How and when should you leverage internal audit?
March 28, 2017

Agenda

• Internal Audit foundation
• 3 lines of defense
• Trends in consultative & value enhancement work
• Why you should care
• Key takeaways
What are your initial thoughts on internal audit?

Boring! Adversaries!

Who? Strategic Partner?

Nuisance! Blocking and tackling

Gotcha! Financials

Sleepy time!
**Internal audit overview**

What is internal audit?

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”

- The Foundation for the IIA Standards

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**Wait! Before we go on...**

....isn’t internal audit the same as compliance or quality assurance?

Great question!

What do you think?

Are they the same? How should they differ?
### 3 lines of defense

<table>
<thead>
<tr>
<th>Risk Management Framework</th>
<th>Internal Audit</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Business Management</strong></td>
<td><strong>Compliance and Quality Assurance</strong></td>
</tr>
<tr>
<td>First line of defense</td>
<td>Second line of defense</td>
</tr>
<tr>
<td>Not independent</td>
<td>Independent</td>
</tr>
</tbody>
</table>

- **First line of defense**
  - Reports on organization’s performance
  - Owns day to day control activities
  - Designs & operates controls
  - Considers costs & benefits
  - Re-evaluates processes & controls
  - Communicates risks & needs to board
  - Establishes escalation methods
  - Remediates identified risks

- **Second line of defense**
  - Monitors, consolidates & reports on control performance
  - Collaborates with management to execute controls & set best practices
  - Verifies risk objectives are being met
  - Monitors remediation efforts & provide inputs as needed
  - Typically focuses on regulatory requirements

- **Third line of defense**
  - Periodically verifies the completeness and accuracy of management reported activities
  - Provides assurance controls are designed & operating effectively to mitigate risks
  - Reports on fraud risk
  - Escalates non-performance to governing bodies
  - Verifies remediation plans mitigate identified risks
  - Can focus on regulatory and institutional operational requirements

### Internal audit vis-à-vis compliance

<table>
<thead>
<tr>
<th>Internal Audit</th>
<th>Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Definition</strong></td>
<td>Independent, objective assurance and consulting activity designed to add value and improve operations</td>
</tr>
<tr>
<td><strong>Purpose</strong></td>
<td>Preserve corporate integrity and adherence to a code of organization ethics and ensure compliance with regulatory matters</td>
</tr>
</tbody>
</table>
  - Independent appraisals of governance, risk and control
  - Review reliability and integrity of financial information
  - Safeguarding of assets
  - Review consistency with operational goals and objectives
  - Recommend operating improvements |
  - Encourage the use of internal controls to monitor adherence to applicable regulations
  - Effect change as necessary to achieve regulatory compliance
  - Create organizational compliance policy and procedure, compliance training
  - Protect and secure PHI
  - Implement HIPAA Privacy and Security standards |
| **Authority**  | Audit Committee Charter
                | Internal Audit Charter |
| **Management Relationship** | Compliance Program
                          | Compliance Committee Charter |
| **Expertise**  | Independent with no operational responsibilities; reports directly to Board or Audit Committee; does not own policies |
| **Internal Controls** | Primarily with internal controls |
| **Compliance** | Operational responsibility for administering the compliance program; reports to management; may create and / or own policies |
| **Internal Controls** | Confirm internal controls are designed and operating effectively |
| **Expertise**  | Primarily in regulatory matters |
| **Compliance** | Understand, help design and encourage the use of internal controls |
**State of the internal audit profession**

- Shifting from retrospective → prospective
- Innovation
- Moving from value protection → value enhancement
- Alignment with business objectives & strategic initiatives
- Collaboration with second line of defenses
- Right mix of talent and business acumen
- Effective & timely communication
- Follow-up and monitoring process

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**Internal audit value enhancement opportunities**
Internal audit value enhancement opportunities

Internal audit can provide a wide range of value-added services ranging from traditional financial assurance to organizational-wide risk management / governance models. Specifically, **management is now looking for a partner to advise during critical and strategic initiatives.**

Range of Internal Audit Activities

- Objective and systematic perspective
- Aligned with management strategic business objectives
- Value add recommendations & enhancement opportunities

Internal audit can help navigate the changing technology landscape

**Internal Audit functions need to evaluate their maturity and ability to help the business identify risks and opportunities in the new technology era.**

- **Staffing & Talent Management**
  - Allocating right resources towards technology audit function
  - Strategic co-sourcing to augment specialized technical skills

- **Strategic Partnerships**
  - Collaborating with information technology to help manage risk and help solve business problems
  - Changing perception from being an “auditor” to “advisor”

- **Managing Increasing Expectations**
  - Helping companies address risks and identify opportunities in cybersecurity and emerging technologies
  - Keeping Boards and Audit Committees informed

- **Change Agents**
  - Acting as change agents to drive innovation and change in Internal Audit and business
  - Differentiating through skills, focus area, and agility to drive value and impact

- **Focusing on the Right Risks**
  - Being relevant by aligning audits and reviews to enterprise-level risks, key initiatives, and relevant hot topics
  - Conducting continuous or dynamic risk assessment

- **Developing Technology Skills**
  - Leveraging technology as part of delivering audit engagements
  - Building, training, and retaining technical capabilities to perform strategy, quality, and value-based technology audits
Internal audit analytics

With the changing organizational risk landscape facing organizations, Internal Audit must focus the right level of testing at the optimal time.

Internal Audit analytics methodology should use flexible, tailored technology throughout the audit lifecycle to highlight, measure, and react to key risk areas, resulting in the right audit coverage, depth and breadth.

Analytics-Enabled Internal Audit Methodology

The approach should tailor the use of analytics to your audit process and audit mandate to provide you with:

- Enhanced capabilities and re-usable analytics across risk areas
- Visibility to risk indicators when and where you need it
- Increased insight to transaction processing and compliance metrics
- Consistent use of analytics to maximize coverage where you need it

Sample Toolkit and Accelerators

Core technical capabilities: visual analytics, risk scoring, data profiling, CAATs, data science and predictive modeling, unstructured data analysis, text analytics, dashboarding, alert monitoring, process interrogation and time sequencing.

Sample projects and coverage

<table>
<thead>
<tr>
<th>Internal Audit Engagements</th>
<th>Compliance Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value Based Program Implementation</td>
<td>CMS Admission Criteria - Inpatient Status vs. Observation/ Outpatient</td>
</tr>
<tr>
<td>Ambulatory Expansion Risk Management Assessment</td>
<td>Admission Orders (Inpatient/ Observation)</td>
</tr>
<tr>
<td>Clinical Research Billing Consultation</td>
<td>Evaluation and Management Services - Facility Level Coding Accuracy</td>
</tr>
<tr>
<td>Entity Level Controls Readiness Assessment</td>
<td>Anesthesia services - Payments for personally performed services</td>
</tr>
<tr>
<td>Medical Device Security Assessment</td>
<td>HIPAA / Privacy Program</td>
</tr>
<tr>
<td>Epic Billing Reimbursement Assessment</td>
<td>Attending Physician Billing Compliance</td>
</tr>
<tr>
<td>Pharmacy Operations Management</td>
<td>Hospital Same - Day Discharges and Readmissions</td>
</tr>
<tr>
<td>Emergency Preparedness and BCM Review</td>
<td>Provider Based Billing Status - Medicare</td>
</tr>
<tr>
<td>340B Data Analytics</td>
<td>Manufacturer Recall Credits</td>
</tr>
</tbody>
</table>
Why should I care?
How does this impact me?

Audit findings - material impacts

Is your internal audit function helping you to manage these risks?
How comfortable are you with your processes and internal controls?

<table>
<thead>
<tr>
<th>Institution</th>
<th>Amount</th>
<th>Reason</th>
</tr>
</thead>
<tbody>
<tr>
<td>University of Minnesota</td>
<td>$32M</td>
<td>Misuse</td>
</tr>
<tr>
<td>NYUMC</td>
<td>$15.5M</td>
<td>Inflated research costs</td>
</tr>
<tr>
<td>Tenet Healthcare</td>
<td>$54M</td>
<td>False Claims Act (kickbacks)</td>
</tr>
<tr>
<td>UCLA</td>
<td>$8.5M</td>
<td>Conflict of interest disclosure</td>
</tr>
<tr>
<td>Mayo</td>
<td>$6.5M</td>
<td>Mischarging grants</td>
</tr>
<tr>
<td>Advocate</td>
<td>$5.55M</td>
<td>Laptop data breach / HIPAA violation</td>
</tr>
<tr>
<td>Northwestern</td>
<td>$3M</td>
<td>Effort</td>
</tr>
<tr>
<td>Cardinal Health</td>
<td>$4.4M</td>
<td>Memorandum compliance due diligence</td>
</tr>
<tr>
<td>Cornell</td>
<td>$4.4M</td>
<td>Clinical research</td>
</tr>
<tr>
<td>Harvard/BIDMC</td>
<td>$3.29M</td>
<td>Costing</td>
</tr>
<tr>
<td>Medtronic</td>
<td>$77M</td>
<td>Price fixing in China</td>
</tr>
<tr>
<td>Rideout Health</td>
<td>$2.4M</td>
<td>Drug records mismanagement</td>
</tr>
<tr>
<td>NY Presbyterian</td>
<td>$2.2M</td>
<td>Patient consent / HIPAA violation</td>
</tr>
<tr>
<td>MedStar Hospitals</td>
<td>Bitcoin</td>
<td>Ransomware attack / held data hostage</td>
</tr>
<tr>
<td>UCLA</td>
<td>TBD / $865K</td>
<td>Data breaches</td>
</tr>
<tr>
<td>Trinity Health</td>
<td>$75M</td>
<td>Pension mismanagement</td>
</tr>
</tbody>
</table>
**Internal audit transformation - areas of focus**

Ensure you obtain the results of all reports issued by other auditors and discuss with auditors and consider any implications to the current year audits. For example:

- External audits of financial statements
- Government / regulatory audits (HRSA, JCAHO, OIG, etc.)
- A-133 reports
- Effort reports
- Second line of defense findings (compliance, quality assurance, etc.)

Understanding the above plus management’s current strategic initiatives, current internal audit functions should be focusing on adding value in:

- Mergers & acquisitions
- Value based programs
- Clinical integrated networks
- Enterprise risk management
- Shared service centers / central business offices
- Quality measures improvement
- Cost allocations / funds flow
- Cybersecurity
- Research / clinical trials

**Key takeaways**

- Internal audit does more than protect the base
- Independence requirements do not impede internal audit from providing consultative services and value enhancement
- Leverage your internal audit as another resource
- Include internal audit as another work stream / department
- Ask your Board and Audit Committee if they are receiving the value expected from internal audit
Questions

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