

Legislative Post Audit Performance Audit Report Highlights

Office of Information Technology Services: Reviewing the Office's Service Rates and Viable Alternatives for Its Services

Report Highlights

December 2013 • R-13-012

Summary of Legislator Concerns

Legislators had expressed a concern that OITS' rates for information technology and telecommunication services may be excessively high because it lacks any private sector competition.

Background Information

The Office of Information Technology Services (OITS) provides some centralized IT services and oversees others.

The 2013 Legislature passed House Bill 2200, which designated OITS as the state's sole provider of telecommunications and data processing services.

As a fee-funded agency, OITS has developed service rates to recover the costs of providing those services.

Federal law allows agencies to use federal funds to pay for the IT services OITS provides, but prohibits OITS from generating profits from those services.

QUESTION 1: Do OITS' service rates reflect actual costs and are they competitive with comparable services provided in the private sector?

- OITS' rates for many individual IT services do not reflect the actual cost of providing them.
- The rates agencies pay for some OITS services are inflated, because they include costs for other underfunded, discounted or waived services.
 - In fiscal year 2012, state agencies paid at least \$2 million in additional costs for underfunded services by paying higher rates for unrelated services.
 - Similarly, OITS has discounted or waived service fees for some state agencies.
 - OITS also includes an administrative fee on most rates which is used in part to cover costs for underfunded, discounted, or waived services.
- Although OITS has developed a complex rate model to help ensure rates reflect actual costs, it does not use the model to set most rates.
 - OITS has a complex rate model to allocate \$36 million in budgeted expenditures in fiscal year 2013 across more than 30 individual service rates.
 - However, in most cases, OITS staff manually set the rates for services rather than using the rates predicted by the model.
 - The manually entered rates can significantly differ from the rates calculated by OITS' rate model.
- Instead of setting rates to reflect actual service costs, OITS sets its rates to ensure budget and funding stability.
 - OITS does not adjust its rates to reflect actual costs because it wants to keep the rates stable for budgeting purposes.
 - OITS also sets its rates to ensure it has adequate funding for the entire agency, instead of setting rates to reflect the actual costs for individual services.

- OITS operates and sets rates with almost no oversight or accountability.
 - OITS' budget is not set through the appropriations process, and there is no legislative oversight of how OITS sets its service rates.
 - The Division of Budget reviews OITS' rates, but does not have the statutory authority to set them.
 - The only formal oversight of OITS is a limited review of its profits and losses by the U.S. Department of Health and Human Services.

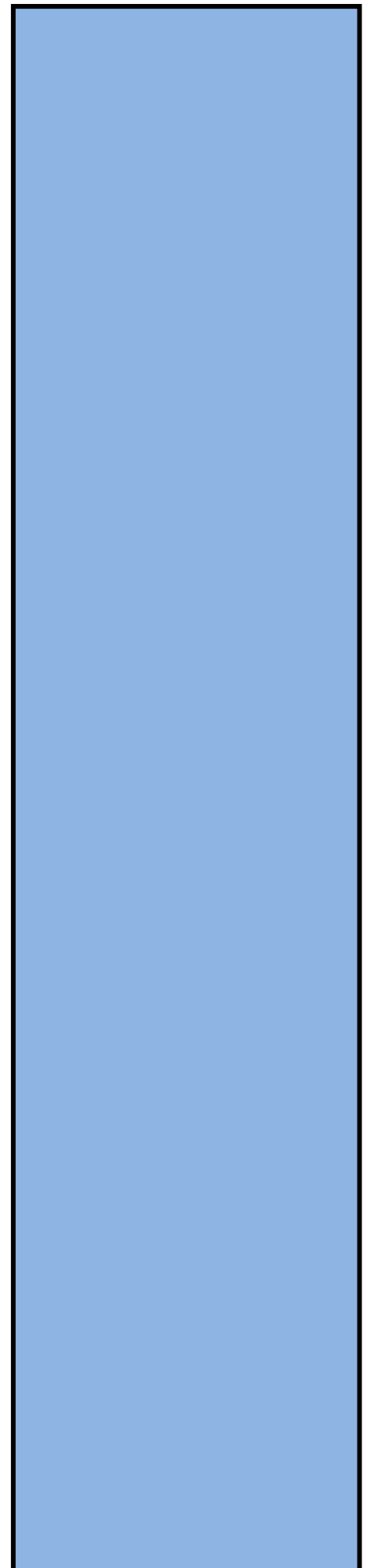
- We were unable to compare the rates OITS charges for its largest services to rates in the private sector.
 - Private sector companies track service usage, whereas OITS generally tracks service access.
 - The available information on private-sector rates for services that are comparable to those provided by OITS is limited.
 - A private-sector comparison has limited value because OITS' rates do not reflect actual costs.

Other Findings

- The way OITS has reported profits for individual services to the federal government appears to violate several federal reporting requirements.
 - Since fiscal year 2009, OITS (and its predecessor, DISC) have made approximately \$6 million in accounting adjustments to avoid reporting profits, which appears to violate federal regulations.
 - In addition, DISC and OITS have consistently used losses from prior years to offset current year profits, which also appears to violate federal regulations.
 - Because of these apparent violations, the state could be required to repay several million dollars in federal funds.

- We identified two additional issues that indicate an unstable fiscal situation at OITS.
 - OITS has had to borrow money and pay penalties to address short-term cash flow problems.
 - OITS and the Department of Administration have had to piece together funding to cover the ongoing operating costs of the state's new accounting system.

- Many of the issues we identified appear to be longstanding issues, some of which current management is trying to address.
 - OITS' current management inherited a complex and fragile rate model from DISC that is difficult to change.
 - The poor practices we identified with the current rate setting process appear to have existed for years.
 - OITS management appears to be trying to address some longstanding issues with its operations and rate setting process.



QUESTION 2: *What viable options exist for decreasing the cost of information technology and telecommunications services for state agencies?*

- Outsourcing, cloud computing, and consolidation are potential options for reducing the state's IT costs.
 - Many states have used these options to reduce IT costs.
 - OITS has taken some steps to consolidate and outsource IT services and is assessing opportunities for cloud computing to reduce IT costs.
- Outsourcing IT services can provide benefits, but requires strong contracts and vendor oversight for successful implementation.
 - Literature and interviews with state IT officials revealed that simple and stable systems such as email are services best suited for outsourcing.
 - At least eight other states including Kansas have outsourced various IT services.
 - States have reported benefits to outsourcing such as better service and cost savings, although few have verified those savings.
 - Some states that have outsourced IT services have faced significant setbacks in the process, including poor service and cost overruns.
 - Negotiating contracts and overseeing vendors are two of the most challenging aspects of outsourcing IT services.
 - Currently, OITS is not well positioned to outsource the state's IT services in their entirety because it is not in a position to determine if outsourcing would save money for agencies.
- Cloud computing offers many opportunities for savings but carries significant security risks.
 - In a 2012 National Association of State Chief Information Officers (NASCIO) survey, 71% of states reported using at least some cloud applications.
 - Moving applications to a cloud can save states money and help them keep pace with new technology.
 - Properly securing sensitive confidential data on a cloud service is challenging, but manageable.
 - OITS is in the process of implementing cloud services for a number of IT functions, including email.
- Although OITS has already consolidated some IT services, consolidating others may achieve further savings.
 - Many states reported they achieved savings through consolidation, but few have quantified those savings.
 - Consolidation can produce a number of other benefits such as improved service.
 - However, consolidation can also create an inflexible or generic service system that does not meet the needs of individual agencies.
 - OITS has consolidated some services such as the statewide network and most mainframe services.
 - OITS is currently in the process of consolidating some, but not all of the other services that it could.

Other Findings

- OITS does not have a process to ensure that costs are minimized and its rates are competitive.

SUMMARY OF RECOMMENDATIONS

Question 1 Recommendations:

- We made several recommendations to OITS to ensure its rates reflect actual costs and to ensure they are properly reporting profits and losses as required by federal regulations.
- We also recommended the Legislature consider action to ensure adequate oversight of the services OITS provides and the rates it charges.

Question 2 Recommendations:

- We recommended OITS continue to evaluate and transition services that are most suitable for outsourcing, cloud computing, and consolidation and should implement an efficiency management process.

AGENCY RESPONSE

The agency generally concurred with the report's finding, conclusions, and recommendations.

HOW DO I REQUEST AN AUDIT?

By law, individual legislators, legislative committees, or the Governor may request an audit, but any audit work conducted by the division must be directed by the Legislative Post Audit Committee. Any legislator who would like to request an audit should contact the division directly at (785) 296-3792.

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