STATE OF NORTH CAROLINA
Office of the State Auditor

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INTERIM REPORT

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Governor Michael F. Easley
Senator Eric Reeves, Co-Chair
Representative Joe Tolson, Co-Chair
Representative Russell Tucker, Co-Chair
Members of the Joint Select Committee on Information Technology
Members of the General Assembly
Mr. Ron Hawley, Chief Information Officer

Ladies and Gentlemen:

Pursuant to Senate Bill 222 of the 1999 Session Laws as passed by the General Assembly, we are submitting this *Interim Report* on the performance audit of the Office of Information Technology Services (ITS) procurement function. Specifically, the legislation directed us to review the procurement process for information technology that was transferred in Senate Bill 222 from the Department of Administration, Division of Purchase and Contract (P&C) to ITS. The specific objectives as identified in the legislation along with ones identified by the State Auditor were:

- Determine whether the Office of Information Technology Services (ITS) established adequate rules and internal procedures to exercise the powers granted especially with regard to the additional powers contained in Senate Bill 222.
- Ascertain whether ITS complied with applicable statutes, rules, and regulations.
- Assess the efficiency and effectiveness of the procurement policies and operations of ITS and compare the procedures and operations of the IT procurement process at ITS to the process previously used at the Department of Administration, Division of Purchase and Contract (P&C).
- Identify the amount spent throughout State government for IT assets.

Office of Information Technology Services Overview

The Office of Information Technology Services (ITS) was placed within the Department of Administration in 1983[1] when it was established, moved to the Office of the State Controller in 1987, and transferred to the Department of Commerce in 1997 where it was when we began this review. Effective September 1, 2000, ITS became a separate agency within the Office of the Governor (House Bill 1578 of the 2000 Session). The State's Chief Information Officer (CIO), who heads ITS, was reporting to the Secretary of Commerce at the beginning of the review. The CIO now reports to the Governor's Chief of Staff.

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[1] ITS was originally called the State Information Processing Services (SIPS). House Bill 253 of the 1999 Session of the General Assembly formally changed the name to ITS.

The Statewide IT Procurement Office is located within the ITS Financial and Facilities Services section. The Chief IT Procurement Officer reports to the ITS Chief Financial Officer. As of June 30, 2000, the Procurement Office contained 13 positions as shown in Table 1, at an estimated total cost (salary and benefits) that will be $850,085 annually. Five new positions were added when the procurement function was transferred from P&C to ITS and two more positions were added during April and May 2000 but were not filled as of June 30, 2000. Since the Procurement Office was just beginning to operate and fill positions, total expenditures for the Office from January to June 2000 were only $178,793 while total revenues were $11,657.

TABLE 1 OFFICE OF INFORMATION TECHNOLOGY SERVICES STATEWIDE IT PROCUREMENT OFFICE STAFFING AS OF JUNE 30, 2000				
Position Title	Prior Organizational Placement	Budgeted Salary	Estimated Benefits	Annual Personnel Cost
Chief IT Procurement Officer	ITS Computing Services	$ 65,400	$ 28,122	$ 93,522
Program Assistant V	New Position Created	29,410	12,646	42,056
State Purchasing Administrator (Statewide)#	New Position Created	56,744	24,400	81,144
State Procurement Specialist III	New Position Created	39,196	16,854	56,050
State Procurement Specialist III	New Position Created	49,493	21,282	70,775
State Procurement Specialist III	New Position Created	49,493	21,282	70,775
State Procurement Specialist III #	New Position Created	49,428	21,254	70,682
Departmental Purchasing Agent III	ITS Business Technology Services	43,892	18,874	62,766
Contract Compliance Specialist	ITS Telecommunications Services	65,885	28,331	94,216
State Purchasing Administrator (ITS Agency)*	ITS Purchasing	42,708	18,364	61,072
Departmental Purchasing Agent II #	ITS Purchasing	36,126	15,534	51,660
Departmental Purchasing Agent II	New Position Created	34,480	14,826	49,306
Departmental Purchasing Agent I	ITS Purchasing	32,210	13,850	46,060
TOTAL		$ 594,465	$ 255,620	$ 850,085
Source: Office of State Personnel Position Histories				
*The additional position of ITS State Purchasing Administrator was created in April 2000.				
# Position vacant at time of audit, salary estimated at mid-point of salary range				
Note: Benefits estimated at 43% of salary				

Audit Progress

Senate Bill 222 directs that this audit be conducted in three phases with an interim report on operations from January 1, 2000 through June 30, 2000, a second interim report on operations from January 1, 2000 through December 31, 2000, and a final report on operations from January 1, 2000 through June 30, 2001. This first interim report covers operations for the Statewide IT Procurement Office for the period January 1, 2000 through June 30, 2000. Office of the State Auditor staff conducted the on-site fieldwork for this interim report during the period August through October 2000. The following pages contain our conclusions on the IT Procurement Office operations, categorized under the four objectives previously identified.

Rules and Internal Procedures

We conducted in-depth interviews, observed operations, reviewed policies and procedures manuals, and viewed information contained on the ITS web site to determine whether adequate rules and internal procedures had been developed. Analysis of Senate Bill 222 indicated which areas were required for development of new rules and procedures. Further, we compared the rules and policies and procedures of ITS to those utilized by the Department of Administration, Division of Purchase and Contract.

Conclusion: ITS established adequate rules and internal procedures to exercise the powers granted by Senate Bill 222 for the IT procurement process. Temporary rules were developed and became effective January 1, 2000. ITS held a public hearing February 15, 2000 and permanent rules were adopted effective August 1, 2000. ITS created information technology procurement policies and procedures and posted these policies on the ITS web site. In addition, ITS established internal policies and procedures governing the operations of the Statewide IT Procurement Office. Table 2, page 4, summarizes the requirements contained in Senate Bill 222 and ITS' progress toward implementing the powers granted.

While ITS did establish adequate rules and internal procedures, we noted a few concerns as summarized below:

- The Statewide IT Procurement Office does not have a formal monitoring process to evaluate the progress and accomplishments of the program.
- There are weaknesses in the Statewide IT Procurement Office's computerized tracking system.
- ITS' internal procedures manual for statewide procurement is vague, inconsistent, and incomplete.

These issues have been discussed with ITS management and ITS has taken, or plans to take, steps to address these concerns.

Compliance with Regulations

We reviewed ITS' policies and procedures, as well as the General Statutes and North Carolina Administrative Code pertaining to ITS and procurement operations. To assess compliance with regulations regarding contracts, we analyzed a sample of contracts approved and awarded by ITS during the first six months of the Procurement Office's operations. In addition, we performed tests of a sample of expenditures incurred during the period January 1, 2000 through June 30, 2000.

Conclusion: ITS complied with statutes, rules, and regulations. However, we noticed that in some instances the Statewide IT Procurement Office contract files did not include all necessary documentation such as required approvals. These issues have been discussed with ITS management and ITS has taken, or plans to take, steps to address these concerns.

TABLE 2 STATUS OF REQUIREMENTS OF SENATE BILL 222			
Cite	**Requirement**	**Status**	**Explanation**
143B-472.50(a)	Establish Office of ITS as a division of Department of Commerce.	Implemented	
143B-472.50(b)	ITS shall be administered by the State Chief Information Officer (CIO)	Implemented	
143B-472.50(b)	The CIO shall be appointed by and report to the Secretary of Commerce.	Implemented	
143B-472.51(a)(1)	Procure all information technology (IT) for State agencies, except the University of NC and its constituent institutions.	Implemented	
143B-472.51(a)(2)	Obtain IRMC approval for all rates and fees for common, shared State government technology services.	Implemented	
143B-472.51(a)(3)	Recommend State government-wide, enterprise-level policies for information technology	Implemented	
143B-472.51(a)(4)	Develop standards, procedures and processes for implementing policies approved by IRMC.	Partially Implemented	ITS is working with the IRMC to establish criteria, dollar thresholds and types of contracts needing approval.
143B-472.51(a)(6)	Develop a plan for managing IT assets to minimize total life cycle costs of assets and have this plan approved by IRMC.	Partially Implemented	ITS is developing an inventory system including total life cycle cost. Estimated completion 2 years.
143B-472.51(b)	Other state agencies and local governmental entities may use the IT programs, services or contracts offered by ITS	Implemented	
143B-472.52(c)	Conduct and maintain a continuous inventory of each State agency's current and planned investments in IT assets. Including the development and implementation of standards, processes and procedures for the inventory.	Partially Implemented	ITS is developing an inventory system including total life cycle cost. Estimated completion 2 years.
143B-472.53(b)	ITS shall develop a plan for the State government-wide management of distributed IT assets. The plan shall prescribe the State government-wide infrastructure and services for managing these assets. The plan must be submitted to the IRMC.	Implemented	
143B-472.54	The office shall procure all IT for State agencies except the UNC System. ITS shall integrate technological review, cost analysis, and procurement for all information technology needs of those state agencies in order to make procurement and implementation of technology more responsive, efficient, and cost effective.	Implemented	
143B-472.55(1)	ITS can authorize any department, institution, or agency to purchase or contract IT assets/services	Implemented	
143B-472.55(2)	Establish processes, specifications and standards that apply to all IT to be purchased licensed or leased in the State government.	Implemented	
143B-472.55(3)	Comply with the state government-wide technical architecture, as required by the IRMC	Implemented	
143B472.56	All State agencies covered by this part shall use contracts for IT acquired by ITS for any IT required by the State agency that is provide by these contracts.	Implemented	
143B-472.58(a)	ITS encourage state agencies to use small, minority, physically handicapped and women contracts.	Implemented	
143B472.58(b)	Every State agency required by this part to use the services of ITS in the procurement of IT which purchases IT directly shall report to ITS the information required by G.S. 143-48(b). ITS will report to the DOA this information.	Repealed by HB1578	
143B-472.60	The Secretary of Commerce and CIO shall not have a financial or personal beneficial interest in the purchase of or contract for IT.	Implemented	
143B-472.60	ITS employees can not accept or receive rebate, gifts or otherwise any money or anything of value from persons, firms or corporation.	Implemented	
143B-472.63(a)	The Secretary will establish a benchmark for contract approval by the Board of Awards.	Implemented	
143B-472.63(b)	The Director of Budget will approve all contracts for IT being acquired by ITS	Implemented	
143B-472.64	Develop a system for budgeting and accounting of expenditures for IT operations, services, projects, infrastructure and assets. This is a joint effort with ITS, OSBM, and OSC	Partially Implemented	ITS, OSC, and OSBM are continuing to develop a uniform reporting system for budgeting and accounting of IT assets and services.
143-135.9(c)	Acquisition of information technology by the State shall be conducted using the "Best Value" procurement method	Implemented	
150B-21.1(a)(4)	The Secretary may adopt temporary IT procurement rules. 30 days prior to adopting temporary rules the Secretary must notify appropriate persons, accept oral and written comments and hold a public hearing	Implemented	
Section 18	The Secretary shall develop policies and procedures to ensure the use of "Best Value" procurement no later then December 31, 1999.	Implemented	
Section 19	The Secretary will provide training to agencies and vendors on "Best Value" procurement.	Implemented	
Section 20	The Secretary will report to the Joint Select Committee on IT on the results of the implementation of this act on or before April 1, 2000.	Implemented	

Efficiency and Effectiveness; Comparison to Prior Process

We calculated the turnaround times for purchase requests processed by the Statewide IT Procurement Office and compared those to times for the Department of Administration, Division of Purchase and Contract. In addition, we conducted a user survey of agency purchasing agents who had used either ITS and/or P&C for their IT purchases since January 1, 2000. We calculated and compared the personnel costs for both ITS and P&C for comparison. Further, we compared the rules and regulations and the policies and procedures for each office. Our user survey provided further information regarding the quality of service provided by each agency. Finally, we analyzed the organizational structure in place at ITS to handle the IT procurement process.

TABLE 3 PURCHASE REQUEST TURNAROUND TIMES (in days) COMPARISON OF ITS TO P&C (Highlighted items show faster time.)		
PURCHASE TYPE	ITS 1/1/2000- 6/30/2000	P&C 7/1/1999-- 12/31/1999
IT Goods	40	35
IT Services	32	45
Bids	59	63
Emergency Purchases	N/A	15
Negotiated Contracts	11	7
Sole Source Contracts	22	20
Overall	36	40
Source: ITS and P&C contract files		

Conclusion: The Statewide IT Procurement Office had a faster overall turnaround time than did P&C. However, each office performed better in certain categories as detailed in Table 3. At this point in time, survey respondents believed that P&C is more responsive, has a higher level of expertise, and is less problematic (see Table 4). These perceptions may be the result of resistance to change. Further, analysis shows that the State actually incurred an additional $119,828 in salaries and benefits from January to June 2000 resulting from the creation of five positions, four of which were filled during this period, to staff the Statewide IT Procurement Office. Finally, the organizational structure could be adjusted to improve operations. Preliminary concerns noted were:

TABLE 4 USER SURVEY RESULTS COMPARISON (Table shows percentage of respondents choosing each entity.)		
FACTOR	ITS	P&C
Experienced problems with service	35%	12%
Personnel Expertise		
Excellent	8%	24%
Good	36%	52%
Fair	20%	16%
Poor	4%	0%
Responsiveness		
Excellent	8%	32%
Good	28%	36%
Fair	32%	20%
Poor	4%	4%
Rating Scale: 5--Excellent, 4--Very Good, 3--Good, 2--Fair, 1--Poor		
Ability to track progress of purchase request/order	2.89	3.92
Purchasing flexibility (not just lowest price)	3.16	3.30
Timeliness of responses	2.89	3.44
Turn-around time of requests/purchase orders	2.95	3.41
Expertise regarding IT items	3.37	3.44
Number of vendors to choose from	3.32	3.96
Ability to negotiate terms of contracts	3.00	3.56
OVERALL EFFECTIVENESS	2.89	3.63
Source: Compiled by OSA from Survey Results		

- The State's purchasing authority is split between two agencies leading to confusion and concern by state agencies and vendors.

- Universities, community colleges, and local government agencies may choose to utilize ITS or P&C which could potentially limit economies of scale that could be achieved through bulk-buying discounts.

- ITS Agency Purchasing is inter-mingled with the Statewide IT Procurement Office.

These issues have been discussed with ITS management and ITS has taken, or plans to take, steps to address these concerns to the extent it can.

Information Technology Expenditures

Based on our preliminary work, the State Auditor added this objective of determining the total information technology expenditures for the State. We obtained the Office of the State Controller's (OSC) "Information Technology Expenditures Report" for the period ended June 30, 2000. We inquired of ITS regarding the creation of a statewide IT inventory and the progress toward achieving that goal.

Conclusion: Table 5 shows the breakdown of IT expenditures throughout the State for FY1999-2000. These amounts were determined by OSC based upon information gathered from the North Carolina Accounting System. OSC estimated the number of IT positions within state government and the University of North Carolina System. ITS does not plan to utilize this information when preparing the statewide inventory of IT assets. Currently, ITS is in the planning stages for a fully automated statewide inventory and asset management system. The project will take 12 to 18 months for completion and implementation. ITS hopes to have full implementation within 2 years.

TABLE 5 INFORMATION TECHNOLOGY EXPENDITURES JULY 1, 1999 TO JUNE 30, 2000		
Description	**Subtotal**	**Total**
State Employees:		
Salary & Fringes		$ 266,429,064
Contracted Personal		107,662,881
Software:		
Maintenance	$ 31,808,639	
Purchase/Development	28,017,126	
Total Software		59,825,765
Hardware: Data Processing		
Repair and Maintenance	11,168,127	
Purchases	127,431,970	
Rent/Lease	7,888,223	
Total DP Hardware		146,488,320
Hardware: Telecommunications		
Purchase	17,889,811	
Rent/Lease	982,302	
Total Telecommunications Hardware		
		18,872,113
Data Processing Supplies		6,028,998
Telecomm/Networking Services		137,988,773
Mainframe Services		98,996,336
Grand Total		**$ 842,292,250**
Source: OSC "NC Information Technology Expenditure Report for Year Ended June 30, 2000."		
Note: Information is unaudited.		

Next Steps

We now have a good understanding of the operational procedures used by ITS for the procurement process. As directed by the legislation, we will assess the effectiveness and efficiency of those procedures for the period ending December 31, 2000. We have shared a draft copy of this interim report with Mr. Ron Hawley, the State's Chief Information Officer. After discussions of our initial points of concern with Mr. Hawley and his staff, ITS has made changes based on those discussions. We will continue to work with ITS staff to complete the second interim report and the final report as directed in the legislation.

We wish to thank the State's Chief Information Officer and the staff at ITS for their cooperation thus far in the audit. As always, we stand ready to discuss this interim report with the Joint Select Committee on Information Technology.

Respectfully submitted,

Ralph Campbell, Jr.
State Auditor