

 **LEGAL SERVICES CORPORATION**

## **Office of Inspector General**

# **RESULTS OF RECIPIENT AUDIT REPORTS FOR THE YEAR ENDED DECEMBER 31, 1997**

**Final Report No. AU98-003**

June 1998

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June 18, 1998

### **TO THE BOARD OF DIRECTORS OF THE LEGAL SERVICES CORPORATION**

As you know, the Corporation's fiscal year 1996 appropriations statute (PL 104-134) directed that annual financial statement audits be used as the primary means for checking grantee compliance with applicable laws and regulations. The fiscal year 1997 appropriations act (PL 104-208) also included this provision. This report presents the results of audits of grantees with fiscal years ending December 31, 1997, or 77% of the LSC grant recipients.

Independent Public Accountants (IPAs) reported 50 critical findings related to 34 grantees in the 205 audit reports received. After reviewing these findings the OIG concluded that 21 were significant and referred them to LSC management for follow up. In addition, an OIG review of a sample of reports with non-critical findings disclosed three findings for one grantee that were significant even though the IPA did not report them as critical findings. In total, 24 findings related to 35 grantees were reported to LSC management. None of the referred findings were for grantee noncompliance with prohibitions and restrictions on the provision of legal services.

Most of the findings were for internal control weaknesses such as a failure to perform client trust account reconciliations. Other findings involved missing or unsigned documents and time keeping deficiencies. This year's findings represent a significant decrease both

in numbers and significance from those reported by the IPAs last year.

This report will be presented to the Corporation's authorization and appropriations committees of Congress and will be made available to the public not later than June 23, 1998.

Edouard R. Quatrevaux  
Inspector General

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## RESULTS

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The audit reports submitted for grantees with fiscal years that ended December 31, 1997 contained 24 findings which were deemed to be significant and which the OIG referred to LSC management for corrective action. Although the categories are not mutually exclusive and some findings could be listed in more than one category, the following summary shows each finding in only one category for ease of reference.

### Summary of Significant Findings

#### Grantee Audit Reports With Fiscal Years Ending December 31, 1997

Category	Number of Findings
Internal Control Problems Procedure lacking or not followed Reconciliation of client trust accounts Processing financial data Weaknesses over cash receipts/disbursements	8
Missing documents and/or unsigned documents (i.e., client statement of facts, citizenship attestation, retainer agreements)	6
Timekeeping procedures and/or systems problems	2
Case management reporting	2
LSC fund balance was greater than 10% of LSC support requiring a waiver from LSC	1
FDIC insurance limits were exceeded and corrective	1

action was not taken before or during the audit	
Other procedural/regulatory problems	4
<b>Total</b>	<b>24</b>

### **Noncompliance with Restrictions**

The IPAs did not report any cases where grantees failed to comply with the legislatively imposed prohibitions and/or restrictions.

### **Internal Controls**

The largest number of significant findings were related to breakdowns in the internal control system. These findings primarily covered controls over financial transactions and data. In other cases, adequate internal control procedures were lacking or not followed.

### **Missing Documentation**

The second largest number of significant findings (6) concerned missing documents, such as client statements of facts, citizenship attestations, and retainer agreements. All cases of missing documents were deemed significant because absence of documentation can obscure instances of noncompliance or other reportable conditions.

### **Timekeeping Deficiencies**

Two findings concerned timekeeping systems. Both findings were deemed significant because accurate and reliable timekeeping is essential to ensure that there are no violations of prohibitions or restrictions.

### **Other Procedural or Regulatory Problems**

Four findings covered procedural or regulatory problems as in the following list.

- An LSC required report on planned priorities on use of resources was not prepared.
- Program/grant expenses were not allocated according to accounting principles and standards.
- Needs appraisal was not updated as scheduled by the Board of Directors.
- A required report on legislative and rulemaking activities was not prepared.

## **Repeat Findings**

Eleven of the above described findings were repeat findings from the fiscal year 1996 audit reports. In these cases, the grantee failed to correct, or only partially corrected the problem reported the previous year. The grantees did not provide reasonable explanations for their failure to correct previously reported problems.

## **Findings Deemed Insignificant**

The IPAs reported 26 additional critical findings for 22 grantees with fiscal years ending on December 31, 1997. In reviewing these reports, the OIG concluded that the findings did not warrant referral to LSC management. Generally, the reported problems had been corrected or were, in the judgment of the OIG staff, insignificant. These findings fall into one or more of the following categories.

- (1) Few insignificant errors in sample and problems not systemic.
- (2) Missing policy and policy adopted during or subsequent to audit.
- (3) Failure to take a physical inventory of law library or other assets, but corrective action taken
- (4) Minor omissions or discrepancies, i.e., document obtained and signed but undated.
- (5) Minor internal control problem.
- (6) Private Attorney Involvement shortfall and waiver requested/received from LSC.
- (12) Improper accounting procedures, but corrective action taken.

## **AUDIT REQUIREMENTS**

Recipients of grants from the Legal Services Corporation (LSC) are responsible for preparing annual financial statements and arranging for audits of those statements by Independent Public Accountants (IPAs). These audits are to be conducted in accordance with Government Auditing Standards promulgated by the Comptroller General of the United States, Office of Management and Budget (OMB) Circular A-133 "Audits of Institutions of Higher Education and Other Non-Profit Institutions," and the LSC "Audit Guide for Recipients and Auditors."

Recipients are required to arrange for audit reports to be submitted to the LSC Office of Inspector General (OIG) within 120 days of the

recipients' fiscal year ends. IPAs should follow the requirements of Government Auditing Standards, OMB Circular A-133, and American Institute of Certified Public Accountants (AICPA) professional standards for guidance on the form and content of reports. Such IPA reports include an opinion on the financial statements, a report on the internal control structure, a report on compliance with laws and regulations, and a management letter, when appropriate.

In addition, IPAs are required to submit a Summary Report Form on Noncompliance with Laws and Regulations, Questioned Costs and Reportable Conditions (SRF). IPAs must submit SRFs via the Internet by completing a form residing on the OIG website. The SRF must be submitted regardless of whether or not there are any audit findings to report. The IPA reports on the SRF any instances of noncompliance, material reportable conditions and additional findings. For reported findings, the IPA provides the findings description and Audit Guide code, the sample size and instances noted, the recipient response, and the amount of any questioned costs.

Under certain circumstances, the recipient is required to submit to the OIG a special report, commonly referred to as a 5-Day letter. When a determination has been made, based on sufficient competent evidential matter, that an instance of noncompliance has occurred, IPAs are to report immediately to the recipient. The report must contain a description of the instances of noncompliance and the circumstances. The recipient is required to submit to the OIG, with a copy to the IPA, a Recipient 5-Day "Special Report" to the OIG on Noncompliance with Laws and Regulations within five business days after issuance of the IPA's special report to the recipient. If the IPA does not receive a copy, the IPA must submit a copy of the report directly to the OIG within five business days of the recipient's failure to provide the required copy.

Recipients must submit corrective action plans to the OIG for all findings and recommendations that include material reportable conditions in internal control, material noncompliance with laws and regulations identified in the LSC Compliance Supplement, and questioned costs including those of sub-recipients. Recipients are required to develop corrective action plans describing the corrective action taken or planned in response to the audit findings and recommendations identified by the IPA. If the recipient disagrees with the finding or believes that corrective action is not required, it must provide an explanation and specific reasons. The recipient must submit the corrective action plan to the OIG within 30 days of

submission of the audit report. Alternatively, the recipient has the option of incorporating the corrective action plans into the audit reports as part of its response to the auditor's findings and recommendations, but this option does not extend the due date for audit reports.

## **SCOPE AND METHODOLOGY**

The scope of this report is grantee audit reports for the calendar year ended December 31, 1997.

### ***Processing Recipient Audit Reports***

The following is a summary of the process carried out by OIG and LSC management from receipt of the Summary Report Form (SRF) through implementation of corrective action.

The OIG developed an Audit Information Management System (AIMS) to support the audit review team in performing a desk review of the grant recipient audit reports by tracking and collecting the SRF, audit reports, 5-day letters, audit costs, and management letters. In addition, AIMS facilitates an OIG focused review, tracks the status, and documents the resolution and corrective action process of audit findings and recommendations.

Once the SRF is received, OIG staff validates the correctness of the SRF submission before it is accepted for entry into AIMS. The SRF can be accepted, edited or deleted. This approach allows the OIG to avoid redundant data entry by transferring the accepted SRF data into AIMS electronically. After the audit reports are received, OIG staff review each of them for completeness.

### ***Focused Review***

Next, the OIG conducts a focused review of audit findings and recommendations for SRF entries which have been accepted and have findings that the IPA considers critical. The OIG auditors can create new findings or amend existing ones based on the SRF, the 5-Day letter, the audit reports, and the management letter. An auditor reviews the findings and recommendations and determines his or her recommended action, which is either to "invoke A-50" or to "close to inventory." The LSC grantee audit follow up process incorporates the concepts of OMB Circular A-50 "Audit Follow up," and hence the use in AIMS of the term "invoke A-50." The auditor then writes a

justification for the recommended action. The recommended action is then approved or revised by OIG audit management.

If the decision is to invoke A-50, OIG audit management refers the audit findings and recommendations to LSC management for follow up action. The referral is made through AIMS by approving the finding for follow up and establishing a project code to track the follow up process through resolution and corrective action.

If the decision is to close to inventory, the findings and recommendations issued to grantees by their IPAs are retained in the AIMS system in an inventory of non-critical findings. These findings are provided to LSC management by the OIG for information only and no follow up action is required. However, under Government Auditing Standards, the IPAs are required to follow up on these findings in the next fiscal year audit. If the IPAs report that these findings are still uncorrected, A-50 will be invoked at that time.

The decision of whether to invoke A-50 or to close to inventory rests on whether or not the finding is significant. A significant finding is one deemed by the OIG to require management's attention based on quantitative and/or qualitative conditions contained in the finding and, thus, is referred to LSC management. The following types of findings and recommendations by grantee IPAs will be referred to LSC management for follow up: instances of noncompliance with laws and regulations which have a material impact on the LSC program, instances of questioned or unsupported costs, instances of material weaknesses, reportable conditions that taken in whole or in part are indicative of a systemic problem, and uncorrected findings from prior reports.

LSC management has the responsibility for follow up on significant findings referred by the OIG to ensure that instances of deficiencies and noncompliance are resolved in a timely manner. To facilitate the responsibilities of LSC management and the OIG, recipients are required to submit corrective action plans to the OIG, which forwards them to LSC management. Corrective action plans are due 30 days after submission of the audit report. If a recipient does not submit a corrective action plan by the due date, the OIG notifies LSC management which contacts the grantee and requires immediate submission of the plan.

### ***Resolution***

Resolution is the point at which LSC management agrees with the

grantee's proposed corrective action plan or accepts the grantee's disagreement with a reported finding and the OIG concurs in the management decision. If agreement cannot be reached, resolution is reached when the LSC Audit Follow Up Official, designated by the LSC President, issues a decision on the matter. LSC management reviews each referred finding and recommendation along with the corrective action plan proposed by the grantee to determine if it is satisfactory. If the proposed corrective action is deemed unsatisfactory, LSC management communicates with the grantee to ensure a satisfactory corrective action plan.

LSC management ensures that proposed corrective actions are consistent with law, regulations, and LSC policy. When accepting the grantee's disagreement with a reported finding or recommendation, LSC management ensures that the grantee provides an adequate written justification containing the legal and factual basis for the disagreement. LSC management notifies the OIG of the corrective action agreed upon by LSC management and the grantee, or of LSC management's acceptance of the grantee's disagreement within 30 days of receipt of the referred finding.

The OIG notifies LSC management within 15 days of its concurrence or nonconcurrence. If the OIG concurs, the finding is considered resolved. If the OIG does not concur, the Audit Follow Up Official has 15 days to seek agreement between LSC management and the OIG. If no agreement is reached within the 15 days, the Audit Follow Up Official issues a decision within 7 days, and the finding is considered resolved.

### ***Corrective Action***

After resolution has been obtained, LSC management ensures that corrective actions have been taken by the grantee within six months of the date on which resolution is reached. LSC requires the grantee to provide sufficient documentation to ensure that the corrective action has been fully implemented. In addition, the grantee is required to certify in writing that all corrective actions have been implemented. LSC management then notifies the OIG of all completed corrective actions and provides the OIG with copies of the grantee certifications. Upon receipt of the notification of completion, the OIG closes the respective findings and recommendations. IPAs will also verify completion of corrective actions during the next fiscal year audit.

### ***Quality Control Process***

The OIG reviews all audit reports submitted with IPA determined critical findings. In addition, a sample of reports lacking critical findings is reviewed as part of the primary review process. From a sample of 20 reports, one report with three findings was referred to LSC management. The grantee had failed to correct the findings from the prior year. As staff is available, additional reports with non-critical findings will be reviewed. On a test basis, the OIG reviews the IPAs' working papers to ensure conformity with applicable auditing standards and the LSC Audit Guide and Compliance Supplement requirements.