Department of Veterans Affairs

Office of Inspector General

Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission

Oversight by VA's Franchise Fund Board of Directors should ensure payroll services contracts are signed before services are initiated and future problems are resolved in a timely manner.

Report No. 01-00256-157 **September 5, 2002**

VA Office of Inspector General
Washington, DC 20420

To Report Suspected Wrongdoing in VA Programs and Operations
Call the OIG Hotline – (800) 488-8244

DEPARTMENT OF VETERANS AFFAIRS
Office of Inspector General
Washington, DC 20420

Memorandum to the Associate Deputy Assistant Secretary for Management (004)

Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission

1. SUMMARY

The former Acting Assistant Secretary for Management requested that the Office of Inspector General (OIG) evaluate business operations between the Department of Veterans Affairs (VA) and the Federal Energy Regulatory Commission (FERC). The purpose of this evaluation was to assess the business and contractual relationships between VA and FERC for payroll services provided by VA's Franchise Fund, and to determine the cost of services provided to FERC and amounts reimbursed by FERC.

In December 1997, VA and FERC signed a contract under which VA would develop a payroll system for FERC using PeopleSoft software products. The contract provided that VA and FERC would negotiate a separate contract before beginning payroll operations, but VA began processing FERC's payroll in December 1998, without a contract.

VA and FERC conducted contract negotiations over approximately 2 years, during which time VA processed FERC's payroll without agreement on how much VA would be reimbursed. A contract for Fiscal Year (FY) 2001 payroll services was finally signed in February 2001. The business relationship between VA and FERC, including the difficulty negotiating a contract, was adversely impacted by VA's designation of successive managers to serve as the primary liaison with FERC, none of whom had line authority over the entire payroll process.

VA was inexperienced with PeopleSoft software products when it initially proposed providing payroll servicing for FERC. VA compensated for its inexperience with PeopleSoft software products by obtaining consultant assistance from Andersen Consulting for the technical requirements of implementing the software to service FERC's payroll. VA did not anticipate the additional difficulties and resource needs that were ultimately required to operate FERC's payroll.

From FY 1998 through FY 2000, VA spent approximately $7.5 million to purchase hardware and software; and to develop, implement, and operate a payroll system for FERC, for which VA was only reimbursed approximately $4.9 million by FERC. VA's Franchise Fund Board of Directors was not apprised of the problems VA encountered servicing FERC's payroll. Additionally, VA lost nearly $116,000 providing FY 2001 payroll services and until January 25, 2002, provided FY 2002 payroll services without a contract because VA and FERC could not agree on a price for payroll servicing.

2. BACKGROUND

The Government Management Reform Act of 1994 allowed Government agencies to join the Franchise Fund Pilot Program. The purpose of program is to provide common administrative support services to the agency and other agencies, for a fee that approximates the cost of the services. Franchise funds are accounted for separate from the agency's general funds by an intra-governmental revolving fund.

VA's Franchise Fund operates under a written charter approved by VA's Franchise Fund Board of Directors. The Franchise Fund has a VA Central Office (VACO) Enterprise Fund Office that oversees six Enterprise Centers:

- Financial Services Center (FSC) in Austin, TX
- Austin Automation Center (AAC) in Austin, TX
- Debt Management Center in St. Paul, MN
- Law Enforcement Training Center in Little Rock, AR
- Records Center and Vault in Neosho, MO
- Security and Investigations Center in Washington, DC

FERC is an independent regulatory agency within the Department of Energy (DOE). DOE and FERC had concluded that the PeopleSoft Human Resource Management System (PS/HRMS) could provide a Microsoft Windows-based, real time, user-friendly integrated human resource and payroll system product, and that an external service provider capable of interfacing with PeopleSoft would be necessary to develop and operate a payroll system.

VA wanted to establish a business line to provide franchised payroll services to other Government agencies. VA was also developing a new system, Human Resources (HR) LINK$, to integrate custom designed applications and PeopleSoft's commercial off-the-shelf Human Resource and Payroll software. Therefore, VA management believed that entering into an agreement with FERC to provide payroll services using PS/HRMS would be advantageous to VA in establishing the business line as well as implementing HR LINK$.

FERC concluded that among six potential providers, VA could implement an integrated system solution using PeopleSoft software in the shortest time frames. In December 1997, FERC and VACO representatives signed a contract for VA to develop a computer environment that could provide FERC payroll processing using PeopleSoft software. The contract provided that development would be completed by November 1998.

According to the contract, VA was to: (i) define hardware needs, (ii) acquire the hardware, (iii) establish FERC's PeopleSoft software on a platform at the AAC, (iv) convert FERC's personnel and accounting data to the new system, (v) load and update security and operational tables needed to activate the system, and (vi) establish payroll operations at VA's Shared Service Center (SSC) in Topeka, KS. The contract only covered establishing the payroll system, and did not address the cost of processing the biweekly payroll for FERC, which according to the December 1997 contract, was to be covered in a separate contract before payroll operations began. VA completed development of the PS/HRMS for FERC in December 1998 and began processing FERC's payroll without a contract on December 20, 1998.

3. SCOPE OF EVALUATION

To evaluate the business and contractual relationship between VA and FERC, determine the approximate cost of services provided to FERC, and identify amounts reimbursed by FERC, we:

- Interviewed VACO, AAC, FSC, SSC, FERC, Andersen Consulting, and Litton PRC employees.
- Assessed applicable VA policies and procedures, laws, regulations, financial records, and FERC related correspondence.
- Reviewed VA Franchise Fund Board of Director meeting minutes.
- Obtained copies of VA billings to FERC and Treasury documents supporting payments from FERC.
- Examined schedules of costs provided by AAC and FSC for developing, implementing, and servicing FERC payroll from FY 1998 through FY 2000.
- Analyzed VA's FY 2001 costs incurred according to FSC's activity based costing system.
- Reviewed FY 2001 payments to VA from FERC for services provided under the February 2001 contract.

The evaluation was conducted in accordance with generally accepted Government auditing standards for staff qualifications, independence, and due professional care; field work standards for planning, supervision, and evidence; and reporting standards for performance audits.

4. RESULTS OF EVALUATION

VA and FERC Contracts

In December 1997, VA and FERC signed a contract agreeing that FERC would pay VA costs to develop a PS/HRMS using PeopleSoft version 7.0. The contract estimated that actual costs would be between $775,143 and $1,185,829 to establish a PS/HRMS for FERC. The approximate $410,000 difference between the low and high estimated amounts resulted from the unknown costs for VA to establish interfaces with FERC personnel and accounting systems and PS/HRMS. Actual costs to develop the PS/HRMS exceeded the contract estimates primarily due to consulting service charges. FERC paid VA approximately $2.6 million to develop the PS/HRMS which included consultant costs of approximately $1.8 million, hardware costs of approximately $230,000, software costs of approximately $380,000, and approximately $150,000 for VA salaries, travel, and other costs incurred through December 1998.

VA completed development of the FERC PS/HRMS using PeopleSoft version 7.0 in December 1998, and although there were gaps in the PeopleSoft software requiring manual workarounds, VA began operating the system for payroll processing. The 1997 contract did not address the amount FERC would pay VA to provide biweekly payroll services, but stated that VA would “enact a separate interagency agreement for the operational aspects of VA’s cross-servicing arrangement with FERC before such operations are scheduled to commence.” VA processed FERC’s payroll based on the implied relationship from the development contract and the fact that FERC could not pay their employees without VA assistance.

From December 1998 until February 2001, VA produced FERC’s biweekly payroll and performed software upgrades without a contract defining the obligations of each of the parties, or how VA would be paid for payroll services. Although VA and FERC conducted contract negotiations over approximately 2 years, the parties did not agree on the amount VA was to receive for services until February 2001.

Successive VA Managers

The business relationship between VA and FERC, including the difficulty in negotiating a contract, was adversely impacted by VA's designation of successive managers to serve as the primary liaison with FERC. Responsibility for coordinating and negotiating with FERC shifted among successive VA managers, none of whom had line authority over the VA entities that were performing FERC payroll servicing.

In July 1997, VACO’s Assistant Deputy Assistant Secretary (ADAS) for Financial Systems was the initial liaison with FERC. In February 1999, the ADAS for Financial Systems designated the HR LINK$ Franchising Program Manager in VACO’s Business Development Support Services office to be the liaison with VA customers including FERC. Neither of these offices had line authority over the AAC and FSC. In November 1999, the Deputy Assistant Secretary (DAS) for Finance transferred liaison for FERC payroll servicing to the FSC Director, who did not have authority over AAC, the application services provider.

VA's business relationship with FERC and the servicing of the FERC payroll was also constrained by managerial and employee turnover during Calendar Year 2000. The former DAS for Finance, ADAS for Financial Systems, AAC Director, FSC Director, and other key VA employees working on FERC servicing either transferred to other Federal agencies or retired from Federal employment between February and November 2000. This managerial and employee turnover meant that the new managers and employees had to reestablish working relationships with FERC management.

PeopleSoft Software Product Implementation

In 1997, when VA initially proposed providing payroll servicing to FERC, VA was inexperienced with PeopleSoft software products. The 1997 contract stated that VA had contracts with consultants to support cross-servicing activities and that VA intended to employ a consultant to fulfill all or part of the work. VA and FERC planned to implement and use PeopleSoft version 7.0 to process FERC's payroll. FERC requested that VA employ Andersen Consulting, as a consultant, in the implementation of PS/HRMS because FERC had previously employed Andersen Consulting for advice concerning FERC decisions on payroll. FERC was in the process of securing additional Andersen Consulting services for counseling on human resource and payroll matters, and FERC believed Andersen Consulting's significant expertise with PeopleSoft software products would facilitate success. Andersen Consulting was also providing consulting services for VA's HR LINK$ project.

As Andersen Consulting had separate contractual relationships with VA for both the HR LINK$ and FERC payroll processing as well as with FERC for human resource and payroll matters, they potentially had conflicts of interests in fulfilling each of their consulting roles. VA managers told us that Andersen Consulting staff communicated more fully with FERC managers regarding development and installation of the PeopleSoft payroll products than with VA managers, although Andersen Consulting's contract was with VA.

Andersen Consulting customized the PeopleSoft software and processing of FERC's biweekly payroll was successful, but manual workarounds were still needed because of gaps in the PeopleSoft software where it did not process pay records correctly or meet Federal Government payroll requirements. PeopleSoft version 7.0 workarounds included manual adjustments to ensure military leave balances were carried forward, life insurance premiums were computed properly, and balances on U.S. Savings Bond deductions were properly refunded to employees if they terminated the bond election.

VA used time and materials contracts and task orders to obtain services from Andersen Consulting for installation of PeopleSoft version 7.0. This contracting methodology based compensation on Andersen Consulting's level of effort and did not require the delivery of specific end products, which made it difficult for VA project managers to hold Andersen Consulting accountable for specific deliverables. AAC and FSC managers told us that Andersen Consulting received payment for their PeopleSoft version 7.0 development services without providing VA full documentation of PeopleSoft system design changes they made or the standard operating procedures they developed.

PeopleSoft version 7.0 was used to process FERC's payroll beginning in December 1998. However, FERC desired additional PeopleSoft software modules that were only available by upgrading to PeopleSoft version 7.5. In March 1999, VA and FERC agreed to upgrade to PeopleSoft version 7.5. The 1997 contract had stated that VA would develop and assess separate charges for additional tasks, such as upgrades to new PeopleSoft software.

AAC changed consultants and contracted with Litton PRC for consulting services to develop the upgrade to PeopleSoft version 7.5. From March through August 1999, AAC, with consulting assistance from Litton PRC, planned, customized, and tested PeopleSoft version 7.5, but VA never installed it to process FERC's payroll due to unresolved problems with the software, including errors on tax withholding and life insurance premiums. VA, Litton PRC, and PeopleSoft were expending efforts to correct problems with version 7.5 when PeopleSoft announced that it would release version 7.51. PeopleSoft advised VA in August 1999 that it would no longer support version 7.5 after December 1999. PeopleSoft recommended that VA and FERC use their newly issued version 7.51.

Version 7.51 was released in October 1999. Version 7.51 included the additional PeopleSoft modules FERC wanted in version 7.5 which VA and FERC had planned to implement by September 1999. VA, with consultant assistance from Litton PRC, installed PeopleSoft version 7.51 to replace version 7.0 payroll processing in November 1999. According to VA and FERC managers and employees, the conversion to PeopleSoft version 7.51 was performed hastily, without a dedicated FSC team leader and without being sufficiently tested by VA or FERC prior to placing it into production. FERC managers complained to us that due to the insufficient testing, there were problems with timekeeping and human resource functions. For example, Standard Form 50s were not processed for 3 months, and it took 8 months to resolve problems with some employee leave records.

Approximate Cost of Services Provided to FERC

We concluded that VA's cost to develop and provide payroll services to FERC for FYs 1998 through 2000 totaled approximately $7.5 million. From FY 1998 through FY 2000, VA did not have a cost accounting system to separate costs incurred servicing FERC's payroll from other operating costs. At our request, AAC and FSC provided separate schedules of amounts collected from FERC and costs VA incurred developing and operating FERC's payroll system.

AAC's and FSC's schedules of costs that they believed VA incurred servicing FERC payroll totaled approximately $5.2 million. The schedules were accompanied by qualifying statements that they were not intended to detail all costs associated with

FERC, should not be used as a VA estimate of costs incurred, and were not used as a basis for VA billings to FERC.

We tested the cost schedules for omissions, duplications, errors, and verified these costs by examining VA payments to consultants, employee timesheets, and billings to FERC. We also compared the cost schedules AAC and FSC provided to their schedules of collections.

We found that the collection schedules included FERC payments for Andersen Consulting services, but the cost schedules excluded these amounts, totaling approximately $2.3 million. We also noted other minor omissions and overstatements in the cost schedules. We estimate the total cost to VA was approximately $7.5 million, and concluded that the net additional costs were approximately $2.3 million, and that this was due primarily to the omission of payments to Andersen Consulting. We cannot provide assurance that there are not other significant costs or adjustments that VA failed to include in their cost schedules. We provided our estimate of additional costs to AAC and FSC representatives and they concurred that the estimate was reasonable.

Amounts Reimbursed by FERC

FSC provided us a schedule of FERC payments totaling $4,898,872 and copies of billing documents sent to FERC. We verified the FERC payments with VA financial records and supporting Treasury documents. As shown below, for the period of FY 1998 through FY 2000, FERC reimbursed VA $4,898,872. This is approximately $2.6 million less than the cost to VA to purchase hardware and software for FERC, and to develop, implement, and process FERC payroll.

Fiscal Year	VA Costs	VA Billings[1]	FERC Payments	Costs in Excess of Collections
1998 & 1999	$4,795,338	$4,530,778[2]	$4,248,872	$ 546,466
2000	2,688,795	650,000	650,000	2,038,795
Total	$7,484,133	$5,180,778	$4,898,872	$2,585,261

We estimated that VA's costs exceeded collections by $546,466 for FYs 1998 and 1999. Of this amount, AAC's Director told us that $516,560 was "transition cost." The Director stated that VA did not bill FERC for the $516,560 costs because VA's HR LINK$ program benefited from the expenditures. We could not determine why VA did not bill FERC for the remaining $29,906 in FYs' 1998 and 1999 costs ($546,466 - $516,560).

We concluded that VA's costs exceeded collections by $2,038,795 for FY 2000. VA and FERC disagreed on how much FERC should pay for payroll services. VA did not invoice FERC for FY 2000 payroll services during FY 2000. FSC's Chief of Accounting,

[1] VA billings and payments are listed by the fiscal year that the services were performed in, and not necessarily the year in which the bills were issued or the payments were received.

[2] VA billings to FERC exceeded FERC payments by $281,906 due to FERC refusing to pay a March 1999 invoice. VA did not document how the March 1999 unpaid invoice was resolved nor could VA representatives recall why collection of the $281,906 was not pursued. Our examination determined that of the $281,906, hardware charges of $191,350 were duplicated from a previous billing that FERC had already paid. Therefore, VA was only entitled to $90,556 of the unpaid invoice.

Reconciliation, and Reports Section stated that invoices were not issued to FERC because without a signed contract to define what services were to be billed and how much to charge for them, they did not know how much to invoice. In October 2000, VA and FERC negotiated a payment of $650,000 for FY 2000 services. The ADAS for Financial Operations advised us that less than VA's full costs were accepted because the lack of an existing contractual agreement made the negotiating position of VA very weak. Consequently, VA negotiated what it believed to be the best agreement it could with FERC, after the fact, which was based on the best cost and financial information available at the time.

VA Franchise Fund Board of Directors Oversight

The VA Franchise Fund Board of Directors is responsible for approving user fees and charges, and identifying and approving actions to resolve Franchise Fund operating problems. The VA Franchise Fund Board of Directors meeting minutes from October 1998 until February 2001, when the contract for FY 2001 services was signed, did not mention any discussion of problems with FERC payroll processing. Managers who attended the meetings confirmed that problems between VA and FERC were not brought to the Board's attention by the former DAS for Finance or the former AAC and FSC Directors. Office of Management officials advised us that, during the summer and fall of 2000, the former Acting VA Chief Financial Officer, who was also Chairman of the VA Franchise Fund Board of Directors, held meetings regarding the FERC payroll processing problems. The meetings included, at various times, the former DAS for Finance and the former AAC and FSC Directors.

5. FISCAL YEARS 2001 AND 2002 OPERATIONS

On February 26, 2001, VA and FERC signed a contract defining services to be provided, billing and payment arrangements, and a price for FY 2001 services. The contract estimated the total cost to FERC for FY 2001 to be $943,772. The contract provided that FERC would reimburse VA the actual costs of Litton PRC consultant assistance estimated at $114,000 and AAC technology management estimated at $277,248. The contract also provided that FERC would pay FSC a firm fixed price of $552,524 for management and administration.

On January 24, 2002, FSC management provided actual year-end FY 2001 operating results from their Itemized Unit Cost Report. According to this report, FSC's own costs to service FERC payroll were $668,442 for FY 2001. This was about 121 percent of FSC's $552,524 firm fixed price portion of the FERC servicing contract and resulted in a net loss of $115,918.

On September 4, 2001, FERC transferred application services from AAC to a commercial provider. FERC was responsible for payment for application services provided by the commercial provider. On January 25, 2002, FSC and FERC signed a contract for FY 2002 services in which FERC agreed to pay FSC $665,011 for PS/HRMS services, plus actual costs for any travel or information technology costs incurred.

VA's Franchise Fund Board of Directors should initiate oversight of payroll services provided to FERC to ensure contracts for future years are issued timely and more closely monitor Enterprise Center activities.

6. RECOMMENDATIONS

We recommend that the Associate Deputy Assistant Secretary for Management:

a. Require signed contracts between VA and FERC for payroll services for future years before initiating services.

b. Require the VA Franchise Fund Board of Directors to initiate oversight of payroll services provided to FERC so that any future problems are resolved in a timely manner.

c. Require the VA Franchise Fund Board of Directors to monitor more closely Enterprise Center activities to better identify and resolve problems with client agencies.

7. COMMENTS OF THE ASSOCIATE DEPUTY ASSISTANT SECRETARY FOR MANAGEMENT

The Associate Deputy Assistant Secretary for Management concurred with the recommendations and provided acceptable implementation plans. Appendix A contains the full text of the comments and includes a "Lessons Learned" summary prepared by the FSC. We will follow up on planned actions until they are completed.

For the Assistant Inspector General for Auditing

(original signed by:)
WILLIAM H. WITHROW
Director, Kansas City Audit Operations Division (52KC)

Department of Veterans Affairs

Memorandum

Date: JUL 1, 2002

From: Associate Deputy Assistant Secretary for Management (004)

Subj: Draft Report, Evaluation of Business Operations between VA and the Federal Energy Regulatory Commission

To: Assistant Inspector General for Auditing (52)

Attached are the Office of Management's comments and responses to the subject report. Please note that the attachment includes a "Lessons Learned" summary prepared by the Financial Services Center. Should you require additional information, please call me at 273-5583 or have a member of your staff contact Rom Mascetti, ADAS for Financial Operations, at 273-9441 or Steve Swanson, Director, Enterprise Fund Office, at 273-9413.

(signed)
William H. Campbell

Attachment

Response to Draft Report, Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission (FERC)

RECOMMENDATIONS (page 9)

Inspector General Recommendation 6a. Require signed contracts between VA and FERC for payroll services for future years before initiating services.

> **Office of Management Response:** Concur. The Financial Services Center began FY 2003 contract negotiations with FERC in May 2002, which included services to be performed and roles and responsibilities. All contracts for payroll services between VA and FERC will be signed before services are initiated.

Inspector General Recommendation 6b. Require the Franchise Fund Board of Directors to initiate oversight of payroll services provided to FERC so that any future problems are resolved in a timely manner.

Inspector General Recommendation 6c. Require the Franchise Fund Board of Directors to monitor more closely Enterprise Center activities to better identify and resolve problems with client agencies.

> **Office of Management Response:** Concur on 6b and 6c. The Enterprise Centers will provide quarterly reports to the board through the Enterprise Fund Office that describe the status of all agreements. The Enterprise Fund Office will ensure—through these reports—that the board is made aware of issues that impede the finalization of Franchise Fund service level agreements administered by the respective Enterprise Centers.
>
> **Implementation Plan:**
>
> Enterprise Centers will make their initial annual baseline report to the board in November 2002. Quarterly updates will be provided to the Board in January 2003, April 2003, and July 2003.

Response to Draft Report, Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission (FERC)

Financial Services Center
Lessons Learned in
Processing PeopleSoft Payroll for FERC
June 12, 2001

In 1996, VA began marketing PeopleSoft payroll and application management services to external federal agencies. Simultaneous with those marketing efforts, the Department of Energy (DOE) decided to discontinue in-house payroll services and outsource their payroll function. DOE was providing payroll services to the Federal Energy Regulatory Commission (FERC). Upon notification that DOE was going to discontinue payroll services, FERC initiated a review of potential payroll providers willing to interface with the PeopleSoft suite of federal software products. FERC was aware of VA's marketing efforts regarding HR LINK*$* services and the PeopleSoft application and contacted VA about providing payroll and application management services to FERC.

In 1997, FERC selected VA to provide implementation, payroll processing, and application management services for their PeopleSoft software. An Interagency Agreement for implementation services was signed. VA participated in the implementation of the PeopleSoft software and began providing production payroll processing and application management services to FERC using the federal PeopleSoft product in December 1998.

VA encountered numerous problems on the FERC PeopleSoft project; however, valuable lessons were learned regarding the provision of payroll services to external federal agencies:

- **Define one project owner and document issues and agreements.**
  The Financial Services Center (FSC) is the current owner of the PeopleSoft payroll product line. However, the FSC did not become the owner of the product line until December 1999. From early 1996 through December 1999, there was no single, continuous VA organizational owner of the product line. In fact, as many as five separate VA organizations had responsibility for the project (HR LINK*$* program office, Office of Finance Business Development and Support Service, Austin Automation Center (AAC), Shared Service Center (SSC), and FSC). Multiple owners of the project led to a lack of accountability, continuity and responsibility. This left an information void each time the project switched owners. FERC asserted that different VA organizations made various promises to FERC regarding pricing, responsibilities and service offerings, but the lack of ownership continuity and documentation made it impossible to validate those promises. Better documentation on all meetings, issues, agreements, and disagreements is essential to ensure consistent treatment if a project changes ownership or if there are management changes on the project.

Response to Draft Report, Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission (FERC)

- **Ensure software is mature and stable prior to offering production payroll services.**
  VA offered payroll and application management services to FERC using an immature software product. FERC was the first federal agency to implement the federal PeopleSoft payroll system, and as a result, encountered numerous quality issues with the software. VA aggressively pursued software patches and fixes from the vendor, but the vendor was often unresponsive. FERC was dissatisfied with the service/performance they received due to VA's inability to fix the software or pressure the vendor to fix the software. VA did not have any leverage with the vendor since FERC owned the PeopleSoft licenses.

- **Obtain signed contractual agreements that include clearly defined roles and responsibilities, performance measures and metrics, and dispute resolution processes.**
  Franchise contractual agreements were not in place when FERC payroll went live in December 1998. When attempts were made—subsequent to implementation—to create agreements between VA and FERC, negotiations always failed due to disagreements over pricing, disputes over promises supposedly made during implementation, and unclear roles and responsibilities. A lack of performance measures and metrics also led to continuous disputes between FERC and VA over payment for services rendered. Since the dispute resolution process was not defined and no agreement was in place, there was no structured method to resolve these disputes.

- **Develop clear business plans for product lines, not just individual projects**.
  Business planning is essential to any product line. Business plans define pricing strategies, breakeven points and marketing strategies. They define infrastructure and excess capacity, and identify potential economies of scale. Business plans also address start-up costs and making capital investments.
  On the FERC project, PeopleSoft application deficiencies resulted in VA paying contractors to remedy production-critical issues. The customer refused to pay the contractor costs because they understood these costs were part of the "total solution" VA offered. FERC also stated that, in offering payroll and technology services under the franchise concept, they were led to believe VA would aggressively pursue other customers in order to lower the overall cost of services. They were also led to believe VA would absorb substantial start-up costs and recover them from several customers over several years. Since there was no clear business plan for the product line, we were unable to adequately handle the costs associated with the start-up of the product line or the costs associated with fixing basic software deficiencies. There was no plan regarding breakeven points or breakeven timeframes. Without a business plan, VA also did not have a marketing strategy to obtain additional customers that would offset costs for FERC.

Response to Draft Report, Evaluation of Business Operations Between the Department of Veterans Affairs and the Federal Energy Regulatory Commission (FERC)

- **Determine core business competencies and only offer services within those competencies.**
  VA struggled to provide comprehensive payroll and application management services to FERC. VA incurred significant expense to offer the application management aspect of PeopleSoft services to FERC with limited positive results. In fact, FERC repeatedly voiced their dissatisfaction with VA services, but this was a direct result from the immaturity of the software and the associated application deficiencies. Since information technology is not the FSC's core business, we were reluctant to provide application management services. Therefore, FERC has contracted with Accenture for these services.

- **Promote open communication and professional, non-confrontational relationships.**
  Excellent communication has turned a dissatisfied customer into a satisfied customer. In the past, communications between FERC and VA were often confrontational and lacking in full disclosure or understanding of each other's position. This resulted in a dysfunctional relationship. Stressing more open communications, especially at the senior executive level, and working hard towards a better professional customer/client relationship between the FSC and FERC has significantly improved customer satisfaction. We now clearly articulate our position on issues and work cooperatively to ensure a satisfactory resolution between both parties.

Bottom Line: The FSC has made significant progress in improving customer relations with FERC. Now a satisfied customer, FERC employees often commend VA payroll services. Recent strides in improving our working relationship can be attributed to identifying the lessons learned above and correcting those issues. For example, the FSC is the product line owner for the FERC project; therefore, our responsibilities are now clear. We also have a signed franchise agreement for the first time with performance measures and metrics. The FSC has made significant progress in business planning and activity-based costing which has improved our ability to appropriately price our services. By stressing a more professional, non-confrontational relationship with FERC, improved communications and customer satisfaction have resulted.

Report Distribution

VA Distribution

Secretary (00)
Deputy Secretary (001)
Executive Secretariat (001B)
Chief of Staff (00A)
General Counsel (02)
Assistant Secretary for Public and Intergovernmental Affairs (002)
Principal Deputy Assistant Secretary for Management (004)
Assistant Secretary for Information and Technology (005)
Assistant Secretary for Policy and Planning (008)
Deputy Assistant Secretary for Congressional Operations (009C)
Deputy Assistant Secretary for Public Affairs (80)
Director, Management and Financial Reports Service (047GB2)
Director, Austin Automation Center (200/00)
Director, Financial Services Center (104/00)

Non-VA Distribution

Office of Management and Budget
General Accounting Office
Congressional Committees (Chairmen and Ranking Members):
  Committee on Governmental Affairs, U.S. Senate
  Committee on Veterans' Affairs, U.S. Senate
  Subcommittee on VA, HUD, and Independent Agencies, Committee on Appropriations, U.S. Senate
  Committee on Veterans' Affairs, U.S. House of Representatives
  Subcommittee on Oversight and Investigations, Committee on Veterans' Affairs, U.S. House of Representatives
  Subcommittee on VA, HUD, and Independent Agencies, U.S. Committee on Appropriations, U.S. House of Representatives
Staff Director, Committee on Veterans' Affairs, U.S. House of Representatives
Staff Director, Subcommittee on Oversight and Investigations, Committee on Veterans' Affairs, U.S. House of Representatives

This report will be available in the near future on the VA Office of Audit Web site at http://www.va.gov/oig/52/reports/mainlist.htm**, *List of Available Reports*. This report will remain on the OIG Web site for 2 fiscal years after it is issued.**