



A REPORT
TO THE
ARIZONA LEGISLATURE

Special Investigative Unit

Special Investigation

Arizona Department of Veterans' Services

Misuse of Public Monies, Conflict of Interest,
and Mifeasance by the Former Director

NOVEMBER • 2009



Debra K. Davenport
Auditor General

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AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

November 19, 2009

Members of the Arizona Legislature

The Honorable Jan Brewer, Arizona Governor

The Honorable Joey Strickland
Office of the Director of the Arizona Department of Veterans' Services

Advisory Commission
Arizona Veterans' Service Advisory Commission

The Honorable Terry Goddard
Office of the Attorney General

The Office of the Auditor General has conducted a special investigation of the Arizona Department of Veterans' Services for the period July 2002 through September 2007. The investigation determined the amount of public monies misused, if any, and whether there were any conflict-of-interest and procurement violations during that period.

The investigation consisted primarily of inquiries and examination of selected financial records and other documentation. Therefore, the investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, the Office does not express an opinion on the adequacy of the financial records or the internal controls of the Arizona Department of Veterans' Services. The Office also does not ensure that all matters involving the Department's internal controls, which might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that may require correction or improvement, have been disclosed.

The accompanying Investigative Report describes the Office's findings and recommendations as a result of this special investigation.

After this report is distributed to the members of the Arizona State Legislature, the Governor, the Director, the Advisory Commission, and the Attorney General, it becomes public record.

Debbie Davenport
Auditor General

Enclosure

SUMMARY

In April 2007, the Arizona Attorney General's Office requested that the Office of the Auditor General (Office) investigate potential conflict-of-interest violations by former Arizona Department of Veterans' Services (Department) Director, Mr. Patrick Chorpenning, Sr., in regard to his son's employment. In October 2008, the Office became aware of other possible misconduct by Mr. Chorpenning, including misuse of public monies, procurement fraud, and additional conflicts of interest. As a result of our investigation, we determined that from July 2002 to September 2007, Mr. Chorpenning authorized the expenditure of \$1,001,640 (as outlined below) in possible violation of several state laws. We have submitted our report to the Attorney General's Office, and they have taken criminal action against Mr. Chorpenning (see the Conclusion on page 27 of this report).

Specifically, Mr. Chorpenning may have violated:

1. Conflict-of-interest laws by participating in authorizing his son's employment agreements with the Department on four occasions and failing to disclose his conflict. Payments for his son's employment totaled \$215,984.
2. Conflict-of-interest laws by directing department employees to hire his wife, creating a position for her, and later approving a 35 percent increase to her salary. Mr. Chorpenning's wife collected \$114,104 in department payments.
3. State laws concerning the use of public monies by improperly gifting public monies to individuals and private corporations totaling \$288,795.
4. State laws concerning the use of public monies and procurement fraud by circumventing procurement rules in order to purchase media and advertising services totaling \$382,757.

Table 1: Summary of Violations
July 2002 to September 2007

| Dates | Description | Procurement Violations | Conflict of Interest | Misuse of Public Monies |
|--------------|---|-----------------------------------|---------------------------------|------------------------------------|
| 12/02-04/05 | Son's employment | - | \$215,984 | - |
| 02/04-03/07 | Wife's employment | - | 114,104 | - |
| 10/02-04/04 | Gifting monies to a private corporation | - | - | \$ 37,000 |
| 11/03-03/07 | Employee-related gifts | - | - | 38,595 |
| 09/03-09/07 | Gifting monies for a war memorial | - | - | 213,200 |
| 07/02-04/05 | Payments to a media company | <u>\$382,757</u> | - | - |
| | Total by Category | <u>\$382,757</u> | <u>\$330,088</u> | <u>\$288,795</u> |
| | | | Total Violations | <u>\$1,001,640</u> |

Further, Mr. Chorpenning may have violated state laws concerning fraudulent schemes by attempting to conceal his improper involvement in hiring his son and his wife. Despite direct inquiries, he failed to inform the Arizona Governor's Office that the Department was paying for his son's employment, and he misled the Governor's Office regarding the circumstances of his wife's initial hire. Additionally, Mr. Chorpenning's wife may have violated public document laws by falsifying her employment application and filing it with the Department.

As a public official, Mr. Chorpenning had a fiduciary duty to Arizona's citizens, in general, and to Arizona veterans and their families, in particular, for ensuring the prudent use of public money. However, Mr. Chorpenning failed in his responsibilities to the public by violating conflict-of-interest statutes, misusing public monies, and circumventing the Arizona Procurement Code. Although no internal control system can totally prevent dishonest actions such as Mr. Chorpenning's, there are actions the Department can take to help deter future instances of misconduct. See Recommendations on page 25 of this report.

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concluded ♦

INTRODUCTION & BACKGROUND

In 1982, the Governor established the Arizona Veterans' Service Commission (Commission) as a separate agency. In 1999, the Legislature separated the Commission from the agency by making the Commission an advisory body and creating a separate department. The Department's mission is to advance the interests of Arizona veterans through advocacy, legislation, service, and community relationships. The director is appointed by the Governor and is responsible for ensuring adequate management of the Department and veterans' affairs, as prescribed by state laws and regulations. The Department is financially accountable to Arizona's citizens, in general, and to Arizona veterans and their families, in particular, for the state appropriations, donations, and state home fund revenue it receives. The Department's fiscal year 2007 appropriations totaled \$18,132,800; fiscal year 2008 totaled \$23,772,600; and fiscal year 2009 totaled \$22,462,800 (all three amounts unaudited).

Pursuant to Arizona Revised Statutes (A.R.S.) §41-602, the Commission is charged with providing policy advice to the Governor and to the Department's director regarding veterans' issues. The Department's director is responsible for informing the Commission regarding policies adopted by the Department; however, the Commission does not have the authority to approve actions taken by the Department nor its director.

The Department employs more than 280 employees and is composed of four divisions:

1. Veterans' Services Division—Provides a network of veterans' benefits and employs counselors based in 24 offices located throughout Arizona. These counselors provide information and assistance to veterans and their family members.
2. Arizona State Veterans' Home (nursing home)—Constructed in 1995, the nursing home is a 200-bed, state-owned, state-operated licensed skilled nursing facility located in Phoenix. The nursing home serves the long-term needs of Arizona veterans and their dependent and surviving spouses. Generally, the nursing home is financially self-sufficient, relying solely on the fees collected to support its operations.

3. Fiduciary Division:
 - a. Guardian—Makes decisions about medical treatment and personal care for those veterans and dependents that the Arizona Superior Court assigns to them.
 - b. Conservator—Manages property and financial affairs for those veterans and dependents that the Arizona Superior Court assigns to them.
 - c. Personal Representative—Administers the estates of deceased veterans and distributes their assets to any heirs.
4. Administration—Composed of the Department Director's Office, Human Resources, Purchasing, Financial Services, and Information Technology.

In addition to the activities described above, the Department is also responsible for:

1. **State Home for Veterans Trust Fund (Veterans' Home Fund)**—Established under A.R.S. §41-608.01, the Veterans' Home Fund is used to account for Arizona State veterans' home operations. The nursing home is designed to be a self-sustaining facility with funding generated from operations that include payments from the U.S. Department of Veterans Affairs, Medicare, Arizona Health Care Cost Containment System, Long Term Care contractors, and private pay residents. Monies in the Home Fund are public money and are subject to state laws, regulations, and procurement policies and procedures unless specifically exempted.
2. **The Veterans' Donation Fund (Donation Fund)**—Established under A.R.S. §41-608, the Donation Fund consists of monies, gifts, and contributions donated to the Department as well as proceeds from the sale of specialty motor vehicle registrations such as Veterans, Military Support, Former Prisoner of War, Purple Heart, and Pearl Harbor Survivor license plates. The Donation Fund may be expended at the discretion of the Department's director for the benefit of veterans within the State of Arizona. Monies in the Donation Fund are public money and are subject to state laws, regulations, and procurement policies and procedures unless specifically exempted.

Patrick Chorpenning, Sr., former Department Director

In February 1999, Mr. Patrick Chorpenning, Sr., was the first director to be appointed under Laws 1999, Chapter 164, by then-Governor, Jane Dee Hull. As the Director, Mr. Chorpenning was responsible for the Department's overall administration, directly supervising an executive management team. In September 2004, Mr. Chorpenning took on additional duties as the Military Affairs Policy Adviser to former Arizona Governor Janet Napolitano, which included securing benefits for members of the National Guard and continually informing the Governor of the military base relocation and closure process.

On March 16, 2007, the U.S. Department of Health & Human Services issued a \$10,000 civil penalty to the Department for substandard care conditions at the nursing home and threatened to revoke the nursing home's status as a Medicare provider unless conditions improved. On March 26, 2007, former Governor Napolitano ordered an immediate review of the nursing home and removed Mr. Chorpenning from direct oversight of the home but allowed him to retain control of all remaining department functions. That next day, Mr. Chorpenning resigned from his director position.

As a result of the deficiencies found by the U.S. Department of Health & Human Services within the nursing home in 2007, the Arizona State Legislature appropriated State General Fund monies for the nursing home. The nursing home received appropriations in fiscal year 2008 totaling \$3,457,900; fiscal year 2009 totaling \$2,855,000; and fiscal year 2010 totaling \$2,855,000 (all three amounts unaudited).

FINDING 1

Former Director engaged in conflicts of interest

From December 2002 to March 2007, the former Department of Veteran's Services Director, Mr. Patrick Chorpenning, Sr., may have intentionally and repeatedly violated conflict-of-interest laws when participating in hiring his son and his wife, allowing payments totaling \$330,088 to sustain their employment. As illustrated in Table 2 below, Mr. Chorpenning directed and ultimately authorized his son's employment with the Department and later created another position for his son through an interagency service agreement. From December 2002 to April 2005, the Department expended \$215,984 for Mr. Chorpenning's son's salary, employer-related benefits, materials, supplies, travel, communications, and equipment. Following his son's hire, Mr. Chorpenning then improperly created a position for his wife at the Department, directed her hiring, and later participated in an unjustified increase to her salary. From February 2004 to March 2007, the Department spent at least \$114,104 for Ms. Chorpenning's salary.

To help ensure that public officials do not improperly use their position for their own benefit, Arizona law requires that public officials make known their substantial interest in any decision (this disclosure must be made available to the public), as well as refrain from voting on or participating in that decision, all of which Mr. Chorpenning failed to do.

Table 2: Conflicts of Interest
December 2002 to March 2007

| Position | Relationship | Dates | Amount |
|---|--------------|---------------------|----------------------------|
| Nursing Home Assistant Administrator | Son | 12/16/02 – 08/01/03 | \$ 40,302 |
| Interagency Service Agreement—Arizona State University Senior Administrator | Son | 07/24/03 – 04/18/05 | <u>175,682¹</u> |
| Total payments for son | | | \$215,984 |
| Strategic Planner/Special Projects | Wife | 02/14/04 – 11/06/05 | 57,000 |
| In-House Design Coordinator | Wife | 11/07/05 – 03/23/07 | <u>57,104</u> |
| Total payments for wife | | | \$114,104 |

1 In total, the Department expended \$250,000 on the interagency service agreement. Mr. Chorpenning's son resigned from his interagency position on April 18, 2005, prior to the agreement's termination date. Therefore, \$175,682 of the \$250,000 was used to fund his son's salary, and employer-related benefits and expenses.

Source: Auditor General staff analysis of Arizona Department of Veterans' Services and Arizona State University records.

Mr. Chorpenning's Son—Nursing Home Assistant Administrator

Mr. Chorpenning may have unlawfully participated in his son's employment by explicitly directing his subordinate staff to hire his son as the assistant administrator of the nursing home. This employment opportunity was not advertised, and no documentation exists showing that Mr. Chorpenning's son interviewed for the position. As a result of Mr. Chorpenning's directives, his son was hired on December 16, 2002, at an annual salary of \$62,000. As an uncovered employee, Mr. Chorpenning's son served at his father's discretion and was primarily responsible for applying for federal grants on the Department's behalf until he resigned effective August 1, 2003. For the period of his employment from December 2002 to August 2003, Mr. Chorpenning's son received approximately \$40,303 in compensation.

Mr. Chorpenning's Son—Interagency Service Agreement Senior Administrator

During Mr. Chorpenning's son's employment at the nursing home, Arizona Department of Administration officials became aware of the employment situation between father and son and informed Mr. Chorpenning of its inappropriate nature. As a result, in June 2003, Mr. Chorpenning initiated an interagency service agreement between Arizona State University (ASU) and the Department to develop programs and services to support the educational needs of veterans, which included providing grant-writing services and serving as the contact between ASU and veterans. Mr.

Chorpenning stipulated that the agreement was contingent upon the Department's assigning a current employee as the senior administrator for the project. In July 2003, Mr. Chorpenning placed his son as the employee and committed \$120,000 of department monies to pay for his son's annual salary of \$65,000, and employer-related benefits, materials, supplies, travel, communications, and equipment. The Department used the Veteran's Home Fund to pay for the initial agreement.

Mr. Chorpenning assigned his son as the employee under the interagency service agreement with Arizona State University.

In April 2004, Mr. Chorpenning continued his improper involvement with his son's employment by approving an extension to the agreement for a 3-month period from June 30, 2004 to September 30, 2004, with no additional monies provided. Mr. Chorpenning also improperly approved a second extension to the agreement for another 1-year period from September 30, 2004 through September 30, 2005, agreeing to an additional \$130,000 to fund his son's annual salary, and employer-related benefits and expenses. The Department used Donation Fund monies to pay for the second extension.

On April 18, 2005, Mr. Chorpenning's son resigned from his ASU position. ASU appointed one of its own employees to fill the son's vacated position for the remainder of the agreement terms. In total, the Department expended \$250,000 on the interagency service agreement with ASU, \$175,682 of which was used to fund the son's annual salary, and employer-related benefits and expenses.

From July 2003 through April 2005, Mr. Chorpenning's son's work product did not fulfill the overall objective of the interagency service agreement, which was to obtain funding opportunities for veterans' education. Instead, at the Department's direction, Mr. Chorpenning's son's work time was spent on applying for federal grants solely on the Department's behalf. Specifically, his son applied for federal grants in efforts to obtain funding for nursing home improvements and building a new Tucson veterans' home. ASU's Project Director had little involvement in the son's day-to-day activities, and in fact, Mr. Chorpenning and his son largely determined the project's direction. Neither the Department nor ASU were able to provide evidence of any funding opportunities the son obtained to enhance veterans' educational opportunities.

Mr. Chorpenning's son's work product did not fulfill the overall objective of the interagency service agreement.

Mr. Chorpenning's Wife—Strategic Planner/Special Projects

Mr. Chorpenning may have unlawfully participated in his wife's employment by directing his subordinate staff to contract with what he claimed was his wife's company, Feather Your Nest Designs, to redecorate the veterans' nursing home. Citing the need to follow procurement rules, department staff refused to issue a contract with Ms. Chorpenning or her company. Mr. Chorpenning then authorized the creation of an additional position so his wife could be hired as an employee, serving at Mr. Chorpenning's discretion.

Mr. Chorpenning improperly directed department employees to contract with his wife to redecorate the veterans' nursing home.

On February 3, 2004, Mr. Chorpenning added the position under the Strategic Planner/Special Projects title, which was offered to Ms. Chorpenning at an \$18 hourly rate. This employment opportunity was not advertised, and no one, including Ms. Chorpenning, interviewed for the position. In fact, Ms. Chorpenning did not submit her employment application until the day after she was hired.

Even though Ms. Chorpenning was hired under the pretext of Strategic Planner/Special Projects, her actual responsibilities differed significantly from the job responsibilities of this position. Rather than the listed duties of developing the Department's strategic plan, conducting business and statistical research, researching personnel issues, and reporting research findings to the Department's executive staff, Ms. Chorpenning was responsible for managing the nursing home's redecorating projects.

Ms. Chorpenning's actual work product was completely unrelated to her hired position.

On October 15, 2004, Mr. Chorpenning significantly increased his wife's salary. Mr. Chorpenning approved a \$6.52 per hour increase to his wife's salary, thereby adjusting her rate from \$18.48 to \$25.00 per hour. This 35 percent increase was not explained, Ms. Chorpenning's title and responsibilities had not changed, no evaluations were performed, and no goals or accolades were documented. In fact, of the five employees receiving pay increases on this date, Ms. Chorpenning was the only one without some sort of personnel action such as a promotion or position change. Moreover, the other hourly increases were much smaller than Ms. Chorpenning's, ranging from \$0.19 to \$2.24 per hour. Finally, the other strategic planner/special projects employee, whom the Department hired more than 10 years ago, was earning approximately \$2.22 per hour less than Ms. Chorpenning, who had been in the same position for less than 9 months.

Mr. Chorpenning improperly approved a 35 percent increase to his wife's salary, without merit or justification.

Mr. Chorpenning's Wife—In-House Design Coordinator

On October 7, 2005, Mr. Chorpenning created a second position specifically for his wife. Specifically, Mr. Chorpenning directed the Department's Human Resources Department to create the In-House Design Coordinator position and reassign his wife from Special Projects/Strategic Planner to this newly created position. The Department failed to post or announce the In-House Design Coordinator position, interview candidates, or require an application for the job. Ms. Chorpenning remained in this position from November 7, 2005, until she resigned on March 23, 2007.

Mr. Chorpenning created a second position specifically for his wife, directing department employees to reassign her to that position.

As of August 2009, neither the Strategic Planner/Special Projects nor the In-House Design Coordinator positions that Ms. Chorpenning vacated had been refilled.

In accordance with A.R.S. §38-503, "Any public officer or employee of a public agency who has, or whose relative has, a substantial interest in any contract, sale, purchase or service to such public agency shall make known that interest in the official records of such public agency and shall refrain from voting upon or otherwise participating in any manner as an officer or employee in such contract, sale or purchase." Further, according to A.R.S. §38-510, "A person who: 1. Intentionally or knowingly violates any provision of sections 38-503 through 38-505 . . ." could be in violation of the law and subject to a class 6 felony.

Impact on Nursing Home Operations and the Veterans' Home Fund

The Veterans' Home Fund accounts for the operation of its 200-bed skilled nursing facility (veterans' nursing home), which serves the long-term needs of Arizona veterans, their dependents, and surviving spouses. The nursing home is financially self-sufficient, relying solely on the fees it collects to support its operations. Further, monies in the Veterans' Home Fund are subject to an annual spending limit that the Arizona State Legislature determines. The Nursing Home Administrator is responsible for managing the nursing home and its operations, with ultimate authority residing with the Department's Director.

From fiscal years 2004 to 2007, nursing home renovations coordinated by Ms. Chorpenning, a portion of Ms. Chorpenning's salary, and a portion of Mr. Chorpenning's son's interagency salary and employer-related expenses totaling at least \$786,820 were financed through the Veterans' Home Fund. Nonetheless, during that same period, Mr. Chorpenning directed the Nursing Home Administrator to reduce spending on nursing home operations, such as decreasing food and dietary staffing, limiting staff overtime, and prohibiting the purchase of nursing home equipment. In fact, the Nursing Home Administrator stated that he had to modify the Home Fund's budget and reduce nursing home positions and certain operations to accommodate these expenditures, and further, to comply with the spending limits the Arizona Legislature established.

Mr. Chorpenning directed the hiring of his wife and redecorating of the nursing home, while at the same time demanding a reduction to spending on nursing home operations and staff expenditures.

Additionally, the Veterans' Home Fund fiscal year-end balance decreased significantly, from \$1,639,204 during fiscal year 2004 to \$30,013 during fiscal year 2007, with a slight increase noted in fiscal year 2008 to \$74,846. Certainly there are other factors that have contributed to the Veterans' Home Fund's declining balance, but the impact of the above-mentioned expenditures totaling at least \$786,820 may have caused a substantial depletion to the Veterans' Home Fund.

In an interview with Auditor General staff, the Nursing Home Administrator stated that it was his belief that Mr. Chorpenning stopped acting in the interest of the veterans, and certainly the nursing home's veterans, and started funneling department monies to his personal friends and family members.

FINDING 2

Former Director concealed his improper actions

On September 17, 2004, the Arizona Governor's Office (Governor's Office) received an anonymous e-mail that contained allegations about Mr. Chorpenning's hiring his relatives, including his son and his wife. The Governor's Office forwarded this e-mail to Mr. Chorpenning for a response. On September 22, 2004, Mr. Chorpenning sent a response letter to the Governor's Office, in which he attempted to conceal his improper involvement by:

1. Failing to inform the Governor's Office of his son's employment status as the senior administrator within the interagency services agreement between the Department and Arizona State University, and
2. Misleading the Governor's Office regarding the circumstances of his wife's hire by providing false information.

Even though Mr. Chorpenning had approved his son's employment under an agreement with Arizona State University over a year earlier and his son was currently in that position and being paid with department monies, he chose not to include that information within his written response to the Governor's Office. In fact, Mr. Chorpenning reported only that his son had left the Department to start a private public policy consulting firm. He never disclosed that his son worked full-time for the Department through an agreement with Arizona State University, which was fully funded with department monies.

Further, Mr. Chorpenning falsely and misleadingly stated in his response to the Governor's Office that the Department's Nursing Home Administrator had hired Ms. Chorpenning and that her hiring was discussed with the Arizona Veterans' Service Advisory Commission. According to the Commission's meeting minutes, no discussion occurred relating to Ms. Chorpenning's initial employment, and further, as discussed in Finding 1, Mr. Chorpenning himself improperly directed the Department's Nursing Home Administrator and other department employees to hire Ms. Chorpenning.

Mr. Chorpenning failed to disclose to the Governor's Office that his son worked for the Department through an agreement with Arizona State University.

Mr. Chorpenning presented false information to the Governor's Office regarding his wife's employment with the Department.

As a result of Mr. Chorpenning's deception, the Governor's Chief of Staff believed the hiring issues involving Mr. Chorpenning's relatives had been resolved and that no further investigation was necessary.

In accordance with A.R.S. §13-2311, ". . . any person who, pursuant to a scheme or artifice to defraud or deceive, knowingly falsifies, conceals or covers up a material fact by any trick, scheme or device or makes or uses any false writing or document knowing such writing or document contains any false, fictitious or fraudulent statement or entry . . ." could be in violation of the law and subject to a class 5 felony.

FINDING 3

Former Director's wife falsified and submitted a public document to the Department

On February 15, 2004, the day after she was hired, Mr. Chorpenning's wife submitted an employment application to the Department falsely claiming that from 2002 to 2004, she worked for Feather Your Nest Design, earning \$800 per week. She also falsely listed her son-in-law as her supervisor. Conversely, Ms. Chorpenning appeared to be unemployed as neither she individually nor Feather Your Nest Design, the company, reported any wages, salary, or income to the Arizona Department of Economic Security from January 1, 2001 to February 14, 2004.

In January 2004, nearly 2 years after the date listed on Ms. Chorpenning's application, she requested her son-in-law's help with creating a business under the name Feather Your Nest Design. Ms. Chorpenning's son-in-law then filed a corporate filing form for the business with the Arizona Corporation Commission. That same month, Ms. Chorpenning's son-in-law also filed for and received a federal Employer Identification Number. However, in November 2004, he filed termination documents with the Arizona Corporation Commission because Ms. Chorpenning said she was too busy and had begun employment with the Department. Ms. Chorpenning's son-in-law stated that he was not aware of any business activity, and he neither employed nor supervised Ms. Chorpenning.

In accordance with A.R.S. §39-161, "A person who . . . offers to be filed, registered or recorded in a public office in this state an instrument he knows to be false or forged . . ." could be in violation of the law and subject to a class 6 felony.

Mr. Chorpenning's wife submitted a falsified employment application to the Department, claiming that she worked for Feather Your Nest Design while being supervised by her son-in-law.

FINDING 4

Former Director misused public monies

Public officials with oversight authority have a responsibility to prudently manage money entrusted to them. However, from October 2002 to September 2007, Mr. Chorpenning may have misused public monies when he improperly authorized the expenditure of monies from the Department's Donation Fund, totaling \$288,795, for purposes inconsistent with serving the needs of Arizona veterans (see Table 3 below). Specifically:

1. From October 2002 to March 2004, Mr. Chorpenning improperly authorized payments totaling \$37,000 to establish a private nonprofit corporation and pay for its administrative costs. No services or products were provided directly to or on behalf of the Department; these payments were a gift of public monies.
2. From November 2003 to March 2007, Mr. Chorpenning improperly authorized payments totaling \$38,595 to pay for employee-related gifts and banquets.
3. From September 2003 to September 2007, Mr. Chorpenning improperly authorized four payments totaling \$113,200 and contractually required two additional payments totaling \$100,000 to build a war memorial. However, former Arizona Governor Janet Napolitano strictly prohibited the use of any public monies for this memorial.

Table 3: Misuse of Public Monies Summary
October 2002 to September 2007

| Description | Number of Instances | Amount |
|---|---------------------|-------------------------|
| Gifting monies to a private corporation | 4 | \$ 37,000 |
| Employee-related gifts | 22 | 38,595 |
| War memorial payments | 6 | 213,200 |
| Misuse of public monies | <u>32</u> | <u>\$288,795</u> |

Source: Auditor General staff analysis of Arizona Department of Veterans' Services, Arizona Department of Administration, and nonprofit organization records.

Department Donation Fund monies should be prudently managed and used for the benefit of Arizona veterans.

The Department's Donation Fund consists of monies, gifts, and contributions donated to the Department as well as proceeds from the sale of specialty motor vehicle license plates. Donation Fund monies may be used at the Director's discretion; however, these monies are public monies and should be prudently managed and used for the benefit of Arizona veterans. Further, the Arizona Constitution prohibits public money from being given or loaned to any individual, association, or corporation. Public money must be spent for a public purpose. The Attorney General has held that an incidental private benefit is not prohibited if there is a public purpose being served by the expenditure and the public value is not far exceeded by the amount being paid.

Gifts of Monies to a Private Organization

The Arizona Constitution prohibits gifting of public monies, including donating or loaning public money to private individuals or organizations.

The Arizona Constitution, Article IX, Section 7,

states: "Neither the State, nor any county, city, town, municipality, or other subdivision of the State shall ever give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation, or become a joint owner with any person, company, or corporation, except as to such ownerships as may accrue to the State by operation or provision of law."

Attorney General Opinion 185-051 states in part:

"While public funds may not be loaned or given to private individuals or entities, an incidental private benefit is not prohibited by Article IX as long as there is a public purpose served by the expenditure or loan of funds and the value to be received by the public is not far exceeded by the consideration being paid."

From October 2002 to April 2004, Mr. Chorpenning improperly used Donation Fund monies totaling \$37,000 to help establish and fund the administrative operations of a planned nonprofit veterans' service organization. On October 24, 2002, Mr. Chorpenning authorized the first payment totaling \$25,000 to this organization, which had not yet applied for nonprofit 501(c)(3) status from the Internal Revenue Service (IRS). In fact, Mr. Chorpenning allowed the private organization to use these Donation Fund monies to pay for its IRS application fee, attorney fees, office rent, employees' salaries, and other administrative costs.

Additionally, from January to April 2004, Mr. Chorpenning improperly authorized three more payments to the newly recognized nonprofit corporation totaling \$12,000 to help their administrative operations. Similarly, these monies were used to pay for the nonprofit corporation's office rent, office supplies, Web site hosting, letterhead, employees' salaries, and other administrative costs.

Although the nonprofit corporation may help serve the Arizona veterans' needs by maintaining a veterans' registry, participating in veterans' outreach programs, and providing other information and benefits to veterans, it was improper for Mr. Chorpenning to use public monies to establish and maintain the administrative operations of this private corporation.

Employee-related Gifts

From November 2003 to March 2007, Mr. Chorpenning improperly authorized 22 payments and transfers from the Donation Fund totaling \$38,595 to purchase gifts and finance end-of-the-year banquets for department employees.

State agencies are allowed to expend certain monies for employee recognition programs; however, in 2003, Mr. Chorpenning began to improperly augment the employee recognition program with Donation Fund monies that were intended for the benefit of Arizona veterans. Specifically, Mr. Chorpenning authorized the transfer of Donation Fund monies to the employee recognition program, and on November 19, 2003, 300 \$25 gift cards were purchased from a local grocery store for all department employees. These gift cards were then distributed to employees at the Department's end-of-the-year banquet, making it appear as though the employee program funded the gifts. In fact, in e-mail correspondence between Mr. Chorpenning and the Department's employee program director, Mr. Chorpenning stated, "Remember this is not a department program but something that the employee association is doing"

In 2003, Mr. Chorpenning began authorizing Donation Fund monies to finance employee gifts, monies that were intended for the benefit of Arizona veterans.

Mr. Chorpenning continued to allow these disbursements from the Donation Fund for employee-related gifts until his resignation in March 2007, at which time the Department's new Interim Director immediately prohibited the use of Donation Fund monies to finance employee-related items, believing this practice to be inappropriate. In total, Donation Fund monies helped finance \$38,595 worth of employee-related gifts and banquets, including the purchase of approximately 1,248 grocery store gift cards (see Table 4 below).

Table 4: Employee Gift Expenditures
November 2003 to March 2007

| Description | Date | # of Gift Cards | Amount |
|--|-------------|---------------------|------------------------|
| Grocery store gift cards | 11/19/03 | 300 | \$ 7,050 |
| Grocery store gift cards | 12/02/04 | 325 | 7,637 |
| Grocery store gift cards | 11/09/05 | 303 | 10,075 |
| Grocery store gift cards | 12/01/06 | 320 | 10,640 |
| Miscellaneous employee expenses (banquet and fund-raising supplies) | 11/03-03/07 | - | 3,193 |
| Total | | <u>1,248</u> | <u>\$38,595</u> |

Source: Auditor General staff analysis of Arizona Department of Veterans' Services and Employee Recognition records.

War Memorial Payments

From September 2003 to September 2007, Mr. Chorpenning improperly authorized \$213,200 of Donation Fund monies for the design and construction of a war memorial in direct opposition to a Governor's Order. In May 2003, former Arizona Governor Janet Napolitano enacted Executive Order 2003-17, which created a 21-member Iraqi War Memorial Commission under the Department's leadership, specifically commanded by Mr. Chorpenning, but prohibited the use of any public monies to fund the project. The Executive Order states, "The Commission [Iraqi Commission] shall have reasonable access to state-owned conference rooms in the Executive Tower and, where feasible, to support staff and facilities of the Governor's Office and/or Department of Veterans' Affairs [Department]; provided, however, that all funding necessary for any war memorials recommended by the Commission shall be funded by private donations, which the Commission shall be authorized to solicit" (emphasis added).

Despite the Governor's order prohibiting the use of public monies, Mr. Chorpenning entered into a contractual agreement, obligating the Department's Donation Fund to pay for memorial expenditures.

On May 13, 2004, Mr. Chorpenning improperly and without authority entered into a contractual agreement with the same private nonprofit veterans' service corporation as discussed on page 16 to help finance and construct the memorial. In direct conflict with the Governor's order, Mr. Chorpenning agreed to hold the Department financially responsible for funding the memorial by using Donation Fund monies if necessary. Specifically, the contract stated:

1. "Should there be insufficient funds in the Memorial account . . . ADVS [Department] will appropriate the money to [veterans' service organization] in the amount necessary to pay all costs in full.
2. In the event fundraising cannot generate the funds needed or that the donations raised from the public are insufficient to build the memorial by the completion date set by Legislation ADVS [Department] may pay the costs to build and/or complete the memorial from the Veterans Donation Fund."

The Iraqi Commission was unable to raise enough money to fully fund the construction of the memorial. As a result, Mr. Chorpenning improperly authorized four payments from the Department's Donation Fund totaling \$113,200 to aid with memorial expenditures. These monies were provided to the same contracted nonprofit corporation and used to pay for the costs of artist renderings, fund-raising brochures, and sculpture design and completion.

The payments continued even after Mr. Chorpenning resigned from his position in March 2007. Because of his improper actions making the Department contractually responsible for funding the memorial, the Department was required to make two additional payments in May and September 2007 totaling \$100,000. See Table 5 on page 19.

Table 5: War Memorial Payments
September 2003 to September 2007

| Description | Date | Amount |
|---|----------|-------------------------|
| Artist renderings (\$500 each) and fund-raising brochures | 09/26/03 | \$ 5,000 |
| Enduring Freedom Memorial Scale Model | 08/20/04 | 7,000 |
| Memorial sculpting fee (1/3 payment) | 09/30/06 | 50,600 |
| Memorial sculpting fee (1/3 payment) | 09/30/06 | 50,600 |
| Remaining balance on memorial sculpting fee | 05/01/07 | 50,000 |
| Help with constructing Enduring Freedom Memorial | 09/04/07 | 50,000 |
| Total Misuse of Public Monies | | <u>\$213,200</u> |

Source: Auditor General staff analysis of Arizona Department of Veterans' Services and nonprofit organization records.

On July 13, 2006, 2 years after Mr. Chorpenning had already obligated and used Donation Fund monies for the war memorial, he received support from the Arizona Veterans' Service Advisory Commission to use Donation Fund monies to finance the memorial. However, this support is ineffectual because the Commission does not have the authority to approve or direct the expenditure of these funds nor the authority to override the Governor's executive order and cause public monies to be used on this memorial. Moreover, the Commission had not been fully informed when voting on this matter. Mr. Chorpenning failed to provide the members with the following information:

- Mr. Chorpenning had already signed a contract in May 2004 with a private veterans' service organization, obligating Donation Fund monies for the war memorial.
- \$12,000 of Donation Fund monies had already been spent for the memorial.
- The Governor's executive order strictly prohibited the use of public monies to fund the memorial.¹

Mr. Chorpenning admitted to Auditor General staff that he regretted using Donation Fund monies to finance the memorial. As of May 15, 2009, the war memorial received \$243,687 in donations, with approximately 87 percent of this funding coming directly from the Donation Fund.

In accordance with A.R.S. §35-301, "A public officer or other person . . . charged with the receipt, safekeeping, transfer or disbursement of public money . . . without the authority of law, appropriates it, or any portion thereof, to his own use, or to the use of another . . ." could be in violation of the law and subject to a class 4 felony.

¹ Donation Fund monies are public monies because they are held by the Department and the Director in their official capacities, in accordance with A.R.S. §35-302.

FINDING 5

Former Director violated procurement rules

Arizona Revised Statutes and Arizona Administrative Code guidelines exist, in part, to ensure that public officials obtain the best possible value for the public money they spend by prohibiting the restraint of free trade and unreasonable reduction of competition among vendors. Additionally, as public officials, department employees have a responsibility to prudently manage department assets on behalf of the community they serve. Although ultimately responsible for ensuring that the procurement process was properly followed, Mr. Chorpenning intentionally circumvented these procedures, and from July 2002 to April 2005, improperly spent \$382,757 of Donation Fund monies on media and advertising services that were never competitively procured. Mr. Chorpenning's inappropriate actions may have harmed the Department by limiting competition as he directed business toward a specific vendor without the benefit of full and open competition.

Mr. Chorpenning may have violated state laws, rules, and regulations when he:

- Circumvented the Arizona Procurement Code and the Department's finance and purchasing procedures by exclusively entering into an arrangement with a local media production company (the vendor) to provide media and advertising services.
- Without authority, improperly exceeded the Department's spending limit of \$250,000 for contracts.
- Improperly spent \$85,489 promoting a private trade name.
- Failed to prudently monitor the vendor's services, expending \$39,000 on behalf of a private nonprofit corporation for consulting services that the nonprofit never received.

Mr. Chorpenning circumvented the Arizona Procurement Code

During the period July 2002 to April 2005, Mr. Chorpenning may have violated various state laws, rules, and regulations when purchasing a range of media and advertising services from a local media production company. Mr. Chorpenning improperly initiated an agreement with the Phoenix-based company to promote and advertise the Department, a private trade name called Military Veterans for America, and the same private, nonprofit veterans' service corporation as discussed in Finding 4, without using any competitive process. The Arizona Procurement Code requires that state agencies issue an invitation for bid or request for proposal when purchasing services exceeding the sealed bid threshold, which in 2002 was \$35,000. Despite repeated instruction from State Procurement Office administrators and department staff that the Arizona Procurement Code applied to Donation Fund monies, Mr. Chorpenning failed to use either method when purchasing media and advertising services totaling \$382,757. See Table 6 below.

Table 6: Summary of the Media and Advertising Services Paid for by the Department July 2002 to April 2005

| Fiscal Year | Marketing & Advertising | Consulting, Public and Media Relations | Miscellaneous | Military Veterans for America | Services Not Received | Total |
|--------------|-------------------------|--|------------------------|-------------------------------|------------------------|-------------------------|
| 2002 | \$ 2,000 | \$ 6,000 | \$ 1,000 | \$ 7,200 | - | \$ 16,200 |
| 2003 | 83,226 | 46,498 | 62,032 | 78,289 | - | 270,045 |
| 2004 | 2,550 | 31,500 | 15,062 | - | \$31,500 | 80,612 |
| 2005 | 900 | 7,500 | - | - | 7,500 | 15,900 |
| Total | <u>\$88,676</u> | <u>\$91,498</u> | <u>\$78,094</u> | <u>\$85,489</u> | <u>\$39,000</u> | <u>\$382,757</u> |

Source: Auditor General staff analysis of Arizona Department of Veterans' Services, Arizona Department of Administration, private business, and nonprofit organization records.

The Department's finance and purchasing staff were unaware of Mr. Chorpenning's arrangement for these services until the vendor began issuing invoices. When staff approached Mr. Chorpenning about the lack of procurement, he stated that he had a personal relationship with the vendor's owner and wanted to use the vendor's services because they were good. However, by failing to follow sound procurement practices, the Department may not have received the best value for the services received.

Mr. Chorpenning failed to require a written agreement between the Department and the vendor for the media and advertising services.

In addition to circumventing procurement rules, Mr. Chorpenning also failed to require a written agreement between the Department and the vendor. This agreement should have documented all services to be provided by the vendor and established accountability for those services. Instead, the vendor provided an estimated cost of services on a project-by-project basis.

Mr. Chorpenning exceeded the Department's spending limit of \$250,000

Spending limits are governed by the Arizona Procurement Code, Arizona Governor's Executive Orders, and Arizona State Procurement Office Technical Bulletins. The State Procurement Office determines the limit for each state agency and, beginning in 2002 up to the present date, the Department is permitted to contract for purchases up to \$250,000. Limits are in place to prevent state agencies from entering into contracts that they are not equipped to adequately administer.

However, from July 2002 to April 2005, Mr. Chorpenning exceeded the Department's allowable spending limit of \$250,000 for the media and advertising services project without following any competitive procurement process. Further, Mr. Chorpenning failed to properly seek or receive permission from the State Procurement Office to exceed the maximum limit. In fact, Mr. Chorpenning exceeded the Department's limit by more than \$132,000. Mr. Chorpenning signed authorization forms acknowledging the Department's spending limit thresholds, which were then submitted to the State Procurement Office. During his tenure with the Department, Mr. Chorpenning signed three of these letters, in 2000, 2002, and 2006.

As a result of Mr. Chorpenning's actions, the State Procurement Office may revoke, suspend, or modify the Department's procurement authority for failure to comply with state laws, rules, and regulations.

Mr. Chorpenning exceeded the Department's allowable spending limit for the media and advertising services project without following any competitive procurement process or seeking approval from the State Procurement Office.

Mr. Chorpenning improperly promoted a private trade name

Of the total \$382,757 that the Department expended on media and advertising services, at least \$85,489 was expended for services the vendor provided on behalf of Military Veterans for America (MVFA), an organization in name only. Specifically, from August 2002 to October 2003, the vendor invoiced the Department for services related to MVFA, including consulting and public relations, providing a marketing video, radio and television commercials, footage for a press conference, and a project operations staff person.

Mr. Chorpenning attempted to create MVFA, reportedly to promote veterans' license plate sales, and helped market it as a nonprofit organization that enhanced and raised awareness for veterans' issues, not only in Arizona, but nation-wide. However, no records exist documenting MVFA as a legitimate nonprofit corporation. There are no officers, members, or shareholders.

Mr. Chorpenning asked his personal trainer to voluntarily speak at a press conference, representing himself as the Executive Director for Military Veterans for America, even though he was not.

Mr. Chorpenning worked with the vendor to create a branding message, logo, Web site, and brochure materials to advertise MVFA. Additionally, Mr. Chorpenning authorized the use of Donation Fund monies to pay for a marketing video costing \$30,986 and organized a press conference to campaign for MVFA costing \$6,734. Mr. Chorpenning asked his and his wife's personal trainer to voluntarily speak at the press conference and represent himself as MVFA's Executive Director, even though he was not. While the personal trainer represented himself as MVFA's Executive Director at the press conference, he later stated to Auditor General staff that he did not have any involvement in MVFA other than this speaking engagement.

The public purpose for these disbursements was not identified, and the cost appears to greatly exceed any benefit to the public. Mr. Chorpenning authorized and paid for these services on behalf of MVFA even though MVFA was not an established corporation and these services offered little or no quantifiable benefit to the Department or Arizona veterans.

Mr. Chorpenning allowed the expenditure of public monies for services not received

Of the total \$382,757 the Department expended on media and advertising services, \$39,000 was expended for services the vendor supposedly provided to the same private, nonprofit corporation as discussed in Finding 4. From November 2003 to March 2005, the vendor invoiced the Department for both the nonprofit's and Department's monthly services such as consulting, public relations, and media relations. However, both the vendor and the nonprofit director stated that no services were provided to the nonprofit corporation. The vendor assumed that Mr. Chorpenning, his staff, or the nonprofit director had instructed vendor staff to prepare these invoices; however, both the nonprofit director and department staff deny this. Additionally, the vendor failed to produce any written documentation to support the purposes of its invoicing or services it provided to the nonprofit or the Department. Department staff paid for all media and advertising service invoices at the direction of Mr. Chorpenning. Mr. Chorpenning failed to establish a business climate that prudently monitored these services, and as a result, \$39,000 was expended for services not received.

In accordance with A.R.S. §41-2616, "A person who intentionally or knowingly contracts for or purchases any material, services or construction pursuant to a scheme or artifice to avoid the requirements of this chapter . . ." could be in violation of the law and subject to a class 4 felony. Further, "A person who contracts for or purchases any material, services or construction in a manner contrary to the requirements of this chapter . . . is personally liable for the recovery of all public monies paid plus twenty per cent of such amount and legal interest from the date of payment and all costs and damages arising out of the violation."

RECOMMENDATIONS

To help ensure proper control over public monies, the Arizona Department of Veterans' Services (Department) should ensure that the following actions are taken:

1. The Department should institute policies and procedures that effectively oversee management and address the risk of management override. For example, department management should strengthen their understanding of the business and control climates, brainstorm potential fraud risks within the Department, cultivate a strong whistleblower system, and consistently maintain an appropriate level of independence and skepticism. In doing so, the Department increases the likelihood of preventing, deterring, and detecting fraudulent activity.
2. The Department must take greater care to ensure its employees' compliance with conflict-of-interest statutes and can do so by establishing procedures to periodically notify employees of the requirement to disclose conflicts of interest. In accordance with A.R.S. §38-503, the Department should require all employees who have, or whose relative has, a substantial interest in any department contract, sale, purchase, service, or decision to file a conflict-of-interest statement and refrain from voting upon or otherwise participating in any manner as an employee in that contract, purchase, or service. In addition, if an employee supervises a relative, the employee's conflict-of-interest statement should describe the relationship, and the supervisor must refrain from participating in decisions or contracts relating to that relative, such as hiring and approving pay increases. A.R.S. §38-502(9) defines a relative as a parent, child, sister, brother, spouse, grandchild, grandparent, mother-in-law, father-in-law, brother-in-law, sister-in-law, or stepchild. A separate file should be maintained for public inspection of all known conflicts of interest and monitored by the Department periodically.
3. The Department should strengthen its employment process by ensuring open competitive practices in recruitment, selection, and placement of candidates based on the merit of the candidate's knowledge, skills, and abilities; overall qualifications; and overall fitness for the position responsibilities. The Department must take greater care to ensure that it follows state regulations by

instituting an open recruiting process; establishing procedures for posting vacancy announcements; creating evaluation criteria, including written and performance tests and interviews, and requiring an employment application prior to selecting a candidate.

4. The Department should ensure the prudent use of public money, and more specifically the proper use of Donation Fund and Veterans' Home Fund monies. Public money should not be used for private benefit unless that benefit is incidental to a public purpose being served by the expenditure and the public value is not far exceeded by the amount being paid. Expenditures should be approved only if they support the Department's needs in its role to serve the public, and in particular, Arizona veterans, their dependents, and surviving spouses. The Department should not pay for services on behalf of, or loan or gift public monies to, any organization, corporation, or nonprofit entity.
5. Prior to using Donation Fund monies to make significant purchases of goods or services, the director should consider discussing the project with the Department's legal representative. This will help ensure the Department's compliance with applicable state laws, regulations, and executive orders.
6. The Department must take greater care to ensure that it follows the State's procurement regulations, including the use of written contracts. In addition, the Department must ensure that all contracts for purchases exceeding the sealed bid threshold (currently \$50,000) are awarded in compliance with the Arizona Procurement Code as outlined in Arizona Revised Statutes and the Arizona Administrative Code. These rules exist to help ensure that state agencies receive the best possible value for the public money they spend by prohibiting the restraint of free trade and unreasonable reduction of competition among vendors.
7. The Department should ensure that expenditures are processed based on proper documentation. Such documentation includes, but is not limited to, properly and timely approved purchase requisitions, purchase orders, vendor invoices, and vendor contracts. Further, the Department should take the necessary actions to recover the monies it paid to the media production company for services that it did not receive.
8. The Department should establish periodic monitoring procedures to ensure that all policies and procedures prescribed by Arizona Revised Statutes, Arizona Administrative Code, and Arizona Governor's Executive Orders are being followed.

CONCLUSION

Arizona citizens, in general, and Arizona veterans and their families, in particular, were deprived of proper and prudent management of veterans-related monies by former Arizona Department of Veterans' Services Director, Patrick Chorpenning, Sr., who misused department monies and improperly used his position to obtain salary and other benefits for his family members.

As a result, on November 18, 2009, the Arizona Attorney General's Office took criminal action against Mr. Chorpenning through the State Grand Jury. This action resulted in the indictment of Mr. Chorpenning on eight felony counts related to conflict of interest, fraudulent schemes and practices, misuse of public monies, and procurement fraud.