

## The Added Value of Internal Audit as a Third Line: A Case Study on Indonesia's Social Health Insurance Provider

**Tandid Nasal**

Faculty of Economics and Business, Universitas Indonesia  
[tandidnasal@gmail.com](mailto:tandidnasal@gmail.com)

### Abstract

*The assignment of the Health Social Security Program mandated to Indonesia's Social Health Insurance Provider (ISHP) is very crucial and faces many challenges. Various issues faced by ISHP often disrupt the stability of the Health Social Security program. The strategy's success and proper risk management will determine the program's sustainability. Therefore, the role of internal audit as a third line to ensure the effectiveness of strategic risk management is very important. This study uses a qualitative case study approach with three lines model of the IIA framework. This study evaluates the added value that internal audits can provide as a third line for supporting the success of social health insurance programs.*

### Keywords

added value; internal audit;  
three lines model



### I. Introduction

Law Number 11 of 2011 concerning Social Security Administering Bodies stated that Indonesia's Social Health Insurance Provider (ISHP) is the only institution in Indonesia that provides social health insurance for all Indonesians. ISHP also holds the title of the world's largest social health insurance institution (Sugianto, 2019). ISHP membership in 2022 has reached 242.6 million people (DJSN, 2022).

The assignment of ISHP is very crucial. Therefore ISHP is often faced with various issues, such as data leakage (Putri, 2021) and financial difficulties (Meilanova, 2022). The sustainability of the ISHP program is highly dependent on how the management can manage strategic risk. Internal audit as the third line acts as a supervisor while ensuring that risk management and compliance have been carried out properly and correctly. Audits based on strategic risk can provide the greatest added value (IIA Netherlands and KPMG, 2015).

Lucan et al. (2015) state that an internal auditor represents a real change agent. The effectiveness of the internal auditor's activities is an important factor. Therefore, planning an effective audit activity will be able to encourage the internal audit function as a catalyst for change through various projects that can protect and create value for an organization (Wang et al., 2021).

According to Sawyer et al. (2019), with increasing challenges and changing dynamics in the business and organizational environment, an internal audit requires a solid foundation on the organization's strategy, objectives and risk profile. It is hoped that audit activities can lead to risk-based activities and are oriented towards enhancement and value protection (IIA, 2020).

Risk-based audit activities must be aligned with the risk management processes that the second line of the organization has implemented. According to the IIA (2020), as the third line, internal audit is obliged to carry out an objective assurance and advice function and ensure the effectiveness of the organization's risk management has been carried out properly. Aspects of collaboration and cooperation with the second line are needed so that there are no overlapping activities and all stakeholders can feel added value.

## II. Review of Literature

### 2.1 Application of the Three-Line Model

Applying the three-line model will be effective if its implementation is in line with the conditions and goals of the organization. According to a Gartner Corporate Executive Board survey in Deloitte (2020), 66 percent of company leaders say that business models will continue to change dramatically over the next three years. They seek opportunities to innovate in change and improve the risk landscape. In responding to a complex and fast-moving risk landscape, a first-line role is needed to identify and respond to emerging risk events quickly and effectively. Meanwhile, the second line provides frameworks, policies, tools, and techniques to support risk and compliance management.

While the second line role is not completely independent of management, this is not the case for the third line. According to the IIA (2020), the internal audit function cannot make decisions or activities that are part of management. Assurance and advice activities on matters that can threaten the independence of internal audit can be transferred by using the services of a third party that has adequate qualifications.

According to IIA (2020), the TLM has 6 (six) principles that emphasize communication, cooperation, and collaboration between lines. The six principles include:

1. **Governance Principles.**  
Good governance is created when the structure and business processes enable the Governing Body to have stakeholders accountable, risk-based management actions, assurance considerations and internal audit advice.
2. **Principles of Governing Body.**  
Governing body can ensure that structures and processes are aligned with stakeholder expectations.
3. **First and second-line management roles.**  
First-line management is to carry out activities for their respective functions. Meanwhile, the second line ensures that risk and compliance management and the organization's business processes run properly.
4. **Third Line Role.**  
Internal audit at the third line ensures the adequacy and effectiveness of governance and risk management.
5. **Third Line Independence.**  
Internal audit performs objective assurance and advisory functions free from interference from other parties.
6. **Creating and Protecting Value.**  
All roles collaborate in creating and protecting value for IHSP stakeholders.

### 2.2 Relationships of the Leading Roles in the Three-line Model

To realize the role of an effective three-line model, collaboration and cooperation between several parts is important, including:

1. Management Relations (First Line and Second Line) with Governing Body  
According to the IIA (2020), the governing body usually determines the direction of an organization by defining its values, vision, mission and risk appetite and delegating responsibilities or necessary resources. Eulerich (2021) mentions that the new three-line model allows for a more flexible structure. The main director of an organization can act as a member of the governing body or even as its chairman. The organization allows second-line leaders such as risk management and compliance directors to have direct reporting lines to the Governing Body.
2. Management Relations (First and Second Line Roles) with Internal Audit  
Internal audit is independent of management in ensuring that its activities are free from bias and have access to unlimited resources and information (IIA, 2020). Management and internal audit need to interact regularly to ensure their activities are aligned with the organization's strategy. Coordination and cooperation are also intended to help realize synergies and avoid duplication of functions (Eulerich, 2021).
3. Relationship between Governing Body and Internal Audit.  
Internal audit is usually known as the extension of the ear and eye of the governing body (IIA, 2020). The internal audit examines and evaluates all areas of the organization on behalf of the governing body, which the management board cannot audit and supervisory board (Eulerich, 2021).
4. All Role Relationships.  
According to the IIA (2020), each role in the three-line model has different responsibilities but must be aligned with organizational goals. Therefore, regular and effective collaboration, coordination, and communication are needed.

### **2.3 Added Value of Internal Audit as a Third Line**

IIA Netherlands and KPMG (2015) revealed that the role of internal audit is crucial in the success of the organizational strategy. This can be translated as a significant added value given to stakeholders as a third line. As the third line, internal audit is obliged to ensure the effectiveness of strategic risk management for the second line and ensure that the management follows the first line (IIA, 2020). For this coherence to be successful, conduct regular and effective collaboration between lines. Collaboration will also prevent duplication of functions and responsibilities between the three lines.

When deciding on a commitment to provide continuous and higher value-added, the internal audit function must first gain credibility and trust within the organization. According to Eulerich and Lenz (2020), this can be achieved by offering relevant basic internal audit services and providing high-quality assurance with a focus on GRC.

## **III. Research Method**

The type of research carried out is by using the case study evaluation method. The data/information collected is sourced from primary and secondary data preliminary data obtained through the distribution of questionnaires and interviews. Meanwhile, secondary data was obtained through document observation. This study uses data analysis methods derived from the concept of Miles & Huberman (1994). The data obtained will be analyzed continuously and interactively at each stage until it is complete until reaches data saturation.

## IV. Discussion

### 4.1 Position of Internal Audit in ISHP's GRC Architecture

The establishment of the IHSP GRC architecture was initially initiated by the strategic planning function of the organization. The organization's strategic planning is derived from the Work Plan & Budget and is used as the basis for planning and performance evaluation. According to Ivancevich, Konopaske and Matteson (Busro in Edward, 2020) that performance shows the ability and skills of workers. Performance is a person's success in carrying out tasks, work results that can be achieved by a person or group of people in an organization in accordance with their respective authorities and responsibilities (Wulandari, 2021). According to Yani in Syardiansyah (2020) performance is a result of work achieved by a person in carrying out the tasks assigned to him based on skill, experience and sincerity as well as time. This means that in work contains elements of the standard that achievement must be met, so, for those who reach the standards set means good performance (Wahjudewanti, 2021). System management translates organizational planning into business processes that become the reference for all functions in the first line. The first line is compiling a risk profile in accordance with existing regulations and guidelines. This risk profile becomes a reference in implementing the IHSP GRC.

The risk management function compiles the organization's risk profile, while the Internal Compliance Function (second line) compiles the organization's compliance risk profile, including the code of ethics as a report on the effectiveness of controlling and handling organizational risks. This report is a reference for the GRC report, which covers the effectiveness of controlling and handling risks and conflicts of interest that have the potential to harm the organization and become an indicator of the achievement of organizational goals.

The Internal Audit Function then conducts inspections and ensures to the Board of Directors the control functions that may affect the achievement of organizational goals through follow-up recommendations in the GRC report. Implementing the IHSP GRC also integrates the control functions established previously, such as the Ethics Committee, Investment Committee, Information Technology Steering Committee and Fraud Prevention Team.

### 4.2 Internal Audit Relationship with First and Second Line

The integration of Risk Management in the organization's business processes is the key to managing the organization's internal control system, outlined in the form of GRC integration. The integration of risk management between the first, second and third lines in the three-line model at IHSP is vertical integration. Risk control activities in the First Line (work unit) will be the basis for monitoring by the Second Line (Risk Management Unit). Meanwhile, the results of risk monitoring by the Second Line serve as the basis for supervision by the Third Line (Internal Audit).

The relationship between internal audit and the first line is in the form of assurance activities carried out regularly every year to several field functions located at the Head Office, Regional Offices and Branch Offices. However, due to limited resources, several functions are still responsible for managing the organization's strategic risks that the 2021 assignment has not covered.

The lines of communication and coordination between the second and third lines in the IHSP are clearly defined in the GRC architecture. However, in practice the relationship between the two roles is not effective. IHSP still uses the old concept of 3 (three) lines of defense in all guidelines related to GRC. This can be one of the causes of the two lines running independently and not integrated. As said by IIA (2020) the concept of 3 (three) lines of defense has long been abandoned and replaced by the concept of a three-line model. The

three-line model emphasizes the 6 (six) principles of alignment, communication, coordination, cooperation, and collaboration in each section.

Based on the results of the 2021 GRC assessment and interviews with Internal Audit, it is stated that Internal Audit has not carried out an audit using the compliance list to evaluate the realization of the implementation of the substance of compliance. This, of course makes the compliance sub-function in the MSR unit overlap with the internal audit function carried out by Internal Audit. Both tend to implement internal control separately and can lead to a waste of resources.

In addition, IHSP's strategic risks have not been optimally accommodated in the 2021 Work Program. This is evidenced by: there is no change in the work program in 2021, even though the strategic risks in the second semester have changed

#### 4.3 Added Value of Internal Audit that can be provided

Internal audit needs to interact regularly and align its activities in an integrated manner with the risk management function. According to Eulerich (2021), good coordination and cooperation are also intended to help realize synergies and avoid duplication of functions. If the organization's strategic risks have been fully covered in the assignment activities in 2021, the added value created will be greater.

**Table 1.** Regular Audit Coverage

No	Strategic Risk	PIC	Scope of audit 2021
1	Recruitment and retention of participants for the achievement of participant coverage are not on target	Unit 1	Yes
2	The service received does not meet the expectations of the participants	Unit 2	Yes
3	Health facilities that apply for cooperation are not up to standard.	Unit 3, Unit 4	Yes
4	Failure to protect the confidentiality and integrity of data and information	Unit 5	Yes
5	The synergy of organizational information system development with other stakeholder information systems has not been optimal	Unit 6	Yes
6	Low acceptance of contributions and contribution assistance from local governments	Unit 7	Yes
7	The occurrence of regulatory disharmony in the implementation of the program	Unit 8	Not
8	Not achieving the investment fund management results according to the target	Unit 9	Yes
9	Strategic cooperation has no impact on performance achievement	Unit 8	Not
10	Participants cannot access the system/application	Unit 5	Yes
11	A decline in the organization's reputation in implementing the program	Units 10	Not
12	Payment of E	Unit 3, Unit 4	Yes
13	The strategic health spending policies developed have no impact on the efficiency and effectiveness of program implementation	Unit 11	Not
14	Cheating that occurs in the program	Unit 3, Unit 4	Yes
15	Disruption of the Covid-19 claim verification process	Unit 3, Unit 4	Yes

Table 1 shows that there are still strategic risks/main risks that have not been fully covered by internal audit activities, especially in units 8, 10 and 11. Reporting on the interview results, the strategic risk that has not been accommodated is due to limited resources available. There is no official document stating that the strategic risks of semester II have been accommodated in the 2021 activity changes. This shows that the functions of the three lines in IHSP are still seen separately.

The internal audit charter can be used as a foundation for realizing the added value of internal audit. The added value of internal audit, as a third line, should no longer be described as a grey area. Unfortunately, IHSP's internal audit charter has not been updated since 2014. Even though the dynamics of the business environment, the existing Governing Body and various stakeholders have not changed since 2014 until now.

## V. Conclusion

Based on the analysis above, the role of an internal audit carried out by internal audit has not been maximized as the third line in the IHSP. The audit program conducted by the internal audit is not fully integrated with the organization's strategic risks. The perception of internal audit's strategic risk priorities differs from the Risk Management Function (RMF). According to RMF, several risks that threaten the organization's objectives are considered not very relevant as the basis for determining the Internal Audit audit program.

The relationship between the second and third lines is also not going well. This can be seen from the results of the GRC assessment, which states that the internal audit report does not contain conclusions regarding the effectiveness of risk management. This fact shows that there is a potential for overlapping working relationships, duplication of functions and the breakdown of synergies between the second and third lines.

Therefore, ISHP should update the internal audit charter less relevant to the organization's strategy and implement the six principles of collaboration with the three lines model. In addition, assignment activities can also be focused on activities that can provide the greatest added value to the organization.

Future research is expected to explore further the scope of audits that can provide added value and involve other respondents from various stakeholders such as organizational audit committees.

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