STEVEN FORMAN

Compliance Program Leveraging of Audit Resources

Compliance and Auditing Must Work Together to Coordinate Efforts and Avoid Duplication

Steven Forman, CPA, is senior vice president at Strategic Management Services. He has over 40 years experience in financial management and accounting, internal auditing, and compliance consulting and has served in a variety of executive and management positions as a controller, compliance officer, head of internal audit, and director of management operations for the U.S. Department of Health and Human Services (HHS) Office of Inspector General (OIG). He served 10 years as vice president for Internal Audit and Compliance for the largest acute care provider in New York. He can be reached at sforman@strategic.com.

The compliance officer is an independent and objective fact finder with the mission of ensuring the organization is in compliance with all applicable laws, regulations, standards, policies/procedures, and the code of conduct. A compliance officer's major focus is the compliance high-risk areas; however, there are other functions that share some of the same space — internal audit and the external auditors. They also conduct their work independent of management, in an objective manner, to address high-risk areas. With limited resources available to all three functions, it is important and makes sense that they coordinate their efforts and take steps to avoid duplication.

One thing is very clear and that is: "one size does not fit all." Larger organizations can more fully staff their internal audit function to perform a wide range of audit activities, especially for those organizations that are "covered entities" under the Sarbanes-Oxley Act where there are prescribed internal control review requirements. Mid-size organizations, however, may have only very limited resources available for internal auditing and may have to contract out parts or all of the function — or not have the function at all. Smaller organizations are not likely to have any internal audit function.

For health care providers, the compliance officer is responsible for the operation of the organization's compliance program; however, to be successful it is necessary to rely on operations managers to ensure that rules, regulations, and laws are being followed. The question, of course, is how does the compliance officer know that management is, in fact, carrying out its responsibilities effectively? Unfortunately, the compliance officer will never possess sufficient staff or resources to enable direct verification of effectively complying with all applicable laws, regulations, rules, standards, policies, et cetera. The answer to this problem is being able to properly leverage others to assist in this process. For those organizations with an internal audit function, the compliance officer should have engaged continuous contact and discussions with them. Furthermore, this contact should have led to substantive discussions with the external auditors. These two functions are similar to the compliance officer in that they are independent of program management and, as such, represent the best opportunities for leveraging limited resources.

Internal audit is an independent appraisal function within an organization that examines and evaluates its activities as a service to that organization. Internal audit's role varies in different settings, depending on a number of factors such as size and complexity of the organization as well as the scope of work set aside for the external auditor and, in recent years, the growing role of the compliance officer. Its value lies in the fact that the function: (1) is independent (and should *not* report to management other than the chief executive office (CEO) and *should* report to the Audit Committee of the board); (2) is objective (no self-serving agenda); (3) employs a systematic, consistent, standard-based, disciplined approach to evaluate and improve the effectiveness of risk management, controls, and governance processes; (4) is able to furnish analyses, appraisals, recommendations, counsel, and information concerning the activities reviewed; and (5) has considerable expertise and understanding with regard to systems of internal controls — those mechanisms your organization needs to protect itself from the impact of noncompliance.

Generally, the internal audit function is broad in that it can be applied to both financial and non-financial arenas. Its activities should mirror the universe of significant risks to the organization. In carrying out the mission, internal audit should develop an annual audit plan based on an enterprise-wide risk assessment that addresses such areas as financial management and controls, information technology, operations, *and* compliance with applicable rules, regulations, and laws.

While external auditors are not part of the organization, they are engaged by it to provide annually an independent opinion on the organization's financial statements. Their scope of work and objectives are normally set by the Audit Committee of the Board. They seek to test the underlying transactions that form the basis of the financial statements in order to render an opinion as to whether the statements present fairly the financial condition and transactions of the organization. In doing so they must evaluate the adequacy of internal controls as they relate to the financial statements.

They are also required to consider the existence of fraud as they conduct their audit — something that clearly falls within the area of interest of the compliance officer — especially if there are systemic weaknesses discovered either related to a suspected fraud or some other lack of internal controls. Since internal control weaknesses can translate into compliance issues, knowing where those weaknesses exist may give the compliance officer some ideas as to the areas it should be targeting in its own verification activities.

With regard to internal audit, it will be called upon to complete tasks in support of the external auditors. In that vein, it will utilize work plans and protocols approved by the external audit firm. Its work will also be supervised and validated by the external auditors. This can have three potential benefits — 1) reduce the audit fee; 2) provide additional experience for internal audit staff that they otherwise might not obtain; and 3) help internal audit expand its own coverage of the universe of risks faced by its organization. Such work, however, must be carefully planned and coordinated to ensure that maximum benefits are realized and avoid unnecessary burdens being placed on the operations being audited.

Internal audit should coordinate and work with the compliance officer in addressing compliance high-risk areas such as auditing of program operations to determine if managers are meeting their obligations for ongoing monitoring for compliance with applicable rules, regulations, and laws and determining the level of effectiveness of those controls in meeting objectives.

Fundamentally, the role of internal audit is to validate where management believes problems, issues, or weaknesses exist as indicated in management's monitoring activities. If this is to occur efficiently, management must have developed effective internal controls, including metrics that identify problems in real time. If management has to wait for the results of an audit to know there is a problem, then it simply is not doing its job.

In that same vein, the compliance officer depends on the organization's managers to ensure their operations are conforming to existing rules, regulations, standards, and laws. The compliance officer should look upon internal audit to help him or her verify that fact. This can be accomplished by including compliance-related audits in the audit plan. One way to complete this task more efficiently is to have internal audit add compliance tests in its audit protocols. So, for example, if internal audit is going to conduct a revenue cycle audit, it should include compliance elements (*e.g.*, does medical record documentation support coding and billing) in that audit.

One other way that internal audit can provide support to the compliance function is in a consulting capacity. As noted, internal audit understands the necessity for internal controls and how they are supposed to work. Internal audit should be able to provide valuable advice in helping operating managers strengthen their own internal compliance controls and set up tests and metrics to be able to verify that the controls are working as intended. This should in no way affect internal audit's independence as operations are still responsible for the controls and cannot abdicate this responsibility. Consulting is clearly a function envisioned by the Institute of Internal Auditors.

With the growth of the compliance officer functions in health care organizations, at times the lines between it and internal audit can become blurred. In smaller organizations, it is not uncommon to find the internal audit function being subsumed under the compliance officer, by the external auditor. At the other end of the spectrum, in larger organizations, there can be significant tensions between internal audit and the compliance officer, bordering on a "turf war." This should not be the case if each function understands how it can support the other in meeting their respective responsibilities. Both benefit, and more importantly, the overall organization benefits from coordinated effort; and if you add to that equation the external auditor, some real leverage and efficiency can result along with more effective program oversight.