

# INVESTIGATIVE AUDIT REPORT

COMMUNITY HEALTH NETWORK, INC.

JANUARY 1, 2007, THROUGH DECEMBER 31, 2009



## State of Tennessee



**Comptroller of the Treasury  
Department of Audit  
Division of Municipal Audit**



STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Justin P. Wilson

Comptroller

STATE CAPITOL

NASHVILLE, TENNESSEE 37243-9034

PHONE (615) 741-2501

July 7, 2011

Commissioner Mark A. Emkes  
Tennessee Department of Finance and Administration  
and  
Chief Executive Officer and Members of the Board of Directors  
Community Health Network, Inc.  
765 Florence Road  
Savannah, TN 38372

Ladies and Gentlemen:

Presented herewith is the report on our investigative audit of selected records of Community Health Network, Inc. This investigative audit focused on the period January 1, 2007, through December 31, 2009. However, when warranted, this scope was expanded. The Information Systems Audit Section of the Division of State Audit assisted investigators with data recovery and retrieval.

The Comptroller has prescribed a minimum system of recordkeeping for nonprofit agencies, which is detailed in the *Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*. The purpose of our audit was to determine the extent of the entity's compliance with certain laws and regulations, including those in the above-mentioned manual.

Our investigative audit revealed possible criminal conduct related to the former chief executive officer and former assistant director in their failure to account for or misspend funds totaling at least \$1,266,395.

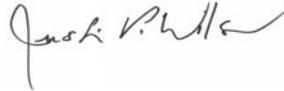
The former chief executive officer of Community Health Network, Inc., and the former assistant director acted together to give themselves unauthorized benefits totaling \$80,862 and \$10,200, respectively. These matters have been referred to the local district attorney general.

Our investigative audit also identified several significant issues related to Community Health Network, Inc.'s management of grant funds. Finally, we included in this report findings and recommendations related to those conditions that we believe warrant your attention.

Commissioner Mark A. Emkes  
Tennessee Department of Finance and Administration  
and  
Chief Executive Officer and Members of the Board of Directors  
Community Health Network, Inc.  
July 7, 2011

Copies of this report are being forwarded to Governor Bill Haslam, the State Attorney General, the District Attorney General, certain state legislators, and various other interested parties. A copy is available for public inspection in our office and may be viewed at [www.comptroller1.state.tn.us](http://www.comptroller1.state.tn.us).

Very truly yours,

A handwritten signature in black ink, appearing to read "Justin P. Wilson", written in a cursive style.

Justin P. Wilson  
Comptroller of the Treasury



**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY  
DEPARTMENT OF AUDIT  
DIVISION OF MUNICIPAL AUDIT**

**Justin P. Wilson**  
Comptroller of the Treasury

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**Dennis F. Dycus, CPA, CFE, Director**  
Division of Municipal Audit

July 7, 2011

Mr. Justin P. Wilson  
Comptroller of the Treasury  
State Capitol  
Nashville, TN 37243-9034

Dear Mr. Wilson:

As part of our ongoing process of examining the records of nonprofit organizations, we have completed our investigative audit of selected records of Community Health Network, Inc.. This investigative audit focused on the period January 1, 2007, through December 31, 2009. However, when the examination warranted, this scope was expanded. The Information Systems Audit Section of the Division of State Audit assisted investigators with data recovery and retrieval.

The Comptroller has prescribed a minimum system of recordkeeping for nonprofit organizations, which is detailed in the *Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*. The purpose of our audit was to determine the extent of the entity's compliance with certain laws and regulations, including those in the above-mentioned manual.

Our investigative audit revealed possible criminal conduct related to the former chief executive officer and former assistant director in their failure to account for or mispend funds totaling at least \$1,266,395.

The former chief executive officer of Community Health Network, Inc., and the former assistant director acted together to give themselves unauthorized benefits totaling \$80,862 and \$10,200, respectively. These matters have been referred to the local district attorney general.

Mr. Justin P. Wilson  
Comptroller of the Treasury  
July 7, 2011

Our investigative audit also identified several significant issues related to Community Health Network, Inc.'s management of grant funds. Finally, we included in this report findings and recommendations related to the following:

1. Inadequate separation of duties
2. Failure to maintain required accounting records
3. Inadequate and incomplete equipment inventory
4. Failure to budget for or allocate recurring costs

If after your review, you have any questions, I will be happy to supply any additional information which you may request.

Sincerely,

A handwritten signature in black ink, appearing to read "Dennis F. Dycus". The signature is fluid and cursive, with a large initial "D" and "F".

Dennis F. Dycus, CPA, CFE, Director  
Division of Municipal Audit

**INVESTIGATIVE AUDIT OF SELECTED RECORDS OF  
COMMUNITY HEALTH NETWORK, INC.  
FOR THE PERIOD JANUARY 1, 2007, THROUGH DECEMBER 31, 2009**

**EXECUTIVE SUMMARY**

**Background**

Community Health Network, Inc. (CHN), is organized under section 501(c)(3) of the Internal Revenue Code as a Tennessee not-for-profit corporation incorporated on January 30, 2002, to assist other not-for-profit medical service providers in sharing business services and technology. In 2009, the entity had 17 member hospitals, clinics, and other health care organizations. Member organizations operated approximately 100 clinic sites. CHN also provided health care technology services to nonmember, not-for-profit health care providers, including rural hospitals.

CHN's stated mission is to provide affordable medical technology to rural communities without ready access to specialized medical services. CHN operated a network of computer and video equipment which allowed a doctor or nurse in a remote clinic to transmit scans, images, and test results to a medical specialist in a major medical center hundreds of miles away. CHN also operated computer information systems to assist hospitals and clinics in transferring their paper medical records and prescriptions into an electronic data base. CHN operated as a pathway for grants from the Tennessee Department of Finance and Administration (TDFA) to health care groups (such as East Tennessee State University (ETSU) Physicians and Associates, Meharry Medical Group, and Cherokee Health Systems). CHN also accepted grants from federal, state, and nongovernmental sources, including the BlueCross BlueShield of Tennessee Health Foundation (THF).

This investigative audit was initiated after TDFA's Office of Internal Audit contract review concluded that CHN failed to provide adequate documentation that it had fulfilled or satisfied the terms of the contract and as a result, owed the state reimbursement of \$628,948.

The matter was referred to the Comptroller of the Treasury, who initiated an investigative audit which focused on the period January 1, 2007, through December 31, 2009. The scope of the investigation was expanded when warranted.

**Result of Investigative Audit**

Our investigative audit revealed possible criminal conduct related to the former chief executive officer (CEO) and former assistant director in their failure to account for or mispend funds totaling at least \$1,266,395. In addition, we discovered the following major deficiencies in the agency's internal controls:

## **Legal Issues**

The former CEO and former assistant director gave themselves unauthorized benefits totaling at least \$80,862 and \$10,200, respectively.

## **Significant Grant Issues**

The former chief executive officer and assistant director of CHN falsified grant invoices, grant reports, and misused grant proceeds from a state grant to purchase unauthorized software. CHN officers accomplished this by using legitimate grantee requests to secure such funds without passing the reimbursements on to the proper recipients (i.e. ETSU Physicians and Associates).

CHN failed to properly process and manage a state grant. As a result of CHN's failure to fulfill its responsibility, qualified and eligible organizations did not receive the assistance they had been promised.

CHN overbilled the state \$131,163 for a computer software purchase related to a state-administered federal grant. Grant participants did not utilize the \$1.47 million computer information system purchased by CHN with these grant funds.

CHN could not account for at least \$446,712 of the \$1,800,000 received from THF. Our audit revealed that CHN failed to properly account for, bill, and pay for the recurring costs of telecommunication lines incurred by CHN member organizations. In order to satisfy that debt, CHN officers intentionally and falsely overbilled THF and used at least \$246,000 of the unearned funds on these expenses not related to the BlueCross Foundation grant.

The former CEO and assistant director obtained grant funds totaling at least \$478,621<sup>1</sup> by presenting fraudulent and/or misleading information, then used the grant money to negotiate two software purchases from a software vendor. During the period of his employment, the former CEO received money from the same software vendor for promoting the sale of the vendor's products and subsequently became a paid consultant to the vendor.

## **Findings**

CHN did not adequately separate incompatible duties of its employees.

CHN did not maintain required accounting records.

CHN did not maintain adequate and complete equipment inventory.

CHN failed to budget and plan for recurring costs, such as software maintenance and telecommunication line fees.

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<sup>1</sup> This is a total of \$347,458 from Issue #1 and \$131,163 from Issue #3.

<b>Summary – Unaccounted for and Misspent Funds</b>			
<b>Grant</b>	<b>Category</b>	<b>Amount</b>	<b>Status</b>
Grant GR-08-23603 (Physician Connectivity Grant to promote electronic prescription software)	Funds not spent for grant purpose ( <i>grant advance, unauthorized software purchase</i> )	\$ 597,458	(owed to state)
East TN Perinatal Project (computer & video equipment to link rural caregivers to specialists)	Unaccounted for funds <sup>2</sup> ( <i>overbilled THF to cover past-due internet bill and other miscellaneous expenses unrelated to this grant</i> )	446,712	(owed to THF)
Grant GR-08-23150 (Health Information Exchange Network)	Funds received in excess of actual expenses ( <i>for software purchase</i> )	131,163	(owed to state)
Keith Williams	Unauthorized salary and benefits ( <i>Theft</i> )	80,862	(owed to CHN)
Paul Monroe	Unauthorized salary and benefits ( <i>Theft</i> )	<u>10,200</u>	(owed to CHN)
	<b>Unaccounted for/misspent total by CHN</b>	<b><u>\$1,266,395</u></b>	

<sup>2</sup> These funds are labeled “unaccounted for” because CHN has not accounted for \$446,712 of the grant proceeds. CHN received \$1,800,000 from THF as a part of the East Tennessee Perinatal Telemedicine Demonstration Project. However, their records indicated that they spent, at most, only \$1,027,886 on legitimate, grant-related expenses. As of July 2, 2010, CHN had only \$325,402 cash on hand; therefore, at least \$446,712 was spent on noneligible expenses.

**LEGAL ISSUES**

1. **ISSUE:      Unauthorized benefits of former chief executive officer and former assistant director**

The former chief executive officer of CHN, Ronald (Keith) Williams<sup>3</sup>, and the former assistant director, Paul Monroe<sup>4</sup>, acted together to provide themselves unauthorized benefits totaling at least \$80,862 and \$10,200, respectively.

Mr. Williams and Mr. Monroe ordered unauthorized payroll payments to themselves in the form of unapproved and unauthorized bonuses. In addition, Mr. Williams used the agency’s credit card for his own personal expenses and for expenses he submitted to other agencies as a paid consultant. Mr. Williams also purchased equipment and other items that he did not return to CHN upon his resignation and was paid for unauthorized expenses that had no supporting documentation. We also noted several instances in which Mr. Williams claimed a per diem meal expense allowance, but charged a meal on the agency credit card on the same day.

<b>Unauthorized Benefits for Keith Williams</b>	
<b>Category</b>	<b>Amount</b>
Unauthorized personal purchases on agency credit card	\$39,021
Unauthorized salary	18,192
Equipment and other items not returned to agency	11,706
Other unauthorized and unsupported expense claims	<u>11,943</u>
<b>Total</b>	<b><u>\$80,862</u></b>

<b>Unauthorized Benefit for Paul Monroe</b>	
<b>Category</b>	<b>Amount</b>
Unauthorized salary	\$10,200

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<sup>3</sup> On January 25, 2010, Mr. Williams notified the executive committee of CHN by e-mail of his immediate resignation from his position of chief executive officer.

<sup>4</sup> Mr. Monroe was terminated from his employment with CHN on March 5, 2010.

## SIGNIFICANT GRANT ISSUES

Our investigative audit revealed that CHN received grant funds from federal, state, and not-for-profit foundations, but failed to maintain adequate accounting records documenting the amount of funds received and expended for each individual grant. Grant revenue was improperly recorded when it was received rather than when it was earned. The organization also failed to maintain accurate and current asset records related to the grants. Our examination revealed that CHN either misspent or could not account for at least \$1,266,395 in grant funds.

1. **ISSUE: CHN failed to account for \$250,000 advance payment, obtained \$347,458 for ineligible expenditures for a combined total of \$597,458, and submitted false or misleading documents for a physician connectivity grant**

Our investigative audit revealed that CHN received a \$250,000 advance related to a grant but failed to account for the advance. In addition, CHN officials submitted a grant reimbursement claim, and were paid \$347,458 for unauthorized and disallowed computer software. The software was never used to further the grant purpose.

In December 2007, the TDFA designated CHN as the organizational contact for all state not-for-profit applicants for the state's Physician Connectivity Grant<sup>5</sup>. CHN obtained a grant in February 2008, to promote and finance the use of electronic prescriptions by physicians. According to the terms of the grant, a hospital, clinic, or physicians' group could obtain some of the grant funds from CHN if the qualified physicians agreed to write prescriptions using computer software for at least two years. The grant contract allowed CHN to pay each medical group \$3,500 per qualified physician. According to the grant, each medical group could seek reimbursement from CHN for qualified expenses related to electronic prescriptions.

In July 2008, CHN was reimbursed \$347,458<sup>6</sup> by the state for the purchase of 85 software licenses. However, according to the grant contract, CHN was authorized to qualify and pay medical groups for physician participation, not to acquire software. Our investigative audit also revealed that the documentation submitted by CHN for the software was a price quote, not an invoice, and the actual payment was only \$289,549<sup>7</sup>. Finally, CHN paid the software vendor<sup>8</sup> in installments, so when the initial request for payment was made to the state, CHN had actually only paid \$116,516. Of the 85 software licenses purchased by CHN under the grant, only five software licenses were put into

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<sup>5</sup> Grant Contract GR-08-23603

<sup>6</sup> CHN actually submitted a claim of \$386,065 for this software; however, as per agreement, the state was to pay 90 percent of expense claims, while the other 10 percent would be deducted from the balance of the advance.

<sup>7</sup> CHN failed to make the last of four payments for the software. CHN also incurred additional maintenance fees, which were not eligible grant costs and were not claimed as part of the grant. These fees are in dispute with the vendor.

<sup>8</sup> The circumstances of the software purchase prompted further inquiry into the relationship between the former executive director of CHN and the software vendor. **Refer to Issue 4.**

service. Those five software licenses were not used by physicians qualified under the connectivity grant.

CHN failed to reimburse eligible providers according to the terms of the grant. Therefore, it appears that CHN officials inappropriately requested and received \$597,458<sup>9</sup> of grant funds for which it was not eligible.

<b>Unaccounted for Amounts Paid to Community Health Network</b>	
<b>Expense Category</b>	<b>Amount</b>
Advance	\$250,000
Software	<u>347,458</u>
<b>Total</b>	<b><u>\$597,458</u></b>

2. **ISSUE:** CHN failed to process applications for funds from physician connectivity grant

Our investigative audit determined that CHN failed to properly process at least \$749,000 in eligible connectivity grant applications. We identified several medical groups that applied for Physicians Connectivity grants through CHN but were never funded. CHN was responsible for ensuring that each medical provider applying for funds had a valid agreement with qualified physicians and could document actual expenses from the purchase of approved computer software and related expenses. CHN was supposed to forward the documentation to the state. Our examination indicated that certain medical groups properly provided all required and requested documentation of their compliance with the grant; however, CHN failed to properly submit that documentation to the state and as a result, these providers were never allotted the grant funds for which they were qualified.

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<sup>9</sup> CHN was paid an additional \$64,050 under this grant for salaries, travel, supplies, and equipment. However, since CHN failed to perform its role under this grant, these costs could be questioned by the state as well. That would make the total of questioned items \$661,508. CHN's internal review proposed that payments to several medical providers which were not properly submitted to TDFA should partially offset any amount owed to the state. According to our review, that would violate the terms of the grant contract.

<b>Eligible Grant Applicants That Received No Grant Reimbursement</b>	
<b>Medical Group</b>	<b>Eligible to Receive</b>
ETSU Physicians and Associates	\$437,500
Meharry Medical Group <sup>10</sup>	206,500
Cherokee Health Systems	87,500
Rural Medical Services	17,500
<b>Minimum Total in Eligible Grant Funds not Processed</b>	<b><u>\$749,000</u></b>

#### East Tennessee State University Physicians and Associates

The executive director of East Tennessee State University Physicians and Associates (ETSU Physicians), in Mountain Home, Tennessee, signed a contract with CHN in May 2008. According to the TDFA, the physicians group was eligible for up to \$437,500 in grant funds for 125 qualified physicians. ETSU Physicians submitted invoices to CHN for reimbursement from the grant in September 2009 and December 2009. In January 2010, CHN's former executive director notified the ETSU Physician's executive director that all necessary documentation had been received and was being processed. However, ETSU Physicians never received funds under the connectivity grant. Our investigative audit revealed that previously, in a June 2008 invoice to the state, CHN had fraudulently used the names of 75 qualified physicians from ETSU Physicians, along with a price quote for a software purchase of NextGen ePrescribe software, to obtain \$347,458 in connectivity grant funds. (Refer to Issue 1.) In fact, the ETSU physicians had obtained their own software, as provided for in the grant contract; they never used the NextGen software purchased by CHN. ETSU Physicians never received connectivity grant funds for which they were eligible.

#### Meharry Medical Group

Although Meharry Medical Group, in Nashville, Tennessee, properly applied through CHN for funds under the connectivity grant, we were unable to find any documentation that CHN properly submitted their documentation. In a letter to Meharry Medical Group dated August 13, 2009, CHN's former chief executive officer advised the group that CHN was processing their application for \$301,000 in grant funds. However, our investigative audit revealed nothing in CHN or state records that supported the former CHN official's claim. Meharry Medical Group officials told state auditors that they had

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<sup>10</sup> According to records with the state Department of Finance and Administration, Meharry Medical Group was eligible to receive at least \$206,500 based on the number of qualified and approved practitioners. We have reviewed documentation from Meharry Medical Group which indicates Meharry may have been eligible for additional grant funds. An August 13, 2009, letter from CHN's former CEO informed Meharry Medical Group that \$301,000 in grant funds was in process. We have used the amount of \$206,500 in grant funds Meharry was eligible to receive as a minimum.

relied on that reassurance that their request was in process. The group never received connectivity grant funds for which they were eligible.

### Cherokee Health Systems

Cherokee Health Systems (Cherokee), in Knoxville, also applied for funds from the state grant through CHN. TDFA determined that Cherokee was eligible to receive \$87,500. Cherokee officials stated that they incurred at least that amount in implementing electronic prescription records. CHN's former assistant director acknowledged in a written communication to Cherokee that CHN owed \$84,000 from the connectivity grant. However, our investigative audit determined that CHN never submitted proper documentation from Cherokee to the state and, as a result, Cherokee never received connectivity grant funds for which they were eligible.

### Rural Medical Services

CHN's own internal review also concluded that Rural Medical Services was eligible to receive \$17,500 under the connectivity grant. Our examination determined that the organization did not actually receive funds.

### 3. **ISSUE: CHN overclaimed \$131,163 on a \$1.47 million computer information system grant and then failed to utilize the system**

Our investigative audit determined that CHN asked for and received \$131,163 more from a TDFA-administered federal grant<sup>11</sup> than it had expended. In addition, the \$1.47 million computer information system paid for with these grant funds was not utilized.

In 2008 and 2009, CHN received \$1.47 million in grant funds to install computer software and equipment to provide doctors in four participating hospitals with ready access to medical information about any patient who had visited any one of the participating medical providers. The purpose of the grant was to improve medical care through quick access to patient information. TDFA administered the federal grant on behalf of the Tennessee Department of Health. According to CHN's financial records, CHN paid \$131,163 less than the amount it had requested and received for the computer software.

A consultant hired by CHN evaluated the grant project in January 2010. According to the consultant's evaluation, the system was fully operational at the completion of the grant on December 31, 2009. However, the system was not actually being used. Participants were not able to negotiate and sign agreements to share data with each other. Participants also could not or would not pay the \$22,000 per month license and support costs. As a result,

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<sup>11</sup> GR-08-23150 Health Information Exchange Network Grant

at the time of our audit, the computer information system that cost more than \$1.47 million in taxpayer money was not being used by the participants.

4. **ISSUE: East Tennessee Perinatal Telemedicine Demonstration Project**

Our investigative audit revealed that in at least one instance, CHN officials claimed and were reimbursed for the same purchase with grants from two separate sources, a THF and federal grant. The CHN officials also inflated the cost of equipment in their financial records, and used THF grant funds for nongrant expenditures, all totaling at least \$446,712.

In November 2008, the THF awarded \$1.8 million to CHN. The grant's objective was to significantly improve outcomes for high-risk pregnancy and to reduce the rate of premature births in rural areas of the state. Regional Obstetrical Consultants, a physicians group, was selected to provide medical services. The grant funded the acquisition of advanced technology equipment for rural clinics in East Tennessee and the electronic connection of those clinics with the area's two regional perinatal centers in Knoxville and Chattanooga. Computers and video equipment were purchased to allow perinatal specialists to confer with rural family practitioners, obstetricians, and patients.

CHN deposited the first of three \$600,000 payments from the THF in December 2008. CHN's grant budget included \$334,750 for a Gateway bridge server. However, CHN actually purchased that item in January 2009 at a price of only \$294,000. In addition, all but \$80,794 of the purchase price had been paid by a federal grant previously received. As a result, CHN officials not only overstated the cost of the equipment by more than \$40,000, they also attempted to charge the cost of over \$213,000 to both the THF grant and a separate federal grant.

According to the contract between CHN and THF, the second payment of \$600,000 to CHN was to be made on or before December 31, 2009. In an e-mail dated August 6, 2009, CHN's chief executive officer notified his assistant director that he wanted the money from the THF much sooner than December 31. "I just hit BC up for our next \$600K," he wrote. However, related bank transactions revealed that CHN officials intended to use the THF funds for other than grant purposes. The second installment of \$600,000, received in October 2009 was not deposited into the agency's operating bank account but placed into an account at a different bank which had a balance of less than \$6,000. That same day, CHN issued checks on the account of more than \$246,000 to cover past-due bills not related to the THF grant.

In an e-mail on January 8, 2010, Paul Monroe, the former assistant director of CHN admitted to CHN's board president, "We had to 'borrow' from our cash balance to pay the year to date TNii connectivity bills to keep AT&T from terminating the circuits as we had not paid those AP invoices while waiting for the State reimbursements."

<b>Tennessee Health Foundation Grant to Community Health Network</b>	
Grant funds received	\$1,800,000
<b>Less expenses:</b>	
CHN Administration <sup>12</sup>	(300,000)
Computers and communication equipment purchased with THF funds	(324,341)
Phone lines and other connection charges	(45,165)
Payments to Regional Obstetrical Consultants for doctors and nurse practitioners	(349,649)
Contingency funds used	(8,731)
<b>Expected funds remaining</b>	<b>772,114</b>
Cash available as of July 2, 2010	<u>325,402</u>
<b>Shortage</b>	<b><u>\$ (446,712)</u></b>

5. **ISSUE: Community Health Network – Questionable relationship with software vendor**

While employed by CHN, the former CEO made efforts to further the interests of a software company, NextGen Healthcare Information Systems. CHN paid a total of \$805,531.21 to NextGen for software and maintenance from which CHN was improperly reimbursed at least \$478,621<sup>13</sup> by the state.<sup>14</sup>

CHN received a reimbursement from the state of \$347,458 for 85 software licenses. However, the documentation submitted to the state was a price quote, not an actual invoice. Our investigative audit revealed that CHN actually made periodic payments to the software vendor totaling only \$289,549. Our investigative audit also revealed that previously, in June 2008, CHN had used the names of 75 qualified physicians from ETSU Physicians, names of physicians from other groups, and a price quote for a software purchase of NextGen ePrescribe software, to obtain \$347,458 in connectivity grant funds from the TDFA.

Our investigative audit determined that the former CEO:

- had apparently intended to purchase NextGen software even before CHN had received a grant from the state. On December 17, 2007, the former CEO obtained a price quote

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<sup>12</sup> The budget for the three-year grant included \$300,000 for CHN administration. In July 6, 2010, CHN reported that all \$300,000 allocated for administration had already been spent in half of the grant term. However, CHN’s own records indicate administrative expenses were only \$157,240. Due to its mishandling of grant funds and lack of candor to the grantor, it is not clear that CHN would be entitled to *any* administrative costs. Therefore, our use of \$300,000 for these costs was only to calculate a minimum shortage. Any amount less than \$300,000 that CHN used for administrative costs would increase the shortage.

<sup>13</sup> This is a total of \$347,458 from Issue #1 and \$131,163 from Issue #3.

<sup>14</sup> Refer to Subsequent Event following Issue # 5.

which he would eventually use to obtain grant funds. CHN was not awarded the grant until February 6, 2008;

- falsely advised his board in January 30, 2008 that one of the grants allowed CHN to “purchase the NextGen software to facilitate the NextGen EMR (electronic medical records) system.” The grant terms actually required CHN to reimburse medical providers for their participation;
- signed a contract on March 31, 2008, obligating CHN to purchase 85 physician software prescription licenses from NextGen;
- submitted false or misleading information to the State of Tennessee; consequently, CHN improperly obtained at least \$478,621 in state funds for two separate software purchases from NextGen;
- maintained a close relationship with the software vendor. In July 2008, NextGen officials advised the former CEO that they believed he had earned a fee for helping sell their software to a Nashville physicians group. That month, NextGen officials took the former CEO to an Atlanta Braves baseball game;
- signed a finder’s fee agreement with NextGen in January 2009, to become a private consultant for the software company so that he could receive referral fees
- was paid \$10,000 in March 2009 for helping NextGen sell software;
- informed NextGen officials, in May 2009, of his plans to “gradually disentangle” himself from his full-time position as CEO of CHN in order to become a paid consultant to NextGen. He wrote in an e-mail to NextGen officials:

As I also mentioned, I do not plan on being a ‘Vendor-Neutral’ Consultant, first because I don’t believe there are any, but primarily because a large part of what I have to offer potential clients are my relationships that I’ve developed over the years. With that in mind, I would hope that NextGen would consider supporting my efforts in the months and years to come.... My proposal to NextGen, which I will also be making to another complementary vendor group, is for support in an annual amount of \$50,000.

- became a regular paid consultant to the company in October 2009; and
- notified the executive committee of CHN by e-mail on January 25, 2010, of his immediate resignation from his position as CEO.

**Subsequent Event**

On November 30, 2010, CHN owed NextGen \$302,536 for software and maintenance fees. CHN disputed that amount and requested a refund on previous fees and purchases. NextGen apparently agreed to a partial refund of certain software and maintenance fees on the condition that CHN make another major software purchase. On December 30, 2010, with the approval of CHN's board, CHN's CEO signed an agreement for another NextGen software purchase totaling \$866,461. The agreement required CHN to make an 80 percent payment on the new purchase in order to get a refund on previous fees and purchases. The new software purchase was dependent on a federal grant – that grant award has been placed under review. CHN submitted a request for reimbursement for the purchase under the grant but the request was not approved. CHN has not made a payment on the new purchase and has not received a refund. NextGen has issued some credits for returned software and added some charges for maintenance fees. As of May 31, 2011, CHN owed NextGen \$489,622, according to NextGen records.

## **FINDINGS AND RECOMMENDATIONS**

Our investigative audit identified the following internal control conditions which contributed to the failure to detect and correct errors and misstatements on a timely basis.

In preparing our Findings and Recommendations, we noted that the Independent Auditor's Report for CHN's comprehensive annual audit for the fiscal year ending December 31, 2009, raised doubt about CHN's ability to continue to operate as a going concern. Our investigative audit has also revealed additional issues and more uncertainty about CHN's ability to continue operations.

In a December 10, 2010, special meeting of the Board of Directors of Community Health Network, the board's attorney explained why he thought bankruptcy was not a practical option. "... he determined it was not practical to file bankruptcy due to the expense a bankruptcy trustee would incur to maintain the medical records that are private and confidential."

CHN's board discussed the need to evaluate CHN's core mission and values before the adoption of the 2010 budget. A budget for 2010 was never adopted. According to the minutes of a special board meeting on December 10, 2010, CHN's board of directors decided to develop a plan to "wind down" the operations of the organization and transfer CHN's assets and operations to other organizations.

### 1. **FINDING: Inadequate separation of duties**

General: The former chief executive officer directed major purchasing decisions, financial reporting, and even individual accounting transactions. In addition, the board provided no oversight over the former chief executive officer's travel and other expenses. Finally, the former CEO had influence over the preparation of the board meeting minutes.

Major purchases: Major purchasing decisions, including the purchase of NextGen software, were made by the former CEO without adequate deliberation or review by the board.

Financial reports and transactions: Under the direction of the former CEO, the former assistant director prepared multiple financial reports to present to CHN's board of directors. Important elements of those reports, such as unpaid bills and other liabilities, were sometimes removed at the former CEO's direction before presentation to the board.

Unsupervised travel and expense: Supervision of the former CEO was limited to a review of his travel claims by the president of CHN's board. However, in February 2009, although he continued to be paid for travel, the former CEO stopped submitting his travel claims to the former president of the board. This issue was not discovered until after the resignation of the former CEO. In addition, there was no board review of the former CEO's use of the organization's credit card.

Content of board meeting minutes: The former assistant director and CHN employees prepared the minutes of the meetings of the board of directors and executive committee. The former assistant director then submitted draft minutes to the former CEO for approval prior to delivering them to the board.

*Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*, page 2-1, states that the accounting system should meet five objectives essential to the collection, maintenance, and fair presentation of financial data including Objective 4:

Establish controls that provide management with reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are recorded properly and executed in accordance with management's authorization.

**RECOMMENDATION:**

To decrease the risk of undetected errors and irregularities, members of the board of directors should review employees' responsibilities to ensure that no employee has control over a complete transaction.

2. **FINDING:**    **Failure to maintain required accounting records**

The organization failed to maintain separate, complete, and accurate accounting records for grants and restricted contributions. CHN could not provide state auditors with details of the amount of funds received and expended for each grant. The organization also failed to maintain an accurate and complete asset account for each restricted grant or contribution.

*Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*, page 5-8, states:

You should have a deferred revenue control account with a subsidiary ledger for each government contract your organization is awarded. For each donor restricted grant or contribution your organization receives, you will need a separate net asset control account.

**RECOMMENDATION:**

To provide information for the assessment of the organization's financial position and to facilitate compliance with grant requirements, members of the board of directors should

ensure that adequate accounting records and other documentation are prepared and maintained.

3. **FINDING: Inadequate and incomplete equipment inventory**

CHN did not maintain adequate records of equipment purchased and did not perform an annual physical count of assets. Current inventory records were compiled after the resignation of the former CEO and former assistant director. *Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*, page 6-15, states that the organization must maintain internal controls which include a perpetual inventory record periodically balanced to both control accounts as well as periodic physical inventories.

**RECOMMENDATION:**

To better control and account for individual fixed assets and high-risk, moveable property, members of the board of directors should ensure that an annual inventory is properly performed and documented.

4. **FINDING: Failure to budget for or allocate recurring costs**

Our investigative audit determined that CHN management failed to plan for or allocate certain recurring costs. Using state and federal grant funds, CHN operated computer information systems and telecommunication networks which allow medical specialists in urban medical centers to communicate with doctors and nurses providing medical care for disadvantaged and rural patients. (Refer to Issues 3 and 4.) The cost of operating the telecommunications equipment included monthly fees of more than \$30,000 for special telecommunication lines. CHN charged some of the health care providers for these ongoing fees. However, CHN utilized a grant to cover these costs for CHN members. When the grant funding ran out in 2009,<sup>15</sup> CHN did not begin assessing members for the costs. CHN continued to incur these large charges; they simply did not pay them. In October 2009, the telecommunication vendor threatened to suspend service. Apparently as a result of that threatened action, CHN officials shifted grant funds provided specifically for other purposes to pay a portion of those bills and maintain operations. In January 2010, CHN's former assistant director notified several board members that CHN had failed to bill for most telecommunication charges and had used THP grant funds to

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<sup>15</sup> CHN's former CEO apparently advised CHN board members and employees that the State of Tennessee would continue to reimburse CHN for telecommunication lines until a Federal Communications Commission grant took over payment for that expense. However, we found no indication that any official from the State of Tennessee made any such commitment of state funds.

prevent a discontinuation of service. CHN's board did not attempt to recover funds from medical providers which were not billed for connectivity expenses in 2009 and early 2010. CHN officials did examine the telecommunication bill and eliminated unwanted or unused connections. In April 2010, four months after being notified that CHN was incurring bills for unreimbursed member services, the board began billing member agencies based on the costs of telecommunication services. According to the interim president, as of October 6, 2010, CHN owed the telecommunication vendor \$216,745.

It appears that CHN management's failure to properly account for, assess to members, and pay for recurring maintenance and operating costs was a contributing cause of the organization's current distressed financial condition.

*Accounting and Financial Reporting for Not-For-Profit Recipients of Grant Funds in Tennessee*, page 4-1, states that "[a]llocable-direct and administrative costs must be allocated to a particular cost objective, such as a grant, project, service, function, or other activity, in accordance with the relative benefits received."

**RECOMMENDATION:**

To ensure that the costs of specific programs are properly allocated to benefits received, CHN's board should take reasonable measures to ensure that accurate and timely financial reports are prepared and that the costs of CHN operations are properly allocated to the program or entity incurring those costs.