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**Legal Services Corporation**

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March 26, 2015

Mr. Gregory Knoll  
Executive Director  
Legal Aid Society of San Diego  
110 S. Euclid Avenue  
San Diego, CA 92114

Dear Mr. Knoll:

Enclosed is the Office of Inspector General's (OIG) final report for our audit of Selected Internal Controls at Legal Aid Society of San Diego. The OIG has reviewed your comments on the findings and recommendations in the draft report. Your comments are included in the final report as Appendix II.

Grantee Management accepted the recommendation outlined and stated the suggested policies and procedures have been fully documented. The corrective actions outlined in the letter and the supporting documentation provided are responsive to the OIG's recommendation. Therefore, the OIG considers the recommendation closed.

We thank you and your staff for your cooperation and assistance.

Sincerely,

Jeffrey E. Schanz  
Inspector General

Enclosure

cc: Legal Services Corporation  
Jim Sandman, President

Lynn Jennings, Vice President  
For Grants Management

**LEGAL SERVICES CORPORATION**

**OFFICE OF INSPECTOR GENERAL**

**FINAL REPORT ON SELECTED INTERNAL  
CONTROLS**

**LEGAL AID SOCIETY OF SAN DIEGO, INC.**

**RNO 805250**

Report No. AU 15-05

March 2015

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## **INTRODUCTION**

The Legal Services Corporation (LSC) Office of Inspector General (OIG) assessed the adequacy of selected internal controls in place at Legal Aid Society of San Diego, (LASSD or grantee) related to specific grantee operations and oversight. Audit work was conducted at the grantee's administrative office in San Diego, California and at LSC headquarters in Washington, DC.

In accordance with the Legal Services Corporation Accounting Guide for LSC Recipients (2010 Edition) (Accounting Guide), Chapter 3, an LSC grantee "...is required to establish and maintain adequate accounting records and internal control procedures." The Accounting Guide defines internal control as follows:

[T]he process put in place, managed and maintained by the recipient's board of directors and management, which is designed to provide reasonable assurance of achieving the following objectives:

1. safeguarding of assets against unauthorized use or disposition;
2. reliability of financial information and reporting; and
3. compliance with regulations and laws that have a direct and material effect on the program.

Chapter 3 of the Accounting Guide further provides that each grantee "must rely upon its own system of internal accounting controls and procedures to address these concerns" such as preventing defalcations and meeting the complete financial information needs of its management.

## **BACKGROUND**

LASSD operates law programs subject to individual grant and service contract restrictions in the following areas according to their audited financial statements for the fiscal year ended June 30, 2013:

### **Substantive**

- Housing
- Health/income maintenance
- Individual rights
- Family
- Consumer/finance
- Education and juvenile

## **General Priorities**

- Support for families
- Preserving the home
- Maintaining economic stability
- Safety, stability and health
- Populations with special vulnerabilities

LASSD received \$2,750,867 from LSC and \$5,702,460 from other non LSC funders. The grantee serves residents of San Diego County and has two branch offices. According to LASSD's 2012 grantee profile, there are approximately 91 staff consisting of 38 attorneys, 35 paralegals and 18 support staff.

## **OBJECTIVE**

The overall objective was to assess the adequacy of selected internal controls in place at the grantee as the controls related to specific grantee operations and oversight, including program expenditures and fiscal accountability. Specifically, the audit evaluated selected financial and administrative areas and tested the related controls to ensure that costs were adequately supported and allowed under the LSC Act and LSC regulations.

## **AUDIT FINDING**

Internal controls reviewed and tested at LASSD were adequate as the controls related to specific grantee operations and oversight. Controls over program expenditures and fiscal accountability were generally adequate. Our evaluation and testing of controls in the areas of disbursements, credit cards, contracting, property and equipment, internal management reporting and budgeting, and salary advances revealed that the practices in these areas were adequate and in accordance with the *Fundamental Criteria of an Accounting and Financial Reporting System (Fundamental Criteria)* contained in the LSC Accounting Guide.

While many of the controls were adequately designed and properly implemented as they related to specific grantee operations and oversight, some controls need to be strengthened and formalized in writing. The OIG identified the areas listed below that need to be improved.

## **WRITTEN POLICIES AND PROCEDURES**

The grantee's written policies in the areas of contracting, internal budgeting and reporting, attorney fees, derivative income, cost allocation and credit cards need strengthening in order to properly describe the controls and procedures followed by the grantee. Section 3-4 of the Accounting Guide states that each grantee must develop a written accounting manual that describes the specific procedures to be followed in order to comply with the *Fundamental Criteria*. The grantee had adequate practices in place

for all of the areas detailed above, but was unaware the written policies in their accounting manual were deficient.

Fully documenting policies and procedures helps ensure that proper controls are followed, serves as a vehicle to communicate controls to all staff, and helps ensure that staff members understand their roles and responsibilities. Without detailed written procedures, there could be a lack of transparency and consistency in the application of the methodology, especially in cases of staff turnover.

## **Contracting**

LASSD's written contracting policies do not include all the elements for securing contracts and consulting services as required by LSC's *Fundamental Criteria*. The written policy currently does not include:

- the type and dollar value of contracts that require competition;
- the number of bids required for "competitive bids";
- the required approval levels for each contract type and dollar threshold; and
- contract action fully documented and the documentation maintained in a central file.

Section 3-5.16, Contracting, in the *Fundamental Criteria* outlines policies for types of contracts, documentation, competition and approvals. It includes the following:

- a. Types of Contracts: Not all contracts are the same. Management should establish contracting procedures, dollar thresholds, and competition requirements for each type of contract. Contracts that should receive additional oversight include consulting, personal service, and sole-source.
- b. Documentation: The process used for each contract action should be fully documented and the documentation maintained in a central file. Any deviations from the approved contracting process should be fully documented, approved, and maintained in the contract file. In addition, the statement of work should be sufficiently detailed so that contract deliverables can be identified and monitored to ensure the deliverables are completed.
- c. Competition: The type and dollar value of contracts that require competition should be included in the policies of the grantee. Documents to support competition should be retained and kept with the contract files.
- d. Approvals: The required approval level (including items that need to be approved by LSC) should be established for each contract type and dollar threshold, including when the board of directors should be notified and/or provide approval.

## **Internal Management Reporting and Budgeting**

The grantee's written policies on Internal Management Reporting and Budgeting need to be expanded to reflect the actual practice in place. The following items are missing from the written policies:

### Internal Management Reporting

- Descriptions of the types of reports that are prepared (budget vs actual, by funding source, by cost center).
- Types of analysis performed on the reports by the Chief Fiscal Officer.

### Budgeting

General steps on how the budget is formulated, such as:

- Types of schedules prepared to support the budget (assumptions, worksheets, etc.)
- Time of year when the budget process is conducted.
- Budget monitoring procedures and approvals for mid-year budget adjustments.

## **Attorneys' Fees and Derivative Income**

### Attorneys' Fees

The grantee's written policies on attorneys' fees are missing certain elements that describe the actual process in place. The OIG tested attorneys' fees and found that the grantee is properly allocating those fees in accordance with 45 CFR §1609.4(a). However, the written policy is deficient and does not include the allocation methodology used and the procedures followed by the staff in allocating those fees. The grantee has written policies and procedures in its accounting manual for recording and allocating attorneys' fees that do not appear to accurately capture the requirements contained in LSC's Accounting Guide and 45 CFR §1609.4(a). The allocation is supposed to be based on attorney salaries charged by the various funding sources as shown in their timekeeping system (KEMPS) but is not detailed in the written policy.

Grantees shall adopt written policies and procedures to guide its staff in complying with 45 CFR §1609.6.

### Derivative Income

The written derivative income policy does not provide a description of the methodology the grantee uses to allocate interest, rent, reimbursements or proceeds from the sales of assets to the related funding sources. The OIG tested controls in these areas and found that, in practice, they appeared adequate and reasonable.

## **Cost allocation**

The grantee has a written cost allocation policy in its Accounting Manual that appears to be reasonable, consistently applied and equitable in practice. However, the written policy does not fully and adequately detail the specific procedures currently in practice. We performed testing of the grantee's method of allocating both direct and indirect costs to determine whether it was reasonable and in accordance with LSC requirements as well as the grantee's own written policies. Based on our review and testing of the process, the grantee's actual cost allocation procedures were reasonable and in accordance with LSC requirements and its own written policies. However, some of the current practices in place routinely performed by staff were not sufficiently detailed in the Accounting Manual.

The *Fundamental Criteria* states that the allocation formula should be adequately documented in writing with sufficient detail for the auditor, LSC, OIG, GAO and others, to easily understand, follow and test the formula. Approved documented policies and procedures represent management's intentions on how processes are to be handled and also serve as a method to document the design of controls, communicate the controls to staff and help the grantee ensure that proper controls are followed.

## **Credit Cards**

LASSD's written policies for credit cards are generally comparable to LSC's *Fundamental Criteria*, except they do not detail the authorization process for activation and deactivation of credit cards. The controls in this area were tested and deemed adequate. The Executive Director authorized the activation of the grantee's sole credit card. According to grantee management, they were not aware that the authorization process for activation and deactivation of credit cards should be documented in their accounting manual.

**Recommendation:** The Executive Director should:

ensure that written policies and procedures for contracting, internal management reporting and budgeting, attorneys' fees, derivative income, cost allocation and credit cards adequately describe the processes and controls currently in place at the grantee in accordance with LSC's Accounting Guide and *Fundamental Criteria*.

## **SUMMARY OF GRANTEE MANAGEMENT COMMENTS**

Grantee management agreed with the recommendation contained in the report.

Grantee management stated the Accounting Procedures Manual had been amended to include all areas discussed in OIG Draft Report. Supporting documentation was provided for amendments made in the following areas:

- Contracting
- Internal Management Reporting and Budgeting
- Attorneys' Fees and Derivative Income
- Cost Allocation
- Credit Cards

Management's formal comments can be found in Appendix II.

### **OIG EVALUATION OF GRANTEE MANAGEMENT COMMENTS**

The corrective actions outlined in the letter and supporting documentation provided is responsive to the OIG's recommendation. Therefore, the OIG considers the recommendation closed.

## APPENDIX I

### SCOPE AND METHODOLOGY

To accomplish the audit objective, the OIG identified, reviewed, evaluated and tested internal controls related to the following areas.

- Cash disbursements
- Credit card usage
- Cost allocation
- Contracting
- Property and equipment
- Derivative income
- Employee benefits
- Internal management reporting and budgeting

To obtain an understanding of the internal controls over these areas, we reviewed grantee policies and procedures including manuals, guidelines, memoranda, and directives setting forth current grantee practices. We interviewed grantee officials to obtain an understanding of the internal control framework and to assess the level of awareness and knowledge of management and staff of the processes in place. To review and evaluate internal controls, we compared the grantee's internal control system and processes to the guidelines in the *Fundamental Criteria of an Accounting and Financial Reporting System (Fundamental Criteria)* contained in the LSC Accounting Guide. This review was limited in scope and not sufficient for expressing an opinion on the entire system of grantee internal controls over financial operations.

We assessed the reliability of computer-generated data the grantee provided by reviewing source documentation for the entries selected for review. We determined the data were sufficiently reliable for the purposes of this report.

To test the appropriateness of expenditures and test for the existence of adequate supporting documentation, we reviewed disbursements from a judgmentally selected sample of employee and vendor files. We selected 115 transactions from the period January 1, 2013 to June 30, 2014. The 115 transactions totaled \$486,198.84, and represented approximately 4.6 percent of the \$10,490,344.26 disbursed for expenses other than payroll during the period January 1, 2013 through June 30, 2014.

To assess the appropriateness of expenditures, we reviewed invoices and vendor lists, and traced the expenditures to the general ledger. We evaluated the appropriateness of the expenditures on the basis of grant agreements, applicable laws and regulations, and LSC policy guidance.

To evaluate and test internal controls over the contracting process, credit card use, internal management reporting and budgeting, and property and equipment, we interviewed appropriate program personnel, examined related policies and procedures,

and selected specific transactions to review for adequacy. We reviewed controls over salary advances by testing a judgmentally selected sample of salary advances given to employees. To assess the salary advance process, we reviewed salary advance requests for appropriate approvals and compliance with the grantee's internal standards.

To evaluate the adequacy of the cost allocation process, we discussed the process for the period under review with grantee management and reviewed written cost allocation policies and procedures as required by the LSC Accounting Guide. Allocated amounts for sampled months during the period of review were recalculated using the information provided by the grantee.

We reviewed controls over derivative income by interviewing management, identifying current grantee practices, reviewing the written policies contained in the grantee's Accounting Manual, and examining entries to the accounting system which documented receipt and allocation of derivative income.

The OIG conducted on-site fieldwork from August 4, 2014 through August 8, 2014. Our work was conducted at the grantee's central administrative office in San Diego, CA and at LSC headquarters in Washington, DC. Documents pertained primarily to the period January 1, 2013 through June 30, 2014.

This audit was conducted in accordance with generally accepted government auditing standards. Those standards require that the audit be planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. The OIG believes the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objectives.

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**APPENDIX II**

**STANLEY J. PANIKOWSKI, ESQ.**  
**President, Board of Directors**  
**BRIAN M. KRAMER, ESQ.**  
**President-elect, Board of Directors**  
**GREGORY E. KNOLL, ESQ.**  
**Executive Director/Chief Counsel**

March 18, 2015

Sent via Email  
[aramirez@oil.lsc.gov](mailto:aramirez@oil.lsc.gov)

Mr. Anthony M. Ramirez  
Audit Team Leader  
**Office of the Inspector General**  
**Legal Services Corporation**  
3333 K Street NW, 3<sup>rd</sup> Floor  
Washington, D.C. 20007

**Re: Response to your letter dated February 26, 2015 regarding the Draft Report on results of our Audit on Selected Internal Controls – Recipient No. 805250**

Dear Mr. Ramirez:

The Legal Aid Society of San Diego, Inc. ("LASSD") received the Office of Inspector General ("OIG") Draft Report, Recipient No. 805250, as mentioned above. LASSD has received all of the audit findings, and has established written policies and procedures as noted therein, to document and verify the adequate practices which were found to be in place (although not fully documented). The Amendments to the LASSD Accounting Procedures Manual have been written and adopted for that manual as discussed in the OIG Draft Report.

The additional documentation discussed by OIG consisted of additions to the manual in the following areas:

- Contracting (Accounting Procedures Manual redrafted at page 31)
- Internal Management Reporting and Budgeting (Accounting Procedures Manual redrafted at page 52)
- Attorneys' Fees and Derivative Income (Accounting Procedures Manual redrafted at pages 19-20)
- Cost Allocation (Accounting Procedures Manual redrafted at page 43)
- Credit Cards (Accounting Procedures Manual redrafted at page 14)

Appended to this document are two copies of the LASSD Accounting Procedures Manual, as revised per OIG findings and comments.

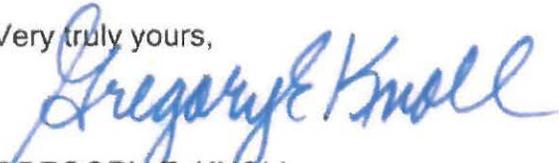
Version one shows the Accounting Procedures Manual with the changes made in "tracking" form, so that OIG may review the new language easily.

The Accounting Procedures Manual version two is the completed manual with all changes accepted and completed in final form.

LASSD believes that the OIG recommendations for our Accounting Procedures Manual have strengthened the manual, made it more effective for guiding both staff and auditors in performing and reviewing our financial work, and have upleveled our Accounting Department documentation.

Please do not hesitate to contact me directly at (619) 471-2620 or at [GEK@lassd.org](mailto:GEK@lassd.org) should you have any questions or require any further information.

Very truly yours,



GREGORY E. KNOLL  
Executive Director/Chief Counsel