Audit and Compliance Committee Conference
Financial Reporting

PRESENTED BY:
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February 12, 2008
• Purpose
  – As an expression of our value of stewardship, the Catholic Healthcare West (CHW) Audit and Compliance Committee is responsible for providing oversight assistance to the Board of Directors in fulfilling its fiduciary responsibility and accountability relating to the following (see next page):
• Corporate accounting and reporting practices
• The quality and integrity of financial, operational, mission integration and corporate integrity reports of CHW
• A reliable system of internal controls, including operational controls
• Compliance with applicable laws and regulations
• Implementation of plans designed to prevent and/or detect violations of law, regulation or CHW policy
• Education standards related to the functions of the CHW Audit and Compliance Committee
• Mission Integration standards
• Understand: accounting and financial reporting process
• Ensure: leadership competency and transparency
• Review: adequacy of internal controls and testing environment
• Review: IT security and controls
• Receive: Recommendations for improvement
Understanding Accounting and Reporting Processes
Key Areas of Management Accounting and Reporting Processes

- Consolidation accounting
- Accounting policies and adherence
- Accounts receivable valuations
- Third party settlement estimates
- Reserves
- Off-balance sheet entities
- Financial statements
Consolidation – Questions to be Asked

- Automated tools
- Timing (close period) – comparable to industry standards?
- Management review of submissions
  - Financial statements with prior year and budget variances
  - Additional schedules
    - Quality of earnings (i.e. scrubbed vs. proforma earnings)
    - Facility narratives (business model understanding)
- Close process
  - Documentation environment
  - Review environment and variance analysis
Accounting Practices – Questions to be Asked

- Policies
  - Documented
  - Updated
  - Adherence (tested by internal and external auditors)

- Accounting and reporting manual

- Standardization of accounting methods
Accounting Practices

- Key accounting principles
  - Equity method for joint ventures
  - Capitalized interest and labor
  - Pension assumptions and methods
  - Malpractice assumptions and methods
  - Investment valuations
  - Operating versus non-operating definitions
  - Standard net A/R calculations and bad debt reserve process
  - Asset impairment reviews
• Periodic interim reviews completed
  – Internal audit
  – External audit
  – Vendor testing of revenue cycle process (charge capture, coding, billing)

• Aging of A/R and bad debt allowance trends
Key ratio trends to observe:

- Days revenue in accounts receivable
- Net A/R as a percentage of total A/R
- Net revenue compared to cash and A/R days
- Bad debt and charity as a percentage of gross charges
- C/A deductions
- Credit balances
- Unbilled A/R days
• Causes
  – Medicare/Medicaid audits of cost reports
  – DSH (disproportionate share) qualification
    • Federal
    • State
    • Local
  – Medicare and Medicaid claim audits
  – Blue Cross and other payors
    • Medical necessity and other denials
    • Inpatient/outpatient classification
    • Payment errors
Third Party Settlement – Background

• History of reserves and development process

• Types of reserves
  – Specific
  – General based on size, complexity of facility (should be a standard range for each facility)
• Reserves policy and modification approval process
• Auditor’s perspective (changing)
• Disclosure
  – Outstanding amounts
  – Changes period to period
Third Party Settlements – Key Questions

- What programs are subject to retroactive settlement?
- What periods or payment streams are subject to settlement?
- What periodic reviews have been done?
- What is the range of potential settlement?
Off-Balance Sheet Entities – Background

- Joint ventures not consolidated
- Financial statement review of ventures vs budget
- Investments recorded on balance sheet
- Majority partner generally controls
Off-Balance Sheet Entities – Key Questions

• Valuation: Underlying information timely and complete
• Debt, guarantees, capital call exposures
• Cash or cashless ventures
Ensure Management Competency
Forthcoming Financial Reporting

- Financials, stats and trends
- Cash flow statement
- Errors and corrections
- Explanations of variances to budget and prior year at market level
- Projections (both earning and cash)
- Quality of earnings statements
- Quarterly disclosure review
- Quarterly external audit testing results
Management Credentials and Ability – Audit Committee Role

• Involved at hiring of key executives
• Credentials and organizational chart
  – CPA’s and MBA’s
  – Government reimbursement experience
  – Industry experience
  – Reputation (feedback from internal and external audits is crucial)
  – Objective testing results should be reviewed
Audit Committee Role

- Turnover and vacancies of key positions
  - Continuing education program
  - Succession planning process
  - Diversity planning process

- Meeting interaction
  - Clarity of financial information
  - Responsiveness to questions
  - Consistency in answers
  - Full disclosure (proactive vs reactive)

- Education sessions available
Review Financial and IT Controls
Examples of Financial Controls Reporting and Practices

- **Representation letters**
  - Monthly/quarterly
  - CFO’s, CEO’s, accounting directors
  - Results summarized and various disclosed

- **Closing checklists**
  - Sign-off on compliance
  - Results summarized
Financial Controls

• Corporate office review of financial statements
  – Inquiries and follow up to field

• Tax compliance
  – Intermediate sanctions policy and procedure
  – Accountable Plan

• Reserves
  – Periodic disclosure
• Revenue capture (charges and coding)
• Revenue valuation (bad debt, charity and contractual allowances and reserves)
• Payroll including pay process and overtime calculation testing
• Purchasing/disbursements
• Closing process (monthly reconciliations of all balance sheet accounts)
• Pension information reporting
• Malpractice claims reporting
Major Areas Requiring Internal Controls and Testing

- Property, plant and equipment (purchases, capitalization and depreciation)
- Debt transactions
- Sarbanes Oxley Section 404
  - Documentation and compliance standards
  - Auditor attestation requirement
  - Alternatives available to not-for-profits
IT Controls – General Categories

• Security
  – Who has access to the system
  – Segregation of duties (programmers and users)
  – Management of passwords
  – Testing environment

• General controls
  – Can changes be made to operating systems without documentation and approval
• Application controls
  – Can changes be made without prior approval and documentation

• Testing environment to ensure compliance
• CIO present/discuss
• Understand plan to correct
Elicit Recommendations for Improvement
Recommendations for Improvement

• External auditors
  – Management letters with written management responses
  – Ask about range of conservatism
  – Ask about consistency or changes in accounting
  – Ask about accounting alternatives discussed during the year
  – Executive session
Recommendations for Improvement

• Internal auditors
  – Review follow up on findings and completion timelines
  – Ask whether policies should be changed

• Management comments
  – Will ask for guidance
Handouts

- Quarterly Financial Statement Representation
- Audit and Compliance Committee Charter
- Internal Audit Summarization Report
- Board of Director’s Highlight Report
- Stewardship Report
Conclusion