



State of South Carolina
Office of the Inspector General

Memorandum

Date: September 1, 2015

To: Honorable Nikki R. Haley, Governor
Honorable Hugh K. Leatherman, Senate Pro Tempore
Honorable James H. "Jay" Lucas, Speaker of the House of Representatives
Honorable Richard Eckstrom, Comptroller General
Honorable Curtis M. Loftis, State Treasurer

From: ^{psm} State Inspector General Patrick J. Maley

Re: South Carolina State Government's Performance Management System – An Untapped Tool Pivotal to Improving State Government

The purpose of this memorandum is to share my observation that state government has an inadequate statewide agency performance management system (PM-System), and a renewed emphasis in a statewide PM-System represents the single best opportunity to address waste in state government.

Problem

In 2004, South Carolina state government had the foresight to forge ahead in the difficult and challenging endeavor of a statewide PM-System requiring each agency to produce an Annual Accountability Report (AAR). The AAR provided a quality framework and guidance, albeit a bit cumbersome by current standards, using criteria for organizational excellence established by the Malcolm Baldrige National Quality Award Standards. However, the envisioned organizational performance tool designed to promote evidenced based management and rigorous data to discern agency performance has fallen short. While some agencies have seized the benefits of the AAR to effectively drive their operations, it has evolved for many other agencies into a superficial annual exercise or more of a self-serving marketing tool. Further, the AAR has no capability to integrate agency results data into a holistic picture of statewide government for policy makers or the public.

The good news is state government leaders have recently made significant strides in their emphasis on oversight and accountability as demonstrated by establishing the Department of Administration; new Legislative oversight mechanisms with dedicated staff; and an improved AAR format by the new Executive Budget Office refocusing on measurable results. Despite this positive energy, more oversight and external audit are helpful, but are secondary to an effective PM-System. An effective PM-System stimulates agency performance improvement, enhances the 7000 Executive Branch managers' evidence based management skills, and provides reliable information meeting the common needs of many stakeholders, to include leveraging the efforts of oversight and audit.

Performance management in state government today is similar to Information Security's (INFOSEC) posture before the 2012 Breach. Every agency conducted INFOSEC, with most feeling they were adequate. The reason agencies felt adequate was because they had no rigorous standard to compare themselves against. After the breach, when basic INFOSEC standards were applied to each agency by the consultant Deloitte & Touche, agencies' "feelings" were replaced by "evidence" demonstrating they were not near as adequate as they felt. I suggest state agencies' performances (results) are not nearly as good as its managers think for the same reason -- the state has not established an effective PM-System to develop rigorous agency performance standards.

In direct terms, agencies select their own success metrics and decide on their own benchmarks/standards to measure success, all without the state taking the time to systematically analyze this performance system and corresponding data to discern if it is accurate, reliable, and fair. A declining agency can go unnoticed because the state has little capacity to scrutinize and discern, let alone challenge, AAR reports containing inaccurate/nonsensical performance data or hollow management jargon creating the impression of a well-honed operation. As evidence, just look at some recent agencies' AARs the year before a major public failure.

Solution

The direction for improvement is a renewed emphasis for an effective PM-System to reinforce the management fundamental to focus on outcomes/results. This should not be viewed as a burden or additional cost; this is how organizations should be expected to operate. Building a PM-System focused on specific strategies, tactics, and measurable results, *along with an audit function to ensure accurate and reliable data* (IG emphasis added), is the cornerstone to improve state efficiency and effectiveness. Nothing improves efficiency and effectiveness, and correspondingly addresses waste, like clear measurable accountability for results. Further, clear accountability standards sets expectations for the human condition to strive to achieve, as well as motivation in knowing falling short will be noticed. This will also save time for oversight and audit by tapping into a single, uniformed, and reliable performance data source. More importantly, it will establish a standard from which oversight and audit actually need prior to conducting an effective review.

PM-System Stimulates Change

An effective PM-System stimulates change because it specifies measurable priorities. The gravity of the status quo and the difficulty in change management is well understood by anyone who has ever led a significant change effort. However, it does not get much simpler than the words from President Woodrow Wilson, "If you want to make enemies, try to change something." Measurable priorities stimulates managers down the simple path of "what gets measured, gets done," and conversely, what does not get measured creates the visibility requiring managers to question the status quo.

From a longer-term perspective, it has been my personal experience over the past three years that state agencies feel stretched thin, if not overburdened. Absent a crisis, change initiatives for downstream improvements have a tendency to get put on a "wish" list rather than a "to do" list. Just about every significant issue identified in an IG review requiring action was, at some level, previously known to the agency. Between the myriad of real or perceived daily crises and the lack of realizing an immediate benefit from acting on an unaddressed significant problem/opportunity, it is easy to kick the can down the road because CHANGE IS HARD. Over the past ten years a common best practice has been to broaden organizational performance systems to set forth planned, but unrealized, change initiatives in organizational strategy documents, such as the balanced scorecard. This concept should be incorporated into the state's AAR to get required changes on the "to do" list, which then creates the visible accountability on change initiatives requiring longer time frames to monitor these initiatives crossing multiple fiscal years.

Change initiatives are not only inherently hard, the problem is exacerbated by the state not providing any systematic management training to develop and nurture these skills. The reality is managers are often selected for, particularly entry level, technical reasons and interpersonal ability, but the hard core management skills,

primarily process, project, and program management, are not provided in any systematic manner which just contributes to the gravity of the status quo. In a recent IG review, a front line supervisor, a staff manager, and an agency head were proactively wrestling with the need to streamline an agency which lost over half of its staff since the recession, yet still was operating much like it did five years ago. Highly motivated state employees knew change was needed, but really had little experience, skills, or confidence to address the issue. Other states deploying aggressive PM-Systems realized they also have to systematically train their managers in process management to provide the tools and common operating expectations to stimulate meaningful and lasting change.

In the IG's view, effectively managing a government entity has a greater need for a PM-System because it is inherently more difficult to manage than in the private sector. The private sector has a single metric that can drive management action---profit or loss. It is a singular barometer to stimulate management introspection on operational effectiveness and improvement opportunities. On the other hand, measuring effective and efficient government, which often produces intangible services, is much more difficult requiring measuring many more factors along with the difficulty in developing comparable benchmarks to accurately gauge levels of success. Further, agency management gets to select its own metrics and comparative benchmarks which the state has no capability to validate. I would submit positive change in government is more a function of the quality of an agency's leader/culture or external stimulation based on a public mistake/controversy than on systematic evidence based planned change.

Glimpses from the Frontline on the State's Current PM-System

For those in state government familiar with the AAR, this memo likely only confirms their suspicions or conclusions. To assist those less familiar, below are several examples to illustrate the current conditions on the ground:

- A small agency failed to produce an AAR in two of the past five years, and the three AARs produced were virtually boilerplate copies lacking meaningful performance data. Yet, this agency's budget has nearly doubled. A cursory review of this agency identified substantial deficiencies with meeting its statutory mission.
- An agency's AARs for years were essentially fictitious in describing a strategic plan with metrics, which literally did not exist. This agency asserted, in a recalcitrant manner, it was so unique the agency did not require basic performance measures for its operations, nor could it develop benchmarks for success because it was not comparable to any other entity. In reality, this agency operated in a highly benchmarked industry which would have long ago exposed this agency's systemic weaknesses if its AAR required standardized industry reporting.
- A review of the most recent AARs (FY 2013 – 2014) for the 17 state universities revealed a high level of variability in reporting results. Success metrics reported by each university varied from six to 145, with a mean and average of 18 and 34, respectively. Eight (47%) universities did not report the standard four & six year graduation rate metrics; five (29%) reported the more favorable six year rate; and only four (24%) reported both graduation rates. Five (29%) universities provided tuition cost comparison data, while only one (6%) reported job placement results. The U.S. Department of Education has identified this same higher education transparency and accountability issue at a national level. It recently required the following mandatory national metrics in stark contrast with the status quo to be used in 2015 to distribute federal financial aid: graduation rates; affordability; student outcomes; and access. Some states have already established a common performance metric baseline for state universities to establish expectations and measure progress, such as Kentucky's five strategic objectives with 27 metrics which also has an emphasis on addressing the national problem of higher dropout rates for low income and minority students (<http://cpe.ky.gov/NR/rdonlyres/76B3B3E7-489E-4972-BDF7-F2203215CAF8/0/AccountabilityReport201213.pdf>).

Interestingly, Kentucky's program is titled, "Stronger by Degrees," which captures the spirit of continuous improvement through meaningful outcome measurements.

The state's universities high variability indicates their self-reported AAR performance data lacks a standardized approach to select the key strategic performance metrics, as well as a tendency to select metrics for marketing purposes or with questionable value indicating strategic performance. Absent selecting fair, objective, and the right metrics indicative of progress against stated strategic goals, the strategic planning process loses its value in producing meaningful information to manage, analyze to stimulate improvement, and facilitate oversight efforts. To illustrate the power of standardized results, the public accounting profession has developed a standard index to measure a university's financial condition known as the Composite Financial Index (CFI). If this was required in state universities' AARs, it would have revealed a recent state university's financial difficulties four years before its current crisis rather than surfacing only after the university literally ran out of money.

- Despite a general consensus of the user community that AARs have low utility, there are many examples of quality AARs which provide clear strategic objectives and equally clear, credible metrics of success providing an effective framework to manage operations, as well as provide confidence to oversight and the public of taxpayer value. With the risk of singling out a specific agency, the Department of Employment Workforce's FY 13-14 AAR is an example of success. Even though its results are unaudited, the appropriateness and specificity of the results data creates credibility and could be easily verified.

There have also been recent examples where oversight has openly, and rightfully, challenged the system as to why catastrophic agency problems were not identified earlier. I would submit the problems had been identified by agencies, but the state does not have a system requiring agencies affirmatively present data in a rigorous performance based framework that will sufficiently focus attention to the problem to stimulate hard questions and action. The state has an overflow of data, but not the right data, validated through audit testing, in the right format to facilitate consistent and meaningful analysis on performance which stimulates positive change.

Lessons can be learned from the state of Indiana's recently initiated PM-System designed to be a "comprehensive enterprise wide data management system that establishes an accurate reporting of agency performance standards to promote efficient, transparent and effective government." As its initial step in 2014, Indiana conducted an assessment of each state agency's current performance management capabilities. This review determined agencies were at different levels of readiness and had significant issues with measure validity and methodology. The review acknowledged agencies were all "measuring something," but questioned if agencies were measuring the right things and using their performance measures to manage their operations. The report concluded it will take "significant changes, effort, and education" for the state to move from its current environment to an effective PM-System. I would submit if a similar review was conducted in South Carolina state government, the results would be the same.

Where to Start?

An adequate PM-System requires not only a better process, but also must be properly staffed. A staff, located in the DOA, would serve as subject matter experts to help agencies develop and mature their strategic planning, execution, and reporting through formalized training and day-to-day collaboration. Equally important, this staff would scrutinize AAR submissions, provide feedback, and coordinate audit testing to provide assurance of the system's data accuracy. This same staff would play a key budget role, particularly the ability to probatively examine data supporting new funding requests and the agency's consideration given to internal reprioritization options. All these efforts, when combined, creates the expectation, as well as the attitude and motivation, for agency managers to truly embrace the capabilities of a substantive strategic planning process to manage operations, which then stimulates all levels of management to focus on strategy, work processes, and

measurable outcomes. The bi-product will be agencies ability to submit accurate AARs capable of being relied upon to make better decisions in the budget process.

To start momentum to build an adequate statewide PM-System, I would recommend the Executive Branch leadership leverage its existing internal audit workforce, estimated between 120-150 professionals, to move away from traditional low risk compliance and financial audits and follow the private sector trend towards improving operational performance through improving risk management, control, and governance processes. This moves internal audit to focus on a top down approach of auditing to assess, improve, and ultimately provide independent assurance that agency management has an adequate strategic planning, execution, and a measurement system. Then, systematically work down through the organization with emphasis on leaning out processes based on a risk-based approach and ensuring results are aligned with objectives. South Carolina spends an inordinate amount of accounting and audit energy, time, and money providing assurance to taxpayers every dollar is tracked, but it lacks an adequate capability to provide assurance to taxpayer of the effectiveness (results/outcomes) of tax dollars spent.

I would then look internally to reallocate existing resources to this higher statewide PM-System priority by redirecting as many of the 120-150 executive branch internal auditors as needed to the DOA. Their skills would support a PM-System through analyzing or coordinating audits of the AARs, followed by bringing to bear their background to assess/scrutinize agency budget requests to development the Governor's annual Executive Branch budget proposal. These internal auditors collective impact on state effectiveness would be astronomically higher, and I can think of no better cost/effective option to reduce waste in state government.

In summary, it is recommended the state strategically locate a robust analytical/audit capability at the singular interface between agencies and the political budget process in the Executive Budget Office, DOA. An effective PM-System well-staffed would then be able to leverage and mature the capabilities of the 7000 Executive Branch managers through process planning, training, and budget feedback/scrutiny to have a heightened focus on results and a continuous improvement mindset. Maturing agencies PM-Systems to support/drive managing agencies to higher levels of effectiveness is a multi-year, long-term effort.

Lessons from Other State's PM-Systems

Fortunately, several other states have blazed the PM-System trail. I encourage you to review the Virginia state government's performance management website (<http://vaperforms.virginia.gov/>), because it may help you visualize how a PM-System tool can really support improved state government and public support through transparency and access to meaningful performance information. Virginia's PM-System starts at the most logical place—identifying the statewide priorities and corresponding performance measures the public expects (economy, health, crime, etc.), which are then cross-walked to the agency(s) responsible and result metric. Agency results can be further “drilled down” in increasing detail from a metrics scorecard, to an agency executive progress report, and then to a comprehensive biennial strategic plan. Indiana has likely the most relevant lessons for South Carolina inasmuch as it only recently initiated its statewide PM-System (<http://www.in.gov/mph>). Washington State (<http://www.results.wa.gov/>) and Ohio (<http://www.lean.ohio.gov/>) emphasize process management training designed for results and culture change towards continuous improvement, which then supports agency-wide strategic planning and results measurements. Ohio's process improvement efforts have resulted in, on average, a 50% reduction in process steps; a 50% reduction in time of service; \$160 million in savings; and higher workforce satisfaction by taking ownership of simplifying their work.

It also may be helpful to read a summary of Virginia's journey, challenges, and benefits from developing its PM-System, with particular notice of how Virginia's starting performance management posture resembles South Carolina's present conditions (<http://www.nascio.org/awards/nominations/2009/2009VA3-NASCIO%202009%20VA%20DIKM%20VA%20Performs.pdf>).

Closing

There are definitely sparks of interest in this PM-System issue throughout South Carolina state government. However, with the press of daily business, it is tough to get “one more issue” in the cue for action. I hope this memo to the most influential state leaders serves as a catalyst for action.

Please don't hesitate to contact me for any questions or provide me your input (803/896-4721). Thank you in advance for your interest in this important issue to improve South Carolina state government.

cc: Chairman W. Brian White, House Ways & Means Committee
Chairman Wm. Weston J. Newton, House Oversight Committee