role in shaping Oregon State government's use of information technology. The department's director relies on the Information Resources Management Division and its Chief Information Officer to lead those efforts. Oregon Revised Statute (ORS) 291.038 directs the department to develop and adopt statewide policies, procedures, standards, and guidelines to govern the state's information technology resources. Additionally, the Governor directed the department to develop a statewide strategic plan for information technology.

The division provides centralized computer services for most state agencies including maintenance of some of the state's largest computer systems.

AUDIT RESULTS

The department has not provided adequate guidance and direction to other state agencies to govern the state's information technology resources. Consequently, state agencies are less likely to act as part of an enterprise or provide the necessary level of control to safeguard other members of the enterprise. In addition, the division did not have adequate controls to manage its own system development projects. Finally, the division's processes for charging its customers should be improved.

The department should work to implement the following priority items to resolve the above issues:

- Improve its methodology for developing an enterprise-wide strategic plan, and then develop a strategic plan according to the Governor's Executive Order 98-05.
- Utilize the Information Resources Management Council as directed by ORS 291.038.
- Develop and adopt enterprise-wide policies, procedures, standards, and guidelines to plan for, acquire, implement, and manage the state's information resources.
- Develop and adopt a comprehensive agency-wide System Development Life Cycle (SDLC) methodology to govern all aspects and phases of the system development life cycle.
- Adopt as part of its SDLC, a project management framework to ensure all projects are effectively managed.
- Seek to recover contract overpayments and consult with the Attorney General regarding its legal options, obligations, and remedies for contracts that may have been adversely affected by the division's use of year 2000 exemptions.
- Improve its rate setting model to ensure that customer charges are equitable.

AGENCY'S RESPONSE IN BRIEF

The Department of Administrative Services generally agrees with our recommendations.

INTRODUCTION

The Department of Administrative Services (department) is the central administrative agency of state government. The department works in partnership with the Governor; the Legislative Assembly and state agencies to put programs, policies, and systems in place and provide centralized services.

In Oregon Revised Statute (ORS) 291.038 the legislature directs the department to play a pivotal role in shaping the way that Oregon state government uses information technology. The statute requires the department to ensure that resources fit together in a statewide system capable of providing ready access to information, computing and telecommunication resources. It further directs the department to develop and adopt statewide rules, policies, procedures, standards, and guidelines so that state agencies will plan, acquire, implement and manage the state's information resources.

The department's director relies on the Information Resources Management Division (division) to provide centralized information technology support and services. The division's administrator is the state's Chief Information Officer. The division's responsibilities include:

- developing and implementing statewide information technology standards and protocols;
- managing the state's voice, video and data networks;
- operating the General Government Data Center;
- planning, developing and managing enterprise databases and applications;
- reviewing agency technology activities and plans;
- providing system development consulting and programming services to state agencies; and
- delivering technical training to state agencies and organizations.

SCOPE AND METHODOLOGY

In September 2000, the Audits Division concluded a preliminary risk assessment of the Information Resources Management Division's operations. The purpose of this audit was to provide additional insight regarding the most important of those issues that we identified during the risk assessment. The first objective of this audit was to determine whether the department provides adequate guidance and direction to other state agencies to govern the state's information technology resources. The second was to determine whether the division has sufficient policies and procedures to manage information system development. Our third objective was to determine whether the division's business processes provided a reasonable basis for cost allocation and recovery.

Our audit work included inquires of department and contract personnel, examination of documents, and the review of accounting records. Specifically, we examined the department's statewide policies and procedures, the State of Oregon Enterprise Information Technology Strategy, one of the division's system development projects, and the division's rate setting processes. We also evaluated the division's compliance with applicable laws, rules, and regulations pertaining to our audit objectives. We performed our fieldwork between October 2000, and April 2001.

We used the Information Systems Audit and Control Foundation’s Control Objectives for Information and Related Technology (COBIT™) to identify generally accepted and applicable control objectives and practices for information systems. We conducted our audit according to generally accepted government auditing standards.

AUDIT RESULTS

CHAPTER 1: STATEWIDE GOVERNANCE OF INFORMATION TECHNOLOGY

The Department of Administrative Services (department) is responsible for establishing and adopting statewide policies and procedures to assure a framework for the review, improvement, integration, development, security and use of information technology (IT) resources. Although the department is not directly responsible for managing other agencies' resources, it is responsible for ensuring that those resources are appropriately managed and controlled.

Enterprise level oversight of IT resources is essential because of the state's increasing dependence on technology as well as the increasing risk of threats to IT assets. Additionally, the complexity and cost of information technology investments punctuate the need for statewide control, coordination, and integration of IT resources.

One of our audit objectives was to determine whether the department provides adequate guidance and direction to other state agencies to govern the state's information technology resources. To achieve this objective, we evaluated the department's statewide policies and procedures as well as the State of Oregon Enterprise Information Technology Strategy.

AUDIT CONCLUSIONS

The department has not provided adequate guidance and direction to other state agencies to govern the state's information technology resources, including a cohesive framework of strategies, policies, and procedures. Consequently, state agencies are less likely to act as an enterprise or provide the necessary level of control to safeguard other members of the enterprise.

The findings identified in Chapter 2 of this report characterize some of the problems that may occur when agencies do not have policies and procedures to govern system development. The results of several of our other information technology audits likewise identified problems relating to system development as well as security. Those findings also ultimately stemmed from inadequate statewide guidance and monitoring.

ENTERPRISE STRATEGIC PLANNING

Effective strategic plans define both long-range and short-term objectives and specify who, what, when, and how those objectives will be accomplished. Strategic plans should also be congruent with the organization's overall vision, mission, and business needs. Furthermore, they should be "living" documents, regularly reviewed and adjusted to fit changes that may have occurred.

In March 1998, Governor Kitzhaber formally assigned the department the responsibility to develop a statewide information technology strategic plan. Executive Order 98-05 required the department, in collaboration with other state agencies and the Information Resources Management Council, to formulate an enterprise strategic plan as follows:

Exhibit I

Executive Order 98-05 – Requirements

A vision of Oregon's future information technology. The vision shall include a migration path and schedule for any required major improvements and changes.

Major capital improvement investments required to implement the plan.

Duties which state agencies and related public organizations must perform in order to implement the plan.

Directions for the use of information resources throughout state government.

Policies, strategies, goals, and objectives relating to the methods by which the state shall plan, acquire, secure, manage, and utilize its information resources.

A design for an advanced digital communications, computing and telecommunications network. The design shall reflect and adequately meet the needs of state agencies.

Methods by which to share state personnel, financing, buildings, and equipment necessary to plan, collect, process, transmit, and store information.

Legislative concepts necessary to implement the Plan.

A cohesive manner in which the elements of the Plan will operate within the statewide information system which provides ready access to information, computing, and telecommunications resources.

Although the executive order constituted an excellent framework for developing an enterprise strategic plan, the department did not address most of these elements in its October 1998, State of Oregon Enterprise Information Technology Strategy (plan). Significant weakness in the plan include the following:

- The plan does not adequately address some of the items required by the governor's executive order. Some critical areas such as the state's strategy and policy for securing its systems were entirely omitted.

- The plan's definition of the "enterprise" is too broad. It defined the enterprise as all state and local governments, educational entities, libraries, "other information partners," and "communities of interest serving a public interest mission." Thus, the plan covered many entities over which state government exercises little or no direct control.

- The plan did not clearly indicate what actions state agencies should take to accomplish the initiatives, principles, practices, or vision.

- The department has not subsequently updated the plan. As of April 2001, the department had no formal policy or procedure to regularly update the plan.

The department did not effectively manage the strategic planning process. Rather, it delegated the responsibility to the Information Resources Management Council (IRMC). Because Oregon state government is highly decentralized, the department, IRMC and other committees had difficulty establishing consensus regarding key strategic planning issues. Consequently, the state does not have a viable enterprise-wide information technology strategic plan for agencies to base their own plans. Therefore, state agencies are less likely to consider enterprise solutions or consider the needs of other agencies.

Furthermore, as of April 2001, the Department of Administrative Services was not using the Information Resources Management Council to provide policy direction for and coordination of information technology for state government as required by ORS 291.038.

We recommend that the department develop a strategic plan as defined in the Governor's Executive Order 98-05. Additionally, the department should develop more effective strategic planning methodologies. Those methodologies should specifically address how to establish consensus within the state's decentralized organizational structure. Alternatively, the department could exercise affirmative control over the strategic planning process.

We also recommend that the department utilize the IRMC as directed by ORS 291.038. Alternatively, the department may ask the legislature to modify or remove the requirement.

STATEWIDE IT POLICIES AND PROCEDURES

As defined in statute, the department is responsible for statewide governance of information technology. The legislature indicated in Oregon Revised Statute (ORS) 291.038 that the department has responsibility to "…adopt by rule policies, procedures, standards and guidelines to plan for, acquire, implement and manage the state's information resources." Additionally, ORS 291.037 stresses that the "importance of information resources in this state require strong and effective management by both individual agencies and the state as a whole." Statewide policies and procedures should be the means of implementing the state's information technology strategic plan. They also should provide mechanisms for ensuring that individual agencies' actions are congruent with the state's plan.

The policies and procedures that the department provided to other state agencies did not establish an enterprise environment for information technologies. In January 2001,the department revised many of its statewide policies to include references to sections of the Information Systems Audit and Control Foundation's Control Objectives for Information and Related Technology (COBIT™). However, those new policies did not provide specific guidance on how agencies should implement the identified control objectives. Instead, the department relies on agencies to interpret the COBIT™

objectives and create their own policies and procedures. Therefore, we concluded that the department has not adequately complied with the provisions of ORS 291.038 requiring it to "…adopt by rule policies, procedures, standards and guidelines to plan for, acquire, implement, and manage the state's information resources."

Although the department expects individual agencies to develop their own policies and procedures regarding the above issues, the department does not verify that agencies have policies and procedures in place to satisfy enterprise requirements or monitor their compliance.

Our information technology audits at other state agencies, as well as the problems noted in Chapter 2 of this report, indicate that improved statewide policies, procedures, guidance, and monitoring are needed to safeguard the state's assets. Problems with security, system development, and impaired system functionality have regularly occurred because agencies did not have, or did not consistently apply, generally accepted information technology controls. Furthermore, as the state moves into electronic government it may not be able to protect itself from increased threats to the security and reliability of its systems and resources.

We recommend that the department comply with ORS 291.038 that requires it to "…adopt by rule policies, procedures, standards and guidelines to plan for, acquire, implement and manage the state's information resources." Those policies, procedures, standards, and guidelines should be based on generally applicable and accepted control standards for information technology. This statewide guidance should be congruent with, and support, enterprise strategic plans. Additionally, the department should implement procedures to monitor state agencies' compliance with the above policies, procedures, standards, and guidelines.

CHAPTER 2: MANAGING INFORMATION SYSTEMS DEVELOPMENT

The Information Resources Management Division (division) is responsible for providing centralized computer services for most state agencies. The division's System Development and Consulting (SDC) section maintains some of the State's largest computer systems including the Statewide Financial Management System. Although SDC routinely manages significant modifications of these systems, it rarely manages other large-scale system development projects.

In recent years, the division appointed project managers from outside SDC to manage specific system development efforts. One of our audit objectives was to determine whether the division has sufficient policies and procedures in place to manage information system development. To achieve this objective, we evaluated one of the division's current system development projects, the replacement of the Network Management Communication Center (NMCC) system.

AUDIT CONCLUSIONS

Based on our review of the NMCC replacement project, we concluded that the division did not have a comprehensive System Development Life Cycle methodology to manage information system development. Additionally, it did not have project management policies and procedures or ensure that contracting issues were appropriately addressed. Consequently, the success of the NMCC replacement project was jeopardized and the division incurred avoidable project costs.

NMCC BACKGROUND AND PROJECT CHRONOLOGY

As early as 1997, the division knew that the computer system it used to manage the state's telephone networks (NMCC system) could not properly process dates on or after January 1, 2000. The NMCC system provided various functions for the division such as billing for state agencies' telephone services, tracking inventory, tracking service calls, and similar activities.

To evaluate this and other year 2000 issues, the division hired a consulting firm to assess the division's needs and suggest solutions. Part of that work included an evaluation of NMCC system functionality.

The division initially planned to either purchase a replacement system or transfer the responsibility for managing the state's telephone networks to an outside vendor. However, three attempts to outsource the function did not succeed. Then with January 2000, less than a year away, the division began evaluating other alternatives including purchasing an existing system from one of the division's communications vendors. The division spent several months evaluating this alternative. In August 1999, the division signed a contract to purchase the software, workstation, and an Oracle software license from the vendor. However, on September 22, 1999 the division decided to cancel the software contract but elected to keep the workstation and Oracle license as well as a contractor employee to manage the hardware and database. Without another viable solution, the division prepared for an imminent year 2000 system failure.

To mitigate some of those risks, the division signed a contract with a software developer in early November 1999, to create a database to capture information regarding telephone usage. This contract, Phase 0 of the project, also called for development of a billing system using the database. In early December, the system was declared year 2000 ready.

In January 2000, the division signed another contract with the software developer to program a system to replace the nonfunctioning NMCC system. This project was to use the workstation and Oracle license the division obtained from the previously cancelled contract. The new project had two phases. The first phase was to create a program to restore the most critical business functions including NMCC billing. The second phase was to polish that programming and add the remaining elements that existed in the original NMCC system.

In May 2000, before completing Phase 1, division management redirected the project to activities that were outside of the original scope of the replacement project and contract. This new project objective was to create a Unified Billing System (UBS) for all units in the division.

In September 2000, division management took a close look at the status of the NMCC system replacement project. Because of that analysis, in October 2000, it suspended further work on the UBS and redirected the project team to complete its original work. The project team reported the first NMCC phase as complete on February 15, 2001, and was still working on the second phase in April 2001.

Although the division did not track all project costs, agency records indicated that the project's contract costs totaled approximately $4.8 million by mid-February 2001, as shown in Exhibit II.

Exhibit II
NMCC Project Costs

Hardware & system software	**$1,203,857**
Unified Billing System development (software developer)	**$1,131,920**
Consulting services (consulting firm)	**$1,008,215**
Phase 0 development (software developer)	**$271,830**
Phase 1 development (software developer)	**$300,280**
Phase 2 development (software developer)	**$349,520**
Other (software developer billings not tied to a specific phase)	**$217,010**
Contracted database and system analyst (software developer, amendment 1)	**$350,000**
External quality assurance contractor	**$8,385**
Total	**$4,841,017**

SYSTEM DEVELOPMENT LIFE CYCLE METHODOLOGY

Organizations that develop systems need to have sound policies and procedures governing system development activities. Department management is ultimately responsible for the acquisition and maintenance of software that it needs to satisfy business requirements. To do this, the organization should adopt and implement information system standards and a Systems Development Life Cycle (SDLC) methodology to govern acquisition, implementation, and maintenance of systems.

The division did not have sufficient SDLC methodologies to control the NMCC project. During the initial phases, project managers did not have a prescribed SDLC methodology to follow. Rather, they took an unstructured approach using consultants to assess the division’s needs and propose solutions. After those processes failed to provide viable solutions, division management decided to convert the project from buying a replacement system to building one.

After project managers decided to develop a new NMCC system, they relied on contracted programmers to provide their own system development procedures. Although those procedures may have satisfied the programmers’ needs, they did not constitute a comprehensive SDLC methodology needed to control the project. The project team planned to use joint application development sessions to work through the details of the development. However, the project team did not use those sessions as anticipated.

Specific SDLC elements missing or not adequately covered by the contractor's development procedures included the following:

- defining system and business requirements,
- considering the system architecture,
- considering security,
- determining the feasibility of proposed solutions,
- approving formal designs,
- developing testing plans and methodology,
- formulating implementation strategies,
- performing quality assurance activities,

- developing user manuals and training, and
- performing a post implementation review.

Many potential risks arise when computer-based systems are developed without adequate SDLC methodologies. The most serious risk is that the completed system may not meet the users' business needs, user requirements, and expectations. Another significant risk is that the project may be delayed or cost more than anticipated. Although following an SDLC methodology reduces many of these risks, it does not provide absolute assurance that projects will be successfully completed. Other factors such as funding restrictions, technical expertise of staff, and management or user involvement also play a major role in the success of system development projects.

Because the division did not have an SDLC methodology to ensure all phases of the project were adequately controlled, some project efforts were not successful, including the following:

- Attempts to contract for outsourcing the desired NMCC functionality did not produce viable solutions.
- Efforts to purchase and implement an already developed NMCC replacement were not successful. Consultant's costs associated with those efforts totaled at least $439,500.
- Efforts to develop a Unified Billing System were suspended due to feasibility issues. Programming costs associated with this segment totaled approximately $1.1 million by February 2001.

Although the division started three years in advance to solve its NMCC year 2000 problems, it was unable to do so by the required deadline. As of April 2001, full system capability has not been restored, including a complete version of the telephone billing subsystem.

We recommend that the department adopt an agency-wide comprehensive SDLC methodology. This methodology should include specific policies and procedures to govern all aspects and phases of the system development life cycle.

PROJECT MANAGEMENT

Organizations should establish and apply sound project management techniques to ensure projects remain on time, task, and budget. Project management should address allocation of responsibilities, task breakdowns, budgeting of time and resources, milestones, check points and approvals. It should also include processes for monitoring costs incurred throughout the life of the project.

Division management did not provide sufficient oversight to ensure the success of the project. Specifically, they did not effectively:

- assign clear responsibility for completing essential tasks,
- ensure team members were accountable for assignments,
- track project costs or provide an accurate accounting for resources expended,
- ensure contract payments reflected work performed, and
- provide for quality assurance.

Project Management Confusion

Although several individuals were concurrently "in charge" of the project, the extent of their actual duties and responsibilities were not well defined. At times, the NMCC project was staffed, managed, and evaluated by various contractors and consultants in addition to a division manager.

One division manager was identified in a contract as "responsible for assuring the success of the project." However, the consulting firm contracted to "apply its project management expertise to the NMCC replacement project activities so that DAS IRMD will meet or exceed the NMCC project objectives." Additionally, the consulting firm was responsible for enabling the division "to fulfill its obligations to" the software developer for the NMCC replacement project. This complex organizational structure posed some unique project management challenges for both contractors and division managers.

When one division manager was moved off the project in May 2000, management did not formally reassign his project responsibilities; consequently, from May to October 2000, no one from the division was responsible for ensuring the project team remained on task and budget.

Cost Accounting

Division managers also did not separately account for all NMCC project costs in its accounting system. The Project Monitor tracked some costs using a spreadsheet; however, it did not include internal costs associated with the project, such as salaries, supplies, legal fees, or administrative overhead. Therefore, as of April 2001, the division could not provide a complete accounting of project costs. Consequently, the division may not be able to accurately capitalize the cost of the system at project completion.

Overpayments

While reviewing contract costs, we determined that the division made overpayments of $124,616 to the software developer, as shown in Exhibit III.

Exhibit III

Contract Overpayments to the Software Developer

May 2000 duplicate invoice for Amendment 1.	$35,000
July 2000 duplicate invoice for Amendment 1.	$35,000
Over-payment of Phase 1 contract amounts retained.	$54,616
Total	**$124,616**

Retainage

Further, the project manager did not always enforce contract provisions. For example, software development contract specified that 20 percent of each invoice would be withheld as retainage. The retainage for each phase was to be paid to the contractor upon the successful completion of the phase. However, the division did not withhold retainage until October 2000, and the amounts actually withheld did not include the full 20 percent.

In February 2001, the division paid the software developer five-sixths of the retainage for Phase 2 invoices relating to development of the Unified Billing System, although the contractor had not yet completed the phase. The division paid the contractor $167,186 of Phase 2 retainage that, by contract, should not have been released.

Quality Assurance

Division policy requires that major projects, like the NMCC replacement, set aside a portion of project budget to fund quality assurance activities. This includes hiring an external quality assurance contractor to evaluate project risks and report whether project timelines and deliverables are being met.

Although the contracted development began in November 1999, the division did not hire a quality assurance contractor for this project until November 2000. Additionally, the division's Quality Assurance Manager assigned to the project did not perform quality assurance reviews or ensure that the external quality assurance contractor was hired.

The division did not provide an adequate project management framework or oversight to ensure that project managers consistently performed critical management tasks.

We recommend that the department adopt, as part of its System Development Life Cycle methodology, a project management framework to ensure all projects are consistently and effectively managed. This framework should at least address allocation of responsibilities, task breakdowns, budgeting of time and resources, milestones, check points and approvals including quality assurance. It should also include processes for monitoring costs incurred throughout the life of the project.

We also recommend that the department adjust future contractor payments to adjust for past payment errors.

CONTRACTING ISSUES

The division's system development projects are subject to the state's purchasing laws and regulations. Some of those rules, such as competitive bidding requirements, help to ensure that the state pays a fair price for goods or services. Additionally, legal sufficiency reviews may help agencies develop contracts that safeguard the state's assets.

The division's contracts often included terminology or requirements that were unclear or ambiguous. One contract did not clearly define the duties and responsibilities of the contractor, the scope of work, or the required deliverables. Additionally, the contracts generally tied contract payments to time spent on the project rather than required deliverables. An amendment to this contract specified that the contractor would be paid a monthly rate for services rather than the typical hourly rate. As a result, during the first month of the amendment, the contractor was paid the full $35,000 monthly amount, even though the company only provided approximately one week of services. Thus, resources may have been expended for work that did not contribute to the project's success.

Division management used year 2000 exemptions as authorization to enter into many of the contracts without competitive bidding. Because of the scope of these contracts, it is not clear that the Division's reliance on year 2000 exemptions was appropriate in all instances. The applicability of the year 2000 exemption relates to the character of the work included under the contract. This mechanism was created to allow timely processing of contracts to resolve year 2000 date problems. However, it is unlikely that the exemption was intended to permit agencies to undertake, without competitive bidding, large-scale information system replacement projects that might, as an incidental matter, remediate year 2000 date issues.

With the above criteria in mind, several of the NMCC project activities did not relate to year 2000 date issues. The $35,000 monthly rate amendment to the software development contract added a database administrator and a systems administrator to work in the division's data center. This work was to perform current data center operations, not year 2000 remediation. Additionally, the division's development of a Unified Billing System was largely unrelated to year 2000 remediation. Only the NMCC billing component had year 2000 issues and, according to the agency's December 1999, year 2000 certification, those problems had already been resolved.

Ultimately, it is management's responsibility to ensure that contracts satisfy all legal requirements and adequately protect the state's interests. As a result of the above contracting issues the division likely incurred unnecessary costs.

We recommend that division management consult with the Attorney General regarding the propriety and legal effect of its reliance on year 2000 exemptions with regard to the NMCC contracts. Division management should also consider requesting more stringent contract reviews from the Attorney General's office.

CHAPTER 3: RECOVERY OF DIVISION COSTS

The Information Resources Management Division (division) is responsible for ensuring that the rates it charges state agencies represents the actual cost of providing those services. Our final audit objective was to determine whether the division's business processes provided a reasonable basis for cost allocation and recovery. To achieve this objective, we evaluated the division's rate setting processes, retained earnings balances, and transfers between operating units.

The division provides centralized services to state agencies on a cost-reimbursement basis. Thus, it uses internal service funds for financial reporting purposes. One of the primary goals of internal service funds is to ensure that costs of providing services are appropriately charged to the organizations that actually received those services. To facilitate this task, management should implement cost tracking procedures that provide a reasonable basis for establishing the rates it charges customers. Internal service funds should retain sufficient earnings to ensure continuing operations; however, significant long-term retained earning surpluses may indicate that customers were overcharged.

AUDIT CONCLUSIONS

Although the division revised its rate setting methodology during the 2000 calendar year, its business processes should be improved to ensure that they provide a reasonable basis for cost allocation and recovery.

Using the prior methodology, the division overcharged some of its customers while undercharging others. In July 2000, division management reduced some General Government Data Center charge rates by approximately 50 percent, even though related expenditures had not substantially declined over the past four years. Another indication of past overcharges was that the division had surplus retained earnings of at least $11 million as of August 2000.

The division's procedures used for developing the rates for the 2001-2003 biennium should be improved. The method based biennial costs on a projection of three months' current expenditures. However, the projection did not differentiate between capital expenditures and operating expenditures, did not include depreciation expenses, and did not appropriately consider beginning retained earnings. Furthermore, division management applied the rate setting method inconsistently.

The division also did not have procedures to monitor costs and revenues to ensure that rates remained reasonable, nor did it have procedures for adjusting rates should changes become necessary. Additionally, some General Government Data Center rates were inequitable because they provided volume discounts to some customers. Thus, total costs were not allocated on a pro-rata basis.

We recommend that the division improve its rate setting model by:

- considering beginning retained earnings and planned future costs when setting rates,

- ensuring that all units properly apply the approved rate setting methodology,

- regularly review rates to ensure they remain valid and provide a mechanism for timely adjusting rates should it become necessary, and

- discontinuing volume discounts for services.

COMMENDATION

The courtesies and cooperation extended by the officials and staff of the Department of Administrative Services Information Resources Management Division during the course of this review were commendable and sincerely appreciated.

AUDIT TEAM

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Mark A Winter, CPA, CISA
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AGENCY'S RESPONSE TO THE AUDIT REPORT

Oregon
John A. Kitzhaber, M.D., Governor

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July 19, 2001

The Honorable Bill Bradbury
Secretary of State
136 State Capitol
Salem, Oregon 97310

John Lattimer
Director
Secretary of State Audits Division
255 Capitol Street NE Suite 500
Salem, Oregon 97310

Dear Secretary Bradbury and Mr. Lattimer:

The Department of Administrative Services (DAS) appreciates the work performed by state auditors in their recent audit of selected activities within the DAS Information Resources Management Division (IRMD). DAS agrees with the findings noted in the audit.

Historically, enterprise leadership provided by DAS IRMD has been insufficient to support the degree of coordinated corporate activity desired by the Governor and by the Legislature. The Department recognizes the need to strengthen its policies, procedures, controls and guidance of state government and has initiated corrective measures.

One theme of the audit is that DAS IRMD should emphasize the compliance role under ORS 291. In the past, DAS IRMD has not focused on a compliance monitor role with Executive Department agencies. We agree that more oversight of technology in state government is now desirable. In the immediate future, IRMD will refocus its efforts on adopting clear statewide policies and standards for technology. Based on that experience, IRMD will develop a budget package for inclusion in the '03-'05 budget process to build additional capacity for enforcement and monitoring of state agencies for the agreed upon statewide technology policies and standards.

One specific recommendation is that the Department adopt "a project management framework to ensure that all projects are consistently and effectively managed."

DAS requested, and the 2001 Legislature approved and funded, a full-time Project Management Office. Once staffed, the Office will design and adopt a comprehensive project management methodology consistent with the national Project Management Institute's (PMI) Guide to the Project Management Body of Knowledge (PMBOK), the International Organization for Standardization (ISO) 9001 standard and the American National Standards Institute's (ANSI) Q10006-1997 standard.

This methodology will be documented and adopted by October 31, 2001. DAS IRMD Statewide Technical Education Program Services Office (STEPS) will work with the Project Management Office to ensure adequate training for state agency employees so that, over time, the State develops a broad corps of project managers who use the same practices in their work.

Finally, the Department appreciates the attention of state auditors and looks forward to continuing to work with you.

Sincerely,

Mike Greenfield
Director

Ann Terry
State Chief Information Officer

FACTS ABOUT THE SECRETARY OF STATE AUDITS DIVISION

The Oregon Constitution provides that the Secretary of State shall be, by virtue of his office, Auditor of Public Accounts. The Audits Division exists to carry out this duty. The division reports to the elected Secretary of State and is independent of the Executive, Legislative, and Judicial branches of Oregon government. The division audits all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

Directory of Key Officials

Director	John N. Lattimer
Deputy Director	Catherine E. Pollino, CGFM
Deputy Director	Sharron E. Walker, CPA, CFE

This report, which is a public record, is intended to promote the best possible management of public resources.

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