

October 27, 2014

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**Subject:        *Outpatient Pharmacy Banking and Financial Management Processes  
Audit & Management Advisory Services Project 2014-44***

The final audit report for Outpatient Pharmacy Banking and Financial Management Processes, Audit Report 2014-44, is attached. We would like to thank all Pharmacy and Finance personnel for their cooperation and assistance during the audit.

Because we were able to reach agreement regarding corrective actions to be taken in response to the audit recommendations, a formal response to the report is not requested.

The findings included in this report will be added to our follow-up system. While management corrective actions have been included in the audit report, we may determine that additional audit procedures to validate the actions agreed to or implemented are warranted. We will contact you to schedule a review of the corrective actions, and will advise you when the findings are closed.

UC wide policy requires that all draft audit reports, both printed and electronic, be destroyed after the final report is issued. Because draft reports can contain sensitive information, please either return these documents to AMAS personnel or destroy them at this time.

David Meier  
Director  
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Attachment

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# UC San Diego

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## AUDIT & MANAGEMENT ADVISORY SERVICES

### Outpatient Pharmacy Banking and Financial Management Processes October 2014

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Project Number: 2014-44

*Outpatient Pharmacy Banking and Financial Management Processes  
Audit & Management Advisory Services Project 2014-44*

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Attachment A: OP Pharmacy Accounting Process

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**I. Background**

Audit & Management Advisory Services (AMAS) has completed a review of Outpatient Pharmacy banking and financial management processes at the request of the Medical Center Controller and Pharmacy management, and as a supplemental audit on our approved audit plan for Fiscal Year (FY) 2013-14. This report summarizes the results of our review.

The Outpatient Pharmacies (OP Pharmacies) operate from five service locations within the UC San Diego Health System, and filled prescriptions with a net receivable value of \$41,212,205 for the period October 26, 2013 to March 31, 2014. Pharmacy management estimated that approximately 10% of prescriptions are cancelled or age out (a filled prescription that does not get picked up within 14 days). As such, we estimate the potential receivables from actual dispensed medications to be approximately \$37 million for this period (\$41.2 million x 90%).

Bank Accounts

Historically, OP Pharmacy revenue was processed through the Main Cashier and deposited into a single bank account, which was reconciled by the Finance accounting staff. Due to a change in business strategy and a planned increase in revenue, OP Pharmacy management requested that the Medical Center Controller work with the campus to open a separate bank account and associated lockbox for OP Pharmacy deposits to segregate its revenue and supporting documents.

The UC San Diego Controller approved the request to open the new bank account, and sent an authorizing letter to University of California Office of the President (UCOP) Banking and Treasury Services on December 4, 2013. After the account was authorized, the Controller's office created balance sheet account 110120<sup>1</sup> to record bank deposits and other transactions. The account was activated in February 2014 to receive deposits from OP Pharmacies at four hospital based locations including: Moores Cancer Center (MCC), Medical Offices South (MOS), Hillcrest Discharge, and Thornton Discharge.

The OP Pharmacies also maintained another bank account<sup>2</sup> to capture the revenue from all Medical Group locations which originally included: San Diego Cancer Center (SDCC), 4<sup>th</sup> and Lewis, Perlman Ambulatory Care Center, and La Jolla Internal Medicine Group. This bank account became active on July 2, 2011, and was reconciled monthly by School of Medicine (SOM) Controller's Office staff. In the fall of 2013 two Pharmacies were sold to an external party and one was closed, therefore, the activity in this account has been steadily decreasing. Eventually, only SDCC Pharmacy collections will be deposited into this account.

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<sup>1</sup> The account title is "BOFA DEP MC Retail Pharmacy and Operat (sic)." It is associated with hospital fund 63000 in the campus Integrated Financial Information System (IFIS).

<sup>2</sup> The account title is Ambulatory Care Pharmacy B of A-DEP

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Billing, Collections and Accounts Receivable

The PCSI Cerner outpatient pharmacy system (Cerner) is the point of sale and billing system deployed in the OP Pharmacies. Cerner is used to record filled prescription sales, verify customer insurance eligibility, and electronically submit insurance claims for covered medication charges.

When a prescription is presented at a Pharmacy, the patient's insurance coverage is verified, and co-payments due from the patient are identified by the system and collected when the prescription is picked up. The remaining cost of the prescription is billed electronically to the patient's insurance carrier in most cases. However, some prescriptions must be billed manually at a later date by staff in the Pharmacy Billing Office. Insurance companies do not pay the retail price for prescriptions. When a prescription is filled, the net expected payment (based on contracted rates) is captured in Cerner. Generally, since the amount of each payment is pre-approved, the expected payment amount is allocated to the Medical Center bulk account associated with the payer. That allocation is made by the Billing Office staff based on information obtained from the billing codes programmed in Cerner.

OP Pharmacy management has not implemented the Cerner accounts receivable (A/R) reconciliation module, but relies on entries to the bulk accounts and analytical review of payments received to predict and manage revenue. The OP Pharmacy A/R balance in the Medical Center general ledger is a calculated value entered by Finance. Bulk accounts are credited based on the explanation of benefits (EOB) attached to each payment.

The OP Pharmacies collect co-payments and cash payments for prescriptions. Generally, all Pharmacy Technicians (PTs) have cash handling responsibilities and have received the cash handling training. Pharmacists have also been trained to perform cash handling duties.

**II. Audit Objective, Scope, and Procedures**

The objective of our review was to determine whether bank account management and related financial system controls related to payments and lockboxes were adequate to ensure that all expected revenue is received and reconciled in accordance with UC policy and good business practices.

We performed the following audit procedures to achieve the project objective:

- Reviewed UC Business and Finance Bulletin BUS-49 - *Policy for Cash and Cash Equivalents Received*;
- Discussed the bank reconciliation process with Finance and SOM Controller's Office staff;
- Reviewed Cerner activity reports to identify how pharmacy revenue is recorded, reported, and collected;

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- Analyzed the manual billing process, including the management of pending charges;
- Reviewed the EPSi 110 Flexible Budget Report to determine gross revenue from the Medical Center Pharmacies; and campus Financial Link reports to verify the gross revenue for the Medical Group locations;
- Interviewed Pharmacists and staff in OP Pharmacies, the Billing Office, Finance Cashiering, and the SOM Controller's Office;
- Identified expected revenue for all OP Pharmacy locations for the period October 26, 2013 to February 28, 2014;
- Created a flowchart depicting the cash handling and revenue allocation process (*Attachment A*);
- Gained an understanding of the bank reconciliation process;
- Identified cash receipts and recorded receivables;
- Observed and /documented cash controls at selected locations;
- Identified cashiering processes for accepting deposits; and
- Traced February 2014 cash and credit card sales from the deposit log for the MCC Pharmacy to the general ledger and bank statement.

**III. Conclusion**

Based on our review procedures, we concluded that OP Pharmacy deposit and revenue reconciliation procedures, and related financial system controls were generally adequate to ensure that payments received were recorded and processed in accordance with UC policy and good business practices. Audit fieldwork confirmed that deposits were transferred to and recorded in the Pharmacy bank accounts, and were accurately recorded in the general ledger.

We noted, however, that some cash handling practices did not strictly comply with UC Policy (BUS-49). We also identified opportunities to make processes more efficient, and comply with UC standards for reporting collections and managing A/R.

These issues are discussed in more detail below.

**IV. Observations and Management Corrective Actions**

**A. Revenue Recognition and Disclosure**

**The OP Pharmacy net revenue calculation method should be disclosed in the monthly financial statements.**

The A/R reconciliation module for the Cerner system was not implemented by OP Pharmacy management because it was not considered to be cost effective due to the additional staff resources that would be required to manage the associated workload. Therefore, Finance calculated monthly revenue net of the estimated A/R balance using the Gross Revenue report generated by the OP Pharmacy Billing Office.

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On the fifth day of each month, the OP Pharmacy Billing Office manually generated the Gross Billing Report, which included the billed gross charges by payer type and store location, and forwarded the report to Finance. Based on a comparison of gross charges to payments received over a specific period of time, Finance found that historically, 95% of gross charges were collected. Therefore, the gross charges on the Gross Billing Report were reduced by 5% to record OP Pharmacy revenue. During our review, Finance staff re-evaluated the reasonableness of the 95% collectability calculation, and revised the reported OP Pharmacy revenue for FY 2014.

The revised method for calculating net revenue assumes an average 15 days of outstanding A/R. The steps followed after the end of each month to complete the calculation include:

1. Obtain the total cash collections from deposit data recorded in the general ledger (**A**) for the period October 26, 2013 (the Epic revenue cycle implementation date) through the end of the month.
2. Compute the average daily cash collected (**B**) by dividing **A** by the number of days since October 26, 2013 (**Z**) less 15 days:

$$\mathbf{B} = \mathbf{A} \div (\mathbf{Z} - 15)$$

3. Compute the estimated A/R by multiplying **B** by 15 days:

$$\mathbf{A/R} = \mathbf{B} \times 15$$

4. Compute net revenue by adding the estimated A/R to cash collections:

$$\mathbf{Net\ revenue} = \mathbf{A/R} + \mathbf{A}$$

When reconciled to Gross Billing Reports, estimated net revenue indicated a cumulative collection rate of approximately 94%.

OP Pharmacy management understands the net revenue calculation methodology. However, other users of the OP Pharmacy financial statements or monthly Health System financial reports may not be aware of the accounting estimates or how they were derived.

**Management Corrective Actions:**

1. OP Pharmacy management is evaluating the use of an outside vendor to manage OP Pharmacy A/R.
2. Finance management will consider including a footnote in the financial statements to advise the reader that net revenue is an estimate based on a consistent methodology.

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3. As of March 2014, the cost of goods sold is being recorded based on the cost of dispensed prescriptions during each reporting period.

**B. Segregation of Duties**

**Cash handling and deposit preparation activities at two pharmacy locations and the Billing Office were not adequately segregated as required by University Policy (BUS-49).**

University cash handling policy requires:

- Establishment of procedures “that ensure that no single individual is responsible for collection, handling, depositing and accounting for cash received by that unit. At least two qualified individuals must be assigned to carry out key duties of the cash handling process.”
- A unit must “provide a cash register drawer, a cash drawer insert or another secure cash receptacle to which only the cashier has access.”
- Deposits are to be “validated and prepared under dual custody at all times in a safe and secure area.”

MOS Pharmacy

We found that the MOS Pharmacy had one cash register and each Technician had unique Cerner login credentials that recorded the Technician’s identity on each sales transaction they completed. However, the register had a single cash drawer that was accessed by both Technicians during the same shift. To ensure individual accountability, each Technician should have a cash drawer that is reconciled at the end of the day.

The single cash drawer was reconciled by two individuals at the end of the business day. The cash drawer was then placed into a safe to which only Pharmacists have the combination. However, the following morning, only one Pharmacy Technician recounted the money, verified totals from the prior day, and prepared the deposit. A Pharmacist subsequently reviewed the deposit. This practice does not strictly comply with UC Policy (BUS-49), which states that “deposits must be validated and prepared under dual custody at all times” which is critical to reduce the risk of errors and misappropriation of cash or cash equivalents.



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SDCC Pharmacy

The Pharmacist was the only staff at the SDCC Pharmacy. The sales volume did not require, and could not support additional staffing for this location. The Pharmacist accepted and filled all prescriptions, entered prescription information into Cerner, dispensed the medications, and accepted payments for the drugs dispensed. The Pharmacist also prepared the deposit and reconciled the cash received to the cash register tapes. The deposit is verified by staff from the SDCC Infusion unit. This process conflicts with the UC Policy (BUS-49) requirement for segregation of duties related to cash handling.

**Management Corrective Actions:**

1. OP Pharmacy management understands the risk associated with not providing each cashier with an individual cash drawer and will continue to rely on staff Cerner access credentials as a compensating control.
2. OP Pharmacy management will:
  - a. Ensure that deposits are validated and prepared under dual custody at all locations.
  - b. Segregate SDCC Pharmacist cash handling duties to the extent possible.

**C. Frequency of Deposits**

**OP Pharmacy deposits did not strictly comply with University Policy (BUS-49) requirements.**

University Policy requires that cash and cash equivalents at sub-cashiering stations and departments be deposited weekly or when deposits on hand exceed \$500.

Billing Office staff indicated that they received insurance check payments through the mail, which are delivered to Pharmacy Administration at the Hillcrest Medical Center. The OP Pharmacy Analyst allocated payments to payer bulk accounts while preparing the deposit. Because the payment allocation was a long process, the allocation and deposits were prepared only once a week.

Loomis picked up deposits weekly and recorded them on a Customer Consignment Log (Loomis Log). Our review of the Loomis Log for the period October 2, 2012 to November 21, 2013 indicated that weekly deposit amounts ranged from \$8,991 (19 checks) to \$332,033 (62 checks). We understand that the number of physical checks mailed to Pharmacy Administration is expected to

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decline with the implementation of the new lockbox procedures. However, any checks that continue to be mailed by payers and processed for deposit should comply with deposit timeliness requirements.

The SDCC Pharmacy also made deposits weekly. Review of several deposit logs for this location in FY 2013-14 identified some weeks when deposits exceeded \$500.

**Management Corrective Actions:**

OP Pharmacy management is implementing procedures to ensure that:

1. Deposits at all locations are made as frequently as possible to comply with policy requirements.
2. The correct bank lockbox remittance address has been included on the electronic payer claim files to increase electronic deposits and reduce the number of check payments remitted to the Pharmacy Administrative Office.

**D. Bank Account Management and Revenue Allocation Procedures**

**Current revenue allocation and bank reconciliation processes were complex and included process steps that did not appear to add value.**

Analysis of the current deposit and revenue allocation process identified inefficiencies in the form of multiple revenue transfers and deposit advices to move revenue between the Medical Center and Medical Group bank accounts. An OP Pharmacy Billing Office Analyst reviewed the EOB form for each check received in the both bank accounts to determine which Pharmacy location should receive the revenue. Checks for Medical Center Pharmacies sent to the Medical Group bank lockbox were transferred to the Pharmacies via a Fund Transfer Request Form completed by the Analyst. The SOM Controller's Office also had to complete a journal voucher to record the income transfer in the financial system. When checks meant for Medical Group Pharmacies were received in the Medical Center bank account, a special Deposit Advice was prepared by the Analyst each week to transfer the revenue, and a journal voucher was processed to record the revenue in the appropriate Medical Group account. A flowchart depicting the current process is presented in ***Attachment A***.

This process could be streamlined if only one bank account were used for all OP Pharmacy locations. The EOB review process would continue to be completed to identify and transfer SDCC Pharmacy payments to the Medical Group, which would require only one journal entry. Credit card receipts for the machine at

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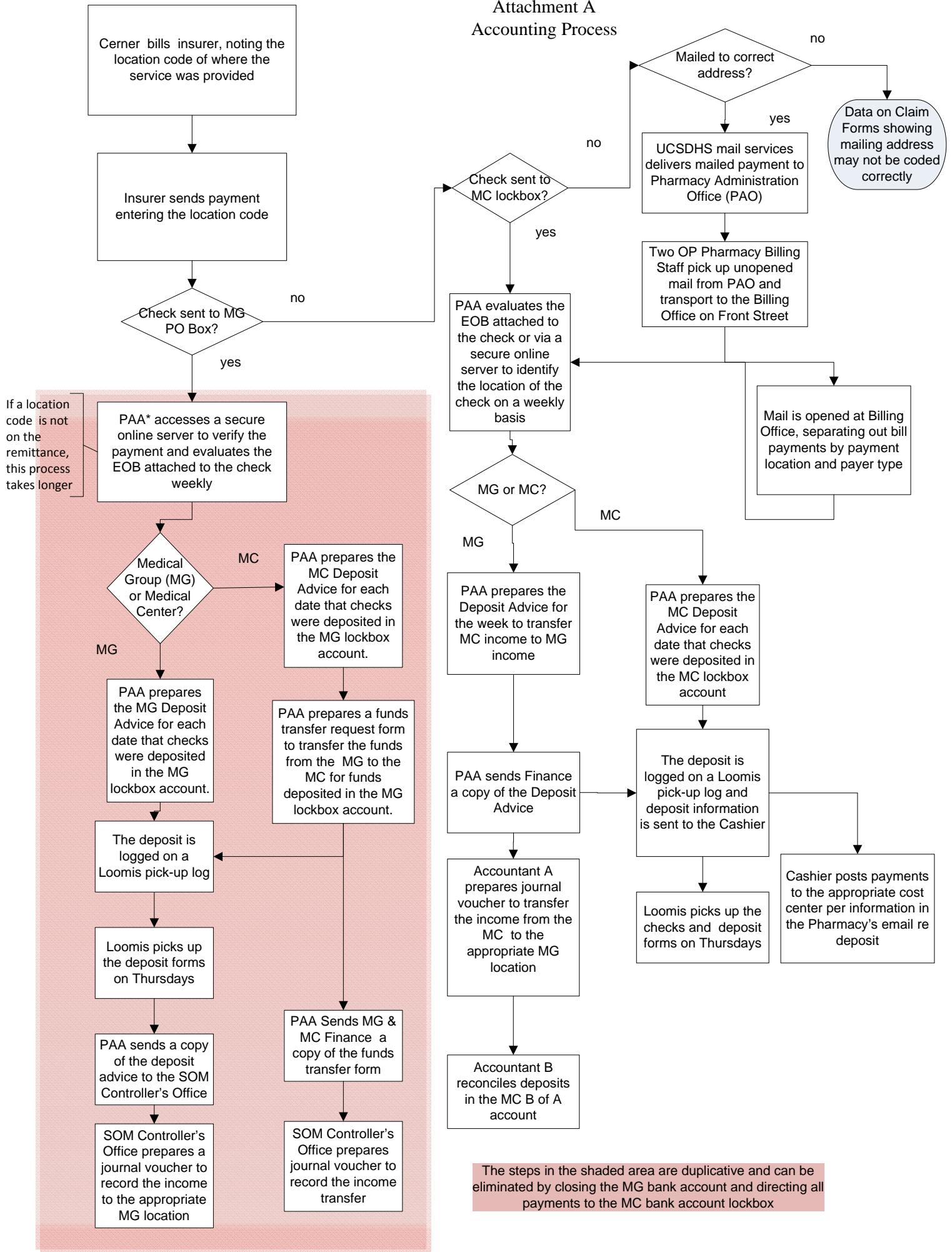
SDCC could also be linked to its Medical Group fund/index, which would continue to be managed by the SOM Controller's Office.

**Management Corrective Action:**

OP Pharmacy management will coordinate with the SOM Controller to close the Pharmacy Medical Group bank account after notifying payers, and re-directing SDCC deposits to the Pharmacy Medical Center bank account.

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Attachment A  
 Accounting Process



\* PAA = Pharmacy Administrative Analyst