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Volume 3
Consulting Expenses



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CONSULTING EXPENSES

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I. INTRODUCTION

As a billion dollar company, Fairview must necessarily retain consultants, expending in excess of \$10 million per year on such fees. (Exhibit 1.) From time to time Fairview adopted written policies and procedures regarding third-party contracts governing such consultants. In 1993, a policy memorandum concerning third-party contracts was distributed to the staff, which required that consultant contracts be approved by management, that they be in writing, that they document the nature and scope of the service to be provided, that the project be summarized, that business objectives be identified, that the cost saving or revenue enhancement purpose of the contract be identified, that a timeframe be established, and that payment terms be disclosed. (Exhibit 2.) In addition, the policy required that Fairview personnel who are responsible for the contract be identified and that all contracts be authorized by a particular level of management. (*Id.*)

This policy was supplemented in February of 2000 by another procedural memorandum, which once again required that third-party contracts be in writing, that a Request for Proposal ("RFP") be utilized, that the services to be provided be described, that the business objectives be described, that the cost saving and revenue enhancement feature of the contract be set forth, that a timeframe for completion of the services be identified, and that the cost and payment terms of the contract be established. (Exhibit 3.) Like the 1993 memorandum, the policy required that each contract identify the Fairview personnel who will be monitoring the contract. In addition, the 2000 policy requires that a proposal letter be submitted to management prior to approval of a contract. The proposal letter was to describe the purpose of the contract, the necessity for using the particular consultant, the manner in which the consultant was selected, and the approval limit of the manager. (*Id.*)

While Fairview has written policies in place concerning third-party contracts, its staff appears to have consistently ignored them. For instance, consulting services were rarely open to competitive bidding. Further, a solicitation package or RFP was rarely utilized. In several cases, payments to contractors could not be supported because no contract existed. In those cases where there were written agreements, several agreements failed to describe the services to be rendered, to identify a business objective, to establish a timeframe for completion, to establish payment terms, to identify the consultant's expertise, or to identify the staff at Fairview who were responsible for oversight of the contract. Several of the written agreements were not executed by the parties, and it appears that at least one of the agreements was written after the consulting project had been completed.

The following sets forth a number of issues relating to the management of consultants by Fairview.

II. COMPLIANCE WITH INDUSTRY STANDARDS AND INTERNAL POLICIES

A. Consulting contract standards.

Numerous periodicals and reference manuals describe reasonable and prudent procedures in the selection and management of outside contractors by nonprofit and other organizations.

(Exhibit 4.) Depending on the size of the contract, nonprofit organizations should:

1. Determine and articulate the goal and desired outcomes of the consulting contract;
2. Interview contractors as to experience, credibility and knowledge;
3. Obtain references regarding competing contractors and issue a request for proposal ("RFP") to each contractor;
4. Enter into a written contract that describes the work to be performed, the desired outcome of the work, the time parameters in which the work will be performed, the expected total project cost, and the documentation necessary to be submitted for payment to be made;

5. Require adequate documentation to support fees. Contractors compensated on an hourly rate basis should submit invoices that detail hours of work performed, identified by day and time bracket, the services performed each hour, and the person who performed the work; and
6. All expenses should be itemized on the invoice and supporting invoices for expenses should be attached.

(Id.)

Because Fairview is a nonprofit corporation that exists to benefit the public, it is important that Fairview conduct its business in a reasonable and prudent manner.

B. Fairview's policies regarding contracts.

In 1993, Fairview published its policies and procedures concerning consulting expenditures. (Exhibit 2.) The policy addresses many of the standards which are referred to in industry manuals concerning third-party contractors and attempts to address the issues discussed above. For instance, the 1993 policy noted that all consulting expenditures are subject to an approval process which required that budgeted expenditures of more than \$5,000 be approved by a vice president or officer of Fairview. The policy established the following guidelines to support the issuance of a third-party consulting contract:

1. A proposal letter must be received from the consulting firm.
2. A Consulting Expenditure Request Form must be completed, a copy of which is attached as Exhibit 5.
3. The Consulting Expenditure Expense Form requires that the Fairview employee identify the reason why a consultant is necessary, the manner in which the consultant was selected, the estimated cost of the consulting engagement, a written description of the scope of the project, documentation concerning approval by an officer (if more than \$5,000), and a statement as to why internal resources could not complete the desired work.
4. Fairview staff must identify whether the consultant should be categorized as an independent contractor or as an employee for purposes of the Internal Revenue Code.

The 1993 policy also required that the proposal letter describe the services to be performed by the consultant, the Fairview business objectives to be obtained, a description of the cost savings and revenue enhancement to be achieved by use of the contractor, an estimated timeframe for completion of services, a description of the end product, a detailed description of the cost, including payment terms, a description of the consultant's expertise, and identification of all individuals who will be responsible to monitor the project.

In February of 2000, a second consulting policy was published by Fairview management. (Exhibit 3.) The 2000 policy followed many of the guidelines established in the 1993 policy. It identified the type of work that would be covered by the policy and identified a similar process to engage a consultant, starting with a request for authorization to be made to an executive at Fairview, followed up by a procedure in which the proposed consultants would submit their proposals and a written contract would be signed. The policy required that a bid request be typed with complete information including quantity, description, bidding period, delivery requirements, and any special conditions.

Oddly enough, the policy contained no reference to a bidding process or to a requirement that competitive bids be obtained prior to the issuance of a contract.

As discussed below, Fairview routinely failed to comply with the requirements set forth in either the 1993 or 2000 policies.

C. 2004 Internal Audit.

In response to the Compliance Review of Allina Health System and HealthPartners, in January of 2004 Fairview conducted an internal audit to review its consulting expenses. (Exhibit 6.) The internal audit consisted of a review of 47 consulting arrangements entered into during fiscal year 2002 and concluded that Fairview's consulting expenditures suffered from the

same problems discussed in the Allina and HealthPartners' Compliance Reviews. The report noted:

Our review of Fairview consulting expenditures revealed similar weaknesses in the documentation process--*i.e.*, outdated policies, no open-bidding process, services provided without contract, inability to locate agreements, and consulting services performed by former employees. In our opinion, Fairview should adopt the procedural recommendations provided herein and develop processes to ensure that the revised procedures are assiduously followed.

(*Id.*, p. 2.)

D. Fairview failed to request competitive bids on projects in violation of industry standards.

While there was no requirement in either of Fairview's 1993 or 2000 policies that competitive bids be obtained prior to issuing a contract, it is clearly an industry standard that bids be obtained in order to ensure that arms length transactions are taking place and that the nonprofit organization is obtaining the best value for its payments. Indeed, Fairview acknowledges that awarding contracts on the basis of a competitive bid ensures that purchased services represent the greatest value to the organization. (Exhibit 6, p.3.) In spite of this, Fairview made a practice of hiring consultants without seeking bids or proposals. In fact, its 2004 audit report found no evidence that consulting services were ever competitively bid. (*Id.*)

Examples where Fairview failed to comply with the common standard of requesting bid proposals include the following:

- Of the numerous consulting arrangements Fairview had with Ernst & Young between 1998 and 2003 and the over \$4 million Fairview paid to Ernst & Young, in consulting fees and expenses paid to Ernst & Young, only *one* request for proposal was made, in 2003. (Exhibit 7.)
- Between 1999 and 2001, Fairview paid over \$1.4 million in consulting fees to Cap Gemini Ernst & Young, but there is no evidence that Fairview requested a bid or received a proposal. (Exhibit 8.)
- Fairview hired Pam Tibbetts, a former Fairview employee, as a consultant without issuing a request for proposal or seeking bids. (Exhibit 9.)

- Fairview retained the Gallup Organization at a cost of \$687,742 to conduct four surveys of its employees. No bid requests or request for proposals were undertaken. (Exhibit 10.)
 - Between 1998 and 2002, Fairview paid almost \$113,000 in consulting fees to Deloitte and Touche without issuing a request for proposals or seeking bids from any other party. (*Id.*)
 - Fairview paid BIC Consulting almost \$400,000 for services rendered in 1998 and 1999 without issuing a request for proposals or seeking bids from any other party. (*Id.*)
 - In 1998, Fairview paid Andersen Consulting over \$650,000 for consulting services and no bids or proposals were requested from any other party. (*Id.*)
 - In 2000 and 2001, Fairview paid over \$185,000 to Marilyn McCarter Associates, including a project for “radiation therapy,” without requesting bids from any other party. (See Exhibits 10 and 11.)
 - From 1998 to 2002, Fairview paid over \$35,500 to Penfield Designs for “design/production” of “ads” without any evidence that bids or proposals were requested from any other party. (See Exhibits 10 and 12.)
 - In 1999 and 2000, Fairview paid over \$625,000 to QuadraMed Corporation for consulting services without seeking bids or proposals from any other party. (See Exhibits 10 and 13.)
 - Close to \$400,000 was paid to Renee Shimitz for her consulting services. It is unknown who Renee Shimitz is, what her area of specialty is, what services she is providing Fairview and whether she is charging a reasonable rate for her services. (See Exhibits 10 and 14.)
 - In 1999, Fairview paid Safenet Consulting over \$1.2 million for Y2K work. There is no evidence that Fairview used any type of bidding process for this project. (See Exhibits 10 and 15.)
- E. Fairview failed to enter into written agreements with consultants, violating its own policies established in 1993 and 2000.**

The internal auditor for Fairview in 2004 requested copies of 47 agreements pursuant to which payments were made during fiscal year 2002. (Exhibit 6.) The auditor received 23 of the requested agreements. (*Id.*) The other 24 agreements could not be located. In other words, the majority of the consulting agreements utilized during 2002 were oral and not subject to verification as to the services to be rendered, the competency of the person providing the services, the scope of the services, the timing of the services, the pricing of the services, or the

monitoring of the contract. The failure to utilize a written contract violates the Fairview policies, violates industry standards, and leaves Fairview vulnerable to excessive and inappropriate payments. Without a written contract, Fairview cannot track the scope of the work being done, determine if the consultants are billing Fairview appropriately, or determine if the work was being executed in a timely manner. In fact, the haphazard manner in which written contracts were ignored raises the question as to whether consulting expenses paid by Fairview were fairly billed or whether appropriate services were provided to Fairview. Examples of invoices that were paid even where there is no written contract include:

- Over \$185,000 paid to Marilyn McCarter Associates including, for example, payments for “radiation therapy.” No other details were given that reflect what this project services entailed. (Exhibit 11.) In fact, a telephone call to Ms. McCarter indicates that she is in the software business.
- Over \$35,500 paid to Penfield Designs for “design/production” of “ads.” Specific details about the project, other than the name of the ad, were not included in the invoice. (See Exhibits 10 and 12.)
- Over \$625,000 paid to QuadraMed Corporation including, for example, payments for “F-UMC Consolidation Project.” The invoices make no effort to describe the work performed. (See Exhibits 10 and 13.)
- Close to \$400,000 paid to Renee Shimitz for “services rendered system-wide JCAHO.” The documents do not make clear who Renee Shimitz is, what her area of specialty is or what services she is providing to Fairview. (See Exhibits 10 and 14.)
- In 1999, Fairview paid Safenet Consulting over \$1.2 million for Y2K work. It is unknown from the documentation what kind of Y2K work Safenet performed. (See Exhibits 10 and 15.)

F. On many occasions the few written agreements utilized by Fairview failed to meet the standards established by its 1993 and 2000 policies.

Of the 23 consulting contracts produced by Fairview for fiscal year 2002, it appears that most of the contracts did not comply with either the 1993 or 2000 policy. For instance, the 2004 internal audit noted the following:

- Five of the 23 written agreements lacked an adequate description of services.

- Five of the 23 written agreements failed to identify a business objective.
- Six of the 23 written agreements failed to identify the value of project to Fairview.
- Seven of the 23 written agreements failed to include a timeframe of completion.
- Seven of the 23 written agreements lacked specific deliverables.
- Two of the 23 written agreements lacked payment terms.
- Twenty-two of the 23 written agreements failed to identify the consultant's expertise.
- Fourteen of the 23 written agreements failed to identify the specific individuals assigned to oversee the project.
- Twenty-two of the 23 written agreements failed to provide references.

(Exhibit 6.)

The failure to identify these objectives increases the risk that the goal of the project will not be achieved. It also renders Fairview vulnerable to excessive billing. As important, vague or absent terms would render it impossible for Fairview to enforce the terms of the agreement if there were a dispute regarding the consulting agreement. Indeed, one of the 23 written agreements was drafted *after completion* of the consulting project, meaning that it could not have been enforced had there been a dispute during the project. In addition, in seven of the 23 contracts, the amount paid to the vendor appears to exceed the contracted amount, largely due to the fact that there is no ability to determine what services were to be provided or the price to be paid for those services.

G. Fairview made payments without careful review of invoices in violation of its 1993 and 2000 policies.

Because no person was identified to be responsible for most of the contracts, the procedures regarding payment appear to be fairly lax. For example, Ernst & Young submitted an

invoice that includes a calculation error resulting in an overbilling of \$2,000, which Fairview paid. (Exhibit 16.) Fairview's lack of scrutiny in reviewing these invoices also permitted numerous invoices to be paid which had insufficient descriptions of work performed and insufficient supporting documents. Indeed, most of the invoices submitted by Fairview's consultants failed to even itemize out-of-pocket expenses. Frequently, the only information provided to justify the expense was a one line sentence stating "out-of-pocket expenses" or "expense." For example, from 1999 to 2003, Fairview paid its consultant, Ernst & Young approximately \$30,000 for unidentified "expenses." (Exhibit 17.) Fairview regularly paid these amounts despite the fact that the invoices fail to itemize the expenses that were incurred.

The description of the services actually performed by the consultants was also deficient in many cases. For example, Cassidy and Associates had a very general flat-fee contract with Fairview and then billed \$93,395 for "professional services" without identifying the actual hours worked, the project worked on, the documents produced, or any other description of work. (See Exhibit 18.) A similar bill was submitted on August 1, 2000 for \$93,341 and for \$93,342 on November 1, 2000. (*Id.*)

Andersen Consulting billed over \$600,000 with a line item that was less than one sentence. (Exhibit 19.) In 1998, Andersen Consulting billed over \$1 million, with the invoices identifying the work simply being in support of the "FUMC Systems Consolidation Design Phase," without even referencing its letter agreement or providing more specifics of the services rendered. (Exhibit 20.)

In 2000, Deloitte and Touche relied on its letter agreement and submitted more than \$25,000 of billings for work simply identified as "professional services rendered in connection with valuation of shared information technology services in connection with the Epic

Independent Clinic pricing proposal,” without identifying the specific professional, actual hours worked and the like. (Exhibit 21.)

In 2000, Cap Gemini Ernst & Young also relied on a letter agreement and billed over \$500,000 for work simply identified as “case management and CDMP engagement,” again failing to provide any specific detailed information on professionals used, actual hours worked and the like. (Exhibit 22.)

The limited descriptions on expense invoices and the lack of reference to a consulting contract make it difficult for Fairview staff, or an auditor, to determine the validity of the expenses or to compare the expenses paid to the services that were rendered. In short, Fairview is unable to prudently evaluate the ability of and prices charged by its consultants.

H. Fairview’s use of former employees as consultants.

In 2002, Fairview spent over \$670,000 on consultants who were former employees. (Exhibits 23 through 25.) These consultants were not required to go through a bidding process nor was it ever determined that utilizing their services as consultants, rather than retaining their services as employees, was the most economical choice. Several examples of former employees who became consultants, as well as the fees charges by these consultants, include:

- Over \$16,000 paid for 13 days of work by Lois Hybben Stehr. On one occasion Ms. Stehr was paid \$1,250 per day as a consultant. (Exhibit 23.)
- \$17,500 per month paid for consulting services by Sandra Rasmussen. (Exhibit 24.)
- Approximately \$76,000 paid to Pamela Tibbetts for periodic consulting work. (Exhibit 25.)

No contracts were provided which identified in sufficient detail the services to be rendered. No bids were obtained. As a result, there is no ability to document whether these former employees offered sufficient value for their pay.

Absent a written contract, there is also no way to determine if payment made to the former employee exceeded the agreed amount. Without appropriate documentation to support the consulting arrangement, these agreements arguably could be deemed to be private inurement. (See Internal Audit Report, Exhibit 6.) The use of former employees as consultants raises the question as to whether such agreements are at arms length or are in the best interest of the Fairview stakeholders.

I. Fairview did not distribute its 1993 and 2000 policies concerning third-party contractors to its staff.

It does not do a nonprofit organization any good to adopt a policy if the policy is not going to be followed by its staff. As discussed, Fairview adopted third-party contractor policies in 1993 and 2000. It did not, however, share these policies with the Fairview staff. Indeed, when the Attorney General's Office requested copies of written policies concerning consulting contracts, Fairview initially responded that there were no written consultant policies adopted by the company in the 1990s. (Exhibit 26.) Indeed, the January 8, 2004 internal audit review by Fairview indicates that its Consulting Expenditure Policy was not available to its staff and was not available on Fairview's intranet website which published its internal policies and procedures. (Exhibit 6.) If an organization is serious about its policies and procedures, it shares them with its staff and enforces the policies. Fairview did neither.

J. The 2004 Consulting Expenditure Policy is appropriate only if it is followed.

In September of 2004, Fairview published a new Consulting Expenditure Policy. (Exhibit 27.) This Consulting Expenditure Policy closely follows the recommendations made in the Internal Audit Report which is dated January 8, 2004. (Exhibit 6.)

The adoption of a consulting expenditure policy should not be deferred until the prospect of a compliance review by the Attorney General's Office. Fairview knew about the Allina audit

in 2001 and the Memorandum of Understanding that had been adopted by Allina and the Attorney General's Office in 2001. Indeed, many of Fairview's policies adopted in 2002 concerning travel and expenses, executive compensation, and deferred compensation appear to closely track many of the recommendations made in the Allina and HealthPartners Compliance Review Reports. For reasons not understood, however, Fairview failed to adopt a consulting expenditure policy until this Compliance Review was undertaken. Fairview should have adopted a tighter policy after it reviewed the Allina compliance report; better yet, it should have simply followed its 1993 and 2002 policies.

III. CONCLUSION

Fairview adopted consulting expenditure policies as far back as 1993. It failed, however, to follow or enforce the policies. Because the company appeared to be lax in even adopting its 2004 standards until this Compliance Review was well underway, it can be questioned whether Fairview seriously will follow its 2004 procedures or whether the procedures were simply adopted as a means to anticipate criticism in this Report. In any event, Fairview's mission would be better served if, through good management policy, Fairview adopted and followed such policies on its own.

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