

# Health care internal audit: Identifying prevalent risks within your organization

## Overview

The health care sector continues to go through many changes, presenting several new risks and a host of complicated regulatory requirements. Recent legislation with respect to health care reform has already changed the way everyone does business, and will have further — and perhaps unforeseen — ramifications for the industry. There have been many modifications to health care regulations, and consequently the risks within organizations must be effectively evaluated now more than ever.

The demands on health care administration are increasing in what is a complex and highly competitive environment. Risks are seemingly around every corner for health care organizations, from legislation and regulatory developments to operational and financial concerns. It is sometimes difficult to be aware of emerging and existing risks while maintaining your focus on your organizational strategy, mission and patient care.

With this in mind, it is important to identify, prioritize and thoroughly evaluate the risks that impact your organization. While there are risks that are specific to your organization, there are also those that are likely specific to your organization, depending on your mission and operations. As you define new objectives and implement new initiatives, and as regulatory demands change, the risks that your organization is exposed to tend to evolve as well. The method with which you assess risk must therefore be flexible.

## Risk assessment

To evaluate and address the risks involved with your organization, undergoing a thorough risk assessment is a very beneficial exercise. Such an assessment takes a holistic view of your organization to understand your goals, objectives, processes and governance structure.

It is the systematic process of identifying all areas in your health care system that could be audited, and the presence of risks in those areas. The goal is to include as much as you possibly can, so that you don't overlook an area that could be important.

There are numerous risks that could be present within a health care system, and just as many ways to select the ones to be analyzed in the risk assessment process. It would be advisable to choose a smaller number of risks that are easy to quantify, and are relevant for the industry and your health system. Risk factors that fit these qualifications and can be used for the risk assessment at your health care system are operational, compliance, financial, environmental, clinical and reputational.

Once the processes are identified, a risk assessment of the inherent risks and internal control structure is performed so that a uniform risk is applied across the organization. These risks will be presented to management and the board. If the risk assessment has been performed by an internal auditor, the assessment is transposed to a "heat map" for illustrative purposes (see image below), and then transformed into an annual audit plan. Depending on the number of risks identified, risks that are not addressed by audits during the year would remain on the heat map and could be added to a three to five year audit plan/focus.



## The internal audit process

An internal audit is an independent appraisal to provide assurance to the organization that its financial and operational controls are sufficient. This procedure compares organizational policies and procedures in relation to required compliance demands. Auditors are not responsible for executing organization activities; however, they advise management and the board of directors on how to more efficiently execute their operations.

Based on the risk assessment of the organization, internal auditors, management and oversight boards establish and agree upon an annual audit plan. Typically this plan will provide a brief overview of the entities to be reviewed and the time frame for the audit to be performed. Before the audit commences, organization management develops and reviews the scope and objectives of the audit.

The internal audit will then proceed into fieldwork, which includes interviews with appropriate management and testing, depending on the specific scope of the audit. The audit evaluates the controls the organization has in place and — taking current risks and compliance demands into consideration — determines if new processes or controls are needed. Upon completion, a report of the audit findings is prepared and shared with the organization where corrective actions are collaboratively developed. After a finalized report is prepared and approved by management, it is presented to the organization's audit committee.

## Internal audit goals

Every area of your operations can be reviewed as a part of an internal audit, including some facets that may not appear to be exposed to risk. Internal audit objectives related to the previously outlined risk areas include:

**Charge Description Master:** The purpose of this review is to evaluate processes and controls over the accuracy, completeness and timeliness of capturing, recording and reconciling patient charges; and to evaluate system access controls.

**Pharmacy:** The purpose of this review is to evaluate areas such as: purchasing and receiving, contract administration, inventory control, drug distribution, charge capture, controlled substances, security, compliance, employee prescription purchases, information systems and outpatient pharmacy operations.

**One-day stays:** The purpose of this review is to assess the effectiveness of the internal controls as they relate to medical reasonableness of inpatient admissions, as well as the ability to detect admissions that do not meet inpatient criteria to comply with CMS regulations and OIG guidelines.

**Managing cash activities:** The purpose of the review is to determine whether the internal controls are adequate for areas that handle cash directly. This includes, but is not limited to, all patient cashiering areas, all petty cash funds, cafeteria cashiering and vending machines.

**Admitting and registration of patients:** The purpose of this review is to: (1) evaluate the adequacy of the system of internal control in all admitting areas, including the emergency department; (2) determine whether the system of internal control is functioning as intended; (3) determine that resources are used in an economical and efficient manner; and (4) ensure that controls over capturing, recording and collecting revenue are adequate.

**Laboratory:** The purpose of this review is to evaluate the adequacy of the system of internal controls for the laboratory department; determine whether the systems of controls are functioning as intended; and to ensure compliance with applicable policies and procedures.

**Charity care:** The purpose of this review is to assess the effectiveness of the internal controls as they relate to the following hospital/business office guidelines as they relate to charity care.

There are a variety of strategies for executing an internal audit. RSM's methodology is a four-step process (see image on next page), taking a holistic look at the organization and its processes. These steps are risk assessment (as discussed earlier), annual internal audit plan development, audit program development and execution, and findings and recommendations.



## Annual audit plan development

After the risk assessment has taken place, an audit plan is built depending on the findings and processes of the organization. This plan identifies the key processes and auditable entities that were found to require regular testing and examination. These processes are ranked according to potential risk and placed in a rotation to allow available resources and the audit schedule to align.

## Audit-based program development and execution

Based on the audit plan developed in the previous step, work plans are developed for each key process and auditable entity. An initial audit plan is developed, addressing the risk and process objectives. This plan normally includes a detailed analysis of the audit objective, scope, period, auditable entity, process owner, audit steps and testing requirement.

Other common steps that take place in the development and execution process include:

- Developing documentation that details prevalent risks, their potential impact and control activities in place to mitigate them.
- Walkthroughs of control activities to ensure that they are performed as described.
- Designing a test plan, including sampling the methodology.
- Analyzing exceptions and offering viable recommendations to mitigate the recurrence of problem areas.

## Findings and recommendations

A final report is produced and, after being approved by management, is presented to the audit committee for review. The committee has the responsibility to provide oversight and direction to the internal audit function. The internal auditor should continue to hold regular meetings with the audit committee to discuss any issues that have been discovered that could result in a change to the annual audit plan.

## Conclusion

The current business atmosphere among health care organizations is very complex and competitive. There are pervasive risks in all facets of your operations and an increasing amount of regulatory requirements that your organization must comply with. As management sets objectives and identifies processes, a successful risk assessment and internal audit can help to locate high-risk areas within your operations as well as potential opportunities. This process will allow your organization to more efficiently determine where resources should be allocated.

*The Healthcare Services Group specializes in providing accounting, tax, payroll & employee benefits, practice management, consulting, compliance and other services to physicians, clinics, hospitals and healthcare systems, ambulatory surgery centers, dentists, orthodontists and other healthcare providers.*

*Source: RSM US LLP. Used with permission as a member of the McGladrey Alliance. [http://rsmus.com/pdf/health\\_care\\_internal\\_audit.pdf](http://rsmus.com/pdf/health_care_internal_audit.pdf)*

*The information contained herein is general in nature and based on authorities that are subject to change. RSM US LLP guarantees neither the accuracy nor completeness of any information and is not responsible for any errors or omissions, or for results obtained by others as a result of reliance upon such information. RSM US LLP assumes no obligation to inform the reader of any changes in tax laws or other factors that could affect information contained herein. This publication does not, and is not intended to, provide legal, tax or accounting advice, and readers should consult their tax advisors concerning the application of tax laws to their particular situations. This analysis is not tax advice and is not intended or written to be used, and cannot be used, for purposes of avoiding tax penalties that may be imposed on any taxpayer.*