

MEMBERS:
TOM BERRYHILL
NORMA TORRES



California State Senate

CONSULTANTS:
MARK IBELE
BRADY VAN ENGELEN

(916) 651-4103

COMMITTEE
ON
BUDGET AND FISCAL REVIEW
SUBCOMMITTEE No. 4 ON
STATE ADMINISTRATION AND GENERAL GOVERNMENT

ROOM 2054, STATE CAPITOL
SACRAMENTO, CA 95814
(916) 651-4007

SENATOR
RICHARD D. ROTH
CHAIR

OVERSIGHT HEARING

State Controller's Office

Thursday, August 15, 2013

State Capitol, Room 112

Upon Adjournment of Session

- Chair, Senator Richard Roth
- Vice Chair, Senator Tom Berryhill

AGENDA

Introductory Remarks

History/Overview of the 21st Century Project

Legislative Analyst's Office

- *Chas Alamo*, Consultant
- *Lourdes Morales*, Consultant

California State Controller's Office

- *Lisa Crowe*, Chief, Personnel and Payroll Services Division
- *Tony Davidson*, Project Director, 21st Century Project
- *Jim Lombard*, Chief Administrative Officer
- *Jan Ross*, Chief Information Officer
- *Tom Yowell*, Chief, Administration and Disbursements Division

California Department of Technology

- *Carlos Ramos*, Secretary, Department of Technology

**State of California Task Force on
Re-Engineering IT Procurement for Success**

- *Dr. Rosio Alvarez*, Chair
- *David Kraus*, Member

Public Comment

Closing Comments

Attachments

- Committee Background
- LAO Background on the 21st Century Project
- 21st Century Project timeline
- 21st Century Project Summary Chart

Background on the 21st Century Project

Background: The State Controller's Office (SCO) is responsible for the payment of salaries and wages to approximately 294,000 employees, including state civil service, California State University and Judicial Council employees, judges and elected officials. The payroll system currently utilized by the SCO is a legacy system developed in the 1970s. The need for an updated payroll system was underscored by the decreasing number of information technology personnel that could understand the language utilized to develop and/or modify this antiquated system. In 2004, the SCO identified a solution that would integrate different components of the existing statewide human resources management system. The intent was to improve management processes and fulfill payroll and reporting obligations in a timely fashion. The project to replace the outdated software platform was defined in a Feasibility Study Report (FSR) as the 21st Century Project. In 2005, the Legislature approved the project with an estimated total cost of \$130 million.

Originally, the SCO utilized a two-phased procurement process. One vendor would provide the software package and another vendor would be responsible for system integration. In April 2005, SAP Public Services was selected to provide the software package. The software package was sold as commercial-off-the-shelf (COTS). The second vendor (primary vendor) was to integrate the software package to meet the business needs of the state. BearingPoint was awarded the primary vendor contract as the system integrator.

Shortly after awarding the prime vendor contract to BearingPoint, the SCO identified a number of issues related to the work product of BearingPoint. BearingPoint countered that the software platform was designed to meet the requirements, as specified in the contract. In October 2007, SCO issued a breach-of-contract notice to BearingPoint. A resolution was finally agreed to, however, the 21st Century Project was now delayed significantly and the estimated overall project cost had risen to \$180 million. On January 6, 2009, SCO formally terminated the prime vendor contract with BearingPoint and the prime vendor related workload related to the 21st Century Project came to a halt. One of the primary driving forces for the termination of the prime vendor contract with Bearing Point was the inability to develop accurate, reliable data conversion programs, scripts and computer instructions that would allow the new SAP software to incorporate and use all of the historical data stored in the SCO's legacy system.

In May 2009, the third Special Project Report (SPR) was released and the scope of the project had changed to no longer include the 54,000 employees at the California State University payroll system. The legacy system would still manage payroll disbursement for CSU employees until a revised system for CSU employees was fully developed. The SCO cited the lower amount of risk and complexity that would be associated with the project since the 21st Century Project now did not include the payroll processing of CSU employees. Overall project cost estimates were reduced to \$126 million and the project completion date was estimated to be June 2010.

The Department of General Services (DGS), which then served as the state's lead IT procurement entity, issued a Request for Proposal (RFP) in March 2009 for a new system integrator. At this point, SCO and DGS utilized a multi-stage procurement process, with Stage consisting of (1) the selection of contractors to evaluate work done to date, and, (2) gaining a better understanding of workload requirements. Two vendors qualified in Stage I (Accenture and SAP) and again only two vendors submitted bids in Stage II. The contract was awarded to SAP in February 2010, and project costs and timeline estimates were revised. Project costs

were upwardly revised to \$305 million and the final implementation date was set to be September 2012.

Upon the contract being awarded to SAP, an implementation schedule was established. The project would be rolled out in five phases. Pilots I and II would be a limited rollout impacting only a small number of state employees. Subsequent waves I, II, and III would integrate more employees into the software platform on a graduated scale of complexity. Pilots I and II were to convert 15,000 state employees to the new MyCalPays user system in 2013. Wave III would follow shortly thereafter and convert another 74,000 state employees to the MyCalPays system. Waves IV and V were 85,000 and 65,000 individuals respectively and were set to be transitioned to the MyCalPays system during the 2014-15 fiscal year.

Data conversion continued to represent a significant challenge for the vendor, and project management staff issued a cure notice in August 2011 to SAP as the primary vendor. The cure notice specified that various issues surrounding data conversion would need to be addressed. SCO representatives made no mention of the cure notice before a Little Hoover Commission oversight hearing related to the progress of the 21st Century Project, nor was it mentioned in the September 2011 progress report issued quarterly to the Legislature. In response to the first cure letter, the primary vendor, SAP, agreed to hire a subcontractor (BackOffice Associates) to manage the data conversion component of the contract. SCO seemed satisfied with the agreement reached regarding hiring a subcontractor to manage the data conversion component and approved continuation of the project.

In June 2012 SCO began the implementation of Pilot I. Pilot I was designed to be a small scale rollout; producing payroll, benefits, timekeeping, and regular disbursement related activities for SCO's 1300 employees. The small number of employees in Pilot I was by design, and would afford the SCO and the vendor the opportunity to address any defects prior to progressing. However, the sheer scale and impact of the defects was unanticipated. For example, pay was incorrectly deducted from SCO staff and, in some cases, medical benefits were denied to staff and dependents. Attempts to correct the issues identified by SCO staff further compounded issues in the subsequent payroll cycle and the SCO chose to delay the implementation of Pilot II in order to address the defects. Pilot II was initially delayed until March 2013.

The SCO issued a second cure letter to SAP on October 25, 2012. The cure letter raised issue with the resources SAP put forward to address the defects and questioned SAP's ability to successfully implement the system. SCO identified thirteen separate points of contention with the vendor and requested that the issues be addressed prior to November 30, 2012, and prior to the contract moving forward. In its response to the cure notice, SAP did not assume responsibility for the issues identified and, according the SCO, did little to correct any of the grievances raised by the SCO's cure letter.

SAP's contract to provide system integration for SAP software was terminated by the SCO on February 8, 2013, and the California Technology Agency has suspended the 21st Century Project until further notice. As of January 1, 2013, total project costs were estimated to be \$255 million, and overall costs project at full implementation were estimated to be \$371 million. The total amount spent on the 21st Century Project is nearly triple the original estimates as identified in the May 2004 Feasibility Study Report (FSR). General Fund contributions for the 21st Century Project have totaled \$180 million. The SCO has returned to its legacy payroll disbursement system that it had used prior to the failed rollout of MyCalPays.

August 15, 2013

State Controller's Office: 21st Century Project

LEGISLATIVE ANALYST'S OFFICE

Presented to:

Senate Budget and Fiscal Review Subcommittee No. 4

On State Administration and General Government

Hon. Richard Roth, Chair





Project Description and Budget



What Is the 21st Century Project?

- The 21st Century Project (TFC) is an information technology project that would replace existing human resources and payroll management systems with a single statewide system.
- The existing systems are old and inflexible, cannot meet the needs and demands of the state, and are at risk of failure.
- The new system, to be called MyCalPAYS, would improve payroll, benefits administration, and timekeeping and include self-service access by employees and managers, among other capabilities.



2013-14 Budget

- The *2013-14 Budget Act* includes \$14.6 million (\$11.9 million General Fund) in 2013-14 for:
 - Reconciliation to ensure State Controller's Office (SCO) employees and vendors received accurate payments and information during the pilot period.
 - Archive the pilot system for record-keeping purposes.
 - Prepare for contractually mandated mediation and potential legal proceedings with SAP Public Services, Inc. (SAP).
- The budget limits funding for these activities to the first two months of the fiscal year—\$2.4 million (\$2 million General Fund)—which correspond with this legislative oversight hearing.
- Funding for the remainder of the fiscal year—\$12.1 million (\$9.9 million General Fund)—will be available no sooner than September 1, 2013, pending this legislative oversight hearing.



Project Description and Budget *(Continued)*



Project Expenditures

- At the time of the contract termination, the state had spent \$262 million of the \$373 million estimated total project cost.



Project Timeline and Status



Timeline

- **May 2004**—The Department of Finance approves the TFC project's Feasibility Study Report and the project begins. The estimated cost of the project is \$130 million and full implementation is scheduled for July 2009.
- **April 2005**—The TFC project procures the SAP software solution for the new system and begins a second procurement for an integration vendor to design, develop, and deploy the solution.
- **June 2006**—The TFC project contracts with BearingPoint, the winning integration vendor.
- **October 2007**—Following multiple schedule delays, the TFC project issues a breach-of-contract notice to BearingPoint. The system integrator and the TFC project go on to reach a plan to address project challenges and integration continues.
- **May 2008**—Estimated cost increases to \$180 million while full implementation is extended to June 2010.
- **January 2009**—After experiencing serious vendor problems, the state issues a notice of default to BearingPoint and terminates the contract.
- **February 2010**—After completing a second vendor procurement, the TFC project contracts with SAP to complete the new system. With the start of the SAP system integration contract, the TFC project updates its costs and schedule to \$283 million and October 2012.
- **Spring 2011**—Initial data conversion tests between the state's existing payroll system and the new system are problematic. The TFC project staff identify additional implementation challenges.



Project Timeline and Status

(Continued)

- **August 2011**—The TFC project issues the first cure notice to the new system integrator, SAP, requiring SAP to improve data conversion, among other requests. The SAP subcontracts with BackOffice Associates to remedy the cure notice, and the project continues.
- **November 2011**—The TFC project staff and SAP review data conversion and replan timeline, delaying the first pilot test by nine months. The TFC project updates its cost estimate to \$373 million and extends the project to September 2013.
- **June 2012**—Pilot 1 goes live, processing payroll for 1,400 SCO employees.
- **August 2012**—The TFC project staff report significant errors during the go-live payroll, including overpayments, incorrect deductions, and leave balance discrepancies. Staff tentatively delay Pilot 2 from September to March 2013.
- **October 25, 2012**—The TFC project issues a second cure notice to the system integrator, SAP, requiring SAP to increase personnel on the project, reschedule project milestones, and stabilize the software so that the subsequent deployments of the system (Pilot 2 and Waves 3, 4, and 5) may go forward, among other requests.
- **November 30, 2012**—The SAP issues its response to SCO's cure notice, denying responsibility for the Pilot 1 payroll inconsistencies and timeline delay. In addition, project staff indicate that SAP denies that their actions breach the original vendor contract.
- **February 8, 2013**—The SCO terminates its vendor contract with SAP and returns Pilot 1 employee payroll to the existing payroll system. At the same time, the California Technology Agency suspends the TFC project, citing the vendor's failure to finish the project and unwillingness to remedy the issues SCO presented in the cure notice.



Project Timeline and Status

(Continued)

- **March 2013**—The SCO begins efforts to run parallel payrolls on the new system and the existing system to identify inaccuracies in the previous eight months of payroll (the period the new system was operational) and ensure that no pay or benefit discrepancies are left unresolved, a process referred to as reconciliation.
- **June 2013**—Contractually mandated mediation between SCO and SAP begins.



Current Status

- The TFC project is reconciling payroll by comparing the pay and benefits processed using the new system to what employees should have been compensated using data from the existing system as a comparison point. This effort is expected to be complete by January 2014.
- The TFC project is also engaged in contractually mandated mediation.

Project Timeline

July 2003 – State chief information officer approves feasibility study for nation's largest payroll/human resources modernization to be known as the 21st Century Project.

May 2004 – Department of Finance approves feasibility study. Project begins with initial cost estimate of **\$132 million** and **mid-2009** completion date.

April 26, 2005 – Project contracts with SAP Public Services, Inc. for software, begins search for “integration vendor” to design, develop and deploy the software.

June 2006 – Controller Steve Westly signs contract with BearingPoint to serve as system integrator.

January 2007 – John Chiang sworn in as new State Controller. Replaces Steve Westly.

Oct. 19, 2007 – SCO issues “cure notice” to BearingPoint, declaring the system integrator in breach of contract and threatening termination.

Oct. 26, 2007 – BearingPoint responds with letter indicating that SCO is responsible for the project's delays and cost over-runs.

May 2008 –SCO, Department of General Services and BearingPoint agree to “rebaseline” the project, adding twelve months to the schedule. Cost increases to **\$179 million**, completion date pushed back a year, to **June 2010**.

January 2009 –SCO terminates BearingPoint contract.

February 2010 – Project restarts with SAP as system integrator, and is rescaled to eliminate California State University's 54,000 employees from project. Cost increases to **\$305 million**, completion date pushed back two more years, to **September 2012**.

Spring 2011 – Data conversion difficulties and other serious implementation issues emerge.

May 18, 2011 – SCO initiates “problem escalation process” for SAP’s alleged failure to resolve “contractually material issues.”

August 19, 2011 – SCO sends “cure notice” to SAP identifying primary problem as stalled data conversion.

Aug. 21, 2011 – SAP cure notice response notes “disagreement between SAP and the SCO as to the contractual responsibility for data conversion.”

Aug. 25, 2011 – Little Hoover Commission oversight hearing includes progress report on 21st Century Project. No mention of Aug. 19 cure notice.

Sept. 1, 2011 – Previously scheduled “go live” date can’t be met and is pushed back to March 2012.

Sept. 7, 2011 – SCO and SAP enter into confidential negotiations to resolve differences outlined in the August cure notice and SAP’s response.

Nov. 17, 2011 – Confidential negotiations between SCO and SAP yield a 39-page settlement agreement to resolve most differences and continue project with significantly higher state costs.

March 2012 – SCO requests an additional \$179 million, pushing the project’s cost to **\$373 million**. Completion date pushed back another year, to **September 2013**.

June 11, 2012 – Pilot1 goes live with SCO’s 1,300 employees, but numerous payroll check errors are noted by SCO.

Aug. 9, 2012 – Pilot 2, incorporating another 15,000 state employees and scheduled to start September 1, is postponed indefinitely because of recurring errors in Pilot 1.

Oct. 25, 2012 – SCO sends “cure notice” to SAP, initiating contract termination, and indicating “SAP’s breaches span the entire breadth of the contract from the project planning and project implementation, to the execution of the plans, and finally to the results.”

Nov. 30, 2012 – SAP response to cure notice states it “...has not breached the contract in any material respect and cannot be terminated for default.”

Feb. 5, 2013 – SAP issues demand for mediation to resolve project disputes.

Feb. 8, 2013 – SCO terminates the contract with SAP Public Services. At the same time, CTA suspends the project.

21st Century Project Action Summary

Action	Date of Approval by CTA	Amount Requested (millions)	Change from original request (millions)	Expected Implementation Date	Phase (Primary Vendor)	Background
FSR	May 14, 2004	\$132	n/a	2009	BearingPoint	Project to replace the legacy system used to pay 294,000 state employees.
SPR 1	April 11, 2004	\$138	\$6	6/2009		SPR adjusts project costs to reflect the procurement of BearingPoint as system integrator and SAP as software.
SPR 2	May 12, 2008	\$179	\$41	6/2010		SPR 2 extends project timeline due to data conversion issues discovered during early phases of project. Resolution between SCO, DGS and Bearing reached.
SPR 3	May 27, 2009	\$126	\$(-53)	6/2010	n/a	SPR 3 addressed project restart, which was necessary after terminating BearingPoint contract. Project scope changed – CSU employees removed.
SPR 4	December 16, 2009	\$305	\$179	9/2012	SAP	SPR 4 reflects SAP as the system integrator. Project costs increased reflecting change in project methodology and use of additional tools.
SPR 5	March 9, 2012	\$371	\$66	9/2013		SPR 5 required after encountering significant issues with data conversion. Data migration vendor brought onto project.