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September 30, 2013

Mr. Norman P. Metzger
Executive Director
Indiana Legal Services, Inc.
151 N. Delaware Street, Suite 1850
Indianapolis, IN 46204

Dear Mr. Metzger:

Enclosed is the Office of Inspector General's (OIG) final report of our audit on Selected Internal Controls at Indiana Legal Services, Inc. (ILS). The OIG has reviewed your comments on the draft report findings and recommendations and has determined that the actions ILS has planned are responsive to the recommendations. All 12 recommendations will remain open until notified in writing that the grantee's Accounting Manual has been updated and communicated to ILS staff. The OIG is referring $4,159 in questioned costs to LSC Management for their determination. These costs involved expenditures of LSC funds that were identified as unallowable or unsupported.

The full text of your comments is included in the report as Appendix II.

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

Sincerely,

Jeffrey E. Schanz
Inspector General

Enclosure

Cc: <u>Legal Services Corporation</u>
Jim Sandman, President

Lynn Jennings, Vice President
For Grants Management

LEGAL SERVICES CORPORATION

OFFICE OF INSPECTOR GENERAL

FINAL REPORT ON SELECTED INTERNAL CONTROLS

INDIANA LEGAL SERVICES, INC

RNO 515030

Report No. AU 13-08

September 2013

www.oig.lsc.gov

INTRODUCTION

The Legal Services Corporation (LSC) Office of Inspector General (OIG) assessed the adequacy of selected internal controls in place at Indiana Legal Services (ILS or grantee), Indianapolis, Indiana, related to specific grantee operations and oversight. Audit work was conducted at the grantee's main office in Indianapolis, Indiana, and at LSC headquarters in Washington, DC.

According to LSC's grant award letter, for calendar year 2012, ILS received over $4.7 million for the Basic Field grant and $107,097 for the Migrant grant. For the calendar year 2013, ILS was awarded over $5.0 million for Basic Field grant and $104,899 for the Migrant grant. Non-LSC funding for calendar year 2012 was approximately $2.9 million according to LSC Grantee Profile, Funding Data on LSC's website.

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.

OBJECTIVE

The overall objective was to assess the adequacy of selected internal controls in place at ILS 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.

OVERALL EVALUATION

While many of the controls were adequately designed and properly implemented as the controls related to specific grantee operations and oversight, the grantee needs to place more emphasis on establishing and documenting some internal controls. The OIG tested 94 disbursements and of that amount, 26 disbursements (27.6 percent), totaling over $6,900, were unallowable, unsupported, or not properly processed.

The grantee's current practices involving soliciting and awarding contracts were generally in accordance with the LSC's *Fundamental Criteria*. However, grantee's written policies and procedures relating to soliciting and awarding contracts need to be revised to include all components of the *Fundamental Criteria*.

ILS has policies and procedures over the use of the corporate credit cards in its Accounting Manual. A review of the credit card statements confirmed that the grantee uses a credit card log that lists all the purchases made for the period with appropriate approvals. However, the grantee did not have an adequate practice over the use of its gas credit cards. Additionally, the grantee needs to develop written policies and procedures over the use of the gas cards.

While the cost allocation process appeared to be reasonable, written procedures relating to cost allocation were not adequate. The procedures need to provide sufficient details, as required by the LSC Accounting Guide, fully describing how costs are allocated.

The grantee did not have written policies regarding accounting for derivative income. While the amounts received for derivative income during the period under audit were minimal, the potential for receiving additional derivative income has increased due to regulatory changes that permit the acceptance of attorney's fees. Written policies and procedures will help ensure that the grantee properly accounts for and allocates these fees when received.

Finally, our review noted that the grantee's fixed assets policies and procedures contained in its Accounting Manual were mostly comparable to LSC *Fundamental Criteria* except for a lack of policies on disposal of ILS property and reconciliation of physical inventory count with property records. However, management was not following some of its own policies in practice, in that inventories were not conducted biennially, inventory count sheets were not fully annotated, and tag numbers were not recorded in the property records. Also, the physical inventory results were not reconciled with property records.

AUDIT FINDINGS

DISBURSEMENTS

Of the 94 disbursements tested, 26 disbursements, valued at $6,968, were not allowed, inadequately supported, or not properly processed. Our testing noted 8 disbursements that were unallowable, 4 that were unsupported, and 14 that were inappropriately processed[1]. Ensuring allowable costs, maintaining adequate supporting documentation and preparing purchase documents appropriately helps to ensure that funds are only used for authorized purposes.

The Controller stated that the unallowable and unsupported disbursements were due to oversight. The grantee's Accounting Manual included a section that prohibited LSC funds from being used for restricted purchases (alcohol was provided as an example). The Controller also stated that the employees were aware of all restricted purchases and that the noted unallowable disbursements were due to oversight.

The inappropriately processed purchase orders originated from one branch office. The Controller stated that the office had been counseled against this practice but there had been no change.

LSC Regulation 45 CFR Part 1630, Costs Standards and Procedures, among other requirements, provides that expenditures by a grantee be reasonable and necessary for the performance of the grant or contract and adequately documented. The *Fundamental Criteria* also states that disbursements require adequate documentation supporting the reason for each disbursement contained in the files. Also, the ILS Accounting Manual, paragraph 3.4, states that three copies of a sequentially numbered purchase order is generated by each office and that purchase orders must be approved by the managing attorney. One copy of the purchase order is sent to the vendor, one to administration, and one to a file at the local office.

Unallowable Costs

LSC funds were used to pay for eight disbursements, totaling $667, that were unallowable.

- Four disbursements totaling $363, to purchase flowers for bereaved employees and members of the Board upon their loss of a family member.
- Four disbursements totaling $304, to pay late fee charges incurred on credit cards and gas cards.

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[1] Based on information received in management comments and management's statements that all items and services were received, we are not questioning the cost. However, the finding and recommendation still remain.

Unsupported Costs

Supporting documentation was missing for four disbursements (representing five transactions) of LSC funds totaling $3,492:

- Employee/intern reimbursement totaling $55 for attending a conference.
- Employee reimbursement totaling $13 for a luncheon.
- Luncheon costs totaling $46 and $500 respectively paid for with LSC funds did not have the business purpose and names of people in attendance included with the receipt.
- Moving and storage expenses totaling $2,878 without a statement of work, signed by grantee management to support the amount paid, detailing the number of hours and workers needed to accomplish the task.

Inappropriately Prepared Purchase Orders

Purchase orders were not prepared in accordance with the grantee's purchasing procedures for 14 disbursements totaling $2,809.

- Eight purchase orders totaling $1,185 had no description of products purchased and instead had "see attached" denoted. The attachment referred to the invoice for the purchase. This implies that the purchase order was not prepared until after the items were ordered.
- Six purchase orders totaling $1,624 were dated after the order was placed to the vendor. This implies the purchase order was prepared after the purchase request.

Additionally, we noted that the grantee did not mark invoices as paid or otherwise cancelled. Of the 94 transactions tested, none of the invoices and other supporting documentation that were approved for payment were marked "paid." The controller stated that they had been stamping the invoices with a paid stamp a while back but stated that they had stopped doing it for no particular reason. Annotating the invoice and supporting documentation that the vendor has been paid helps ensure that duplicate payments are not made.

While the questioned cost amounts are not very large, the lack of controls that allowed these errors is of concern. Therefore, because the 12 disbursements were not allowed or inadequately supported within the meaning of 45 CFR §1630.2, the OIG is questioning $4,159 charged to LSC funds. The OIG will refer the questioned costs to LSC management for review and action.

Recommendation 1: The Executive Director should ensure that staff members follow ILS established policies and procedures.

GAS CREDIT CARDS

The grantee did not have adequate controls over the use of gas credit cards. Specifically, the grantee did not have written policies and procedures to govern the use of the gas credit cards. In addition, the grantee did not have a process in place to ensure that the cards and related gas purchases were used only for business purposes.

The grantee had three gas credit cards. One card was controlled by the Director of Administration and the other two by the Director of Migrant Farmworker Project. According to the grantee, the gas credit cards were used to fuel personal cars for travel to offsite locations. The two cards held by the Director of Migrant Farmworker Project were used by summer interns who travel to remote locations. While a sign-out sheet was used to document when the cards were given to the interns, controls were not in place to ensure that the gas purchased for personal vehicles was reasonable for the business to be conducted. According to the Controller, the program felt that since the gas card could only be used for gas there was no need for policies.

While restricting the card to gas purchases only provides control over what can be purchased. This, by itself, does not prevent the purchase of gas exceeding what is necessary to conduct business or to prevent the purchase of gas for personal use. Properly controlling gas purchases through written policies and sound practices helps reduce the potential for misuse and protects the grantee's limited assets.

Recommendations: The Executive Director should:

Recommendation 2: develop written policies and procedures that govern the use of the gas cards and ensure proper accountability of the gas purchases.

Recommendation 3: develop a reimbursable system based on mileage claims that ensures gas purchases are for business purposes. An example would be the use of a travel reimbursement system that uses a fixed rate per mile and a form that captures the following information:

a. purpose and location of the business trip
b. business miles per trip
c. a computation of the business miles driven times the fixed rate per mile
d. dollar amount of gas purchased using the grantee gas card (receipts required)
e. a computation of amount owed to or by the traveler (item c minus item d)
f. signature blocks for both the traveler making the claim and the manager approving the claim.

WRITTEN POLICIES

Operating practices for some areas reviewed were not documented in the grantee's Accounting Manual to comply with the *Fundamental Criteria* contained in the LSC Accounting Guide. The Accounting Manual documents the policies and procedures to be followed by ILS staff in meeting the objectives and criteria of LSC and its other funding sources. The grantee's current practices in use involving contracting, cost and cost allocation generally conformed to the *Fundamental Criteria*, but these practices need to be fully documented. Additionally, the grantee's derivative income practice needs to be fully documented.

Contracting policies did not include all necessary requirements of LSC's *Fundamental Criteria*. The written policies did not include procedures for various types of contracts; competition requirements; dollar thresholds for approvals; documentation requirements to support contracting decisions and contract modifications; and contract oversight responsibilities. For the seven contracts reviewed, adequate documentation was on file supporting contract decisions and payments made to the vendor agreed with contract terms.

The cost allocation process appears to be reasonable as indirect costs are allocated to each funding source based on direct costs incurred by each source. While the grantee's Accounting Manual did address its allocation system, the written procedures did not fully describe the process as practiced by the grantee. Direct costs were determined by the percent of time staff members were assigned to specific grants. Indirect expenses for each office were apportioned to the grants based on the direct cost percentages. The OIG noted that allowable indirect costs incurred by the administrative office were almost all charged to LSC grant funds rather than allocating the indirect costs to all funders based on the overall percentage of direct cost for each funder. Since the administrative office provides services to all offices and funders, the indirect costs incurred by the administrative office should be allocated to each grant's funds based on an equitable distribution system.

The grantee received derivative income in the form of interest and attorney's fees. The grantee had a practice of allocating 100 percent of the interest and attorney's fees to LSC. However, the policies and procedures on how to allocate derivative income were not documented. Because the potential for attorney's fees has increased due to regulatory changes, written policies and procedures will help ensure that the grantee properly accounts for and allocates these fees when received.

Without adequate written policies and procedures in place, transactions may be initiated and recorded that violate management intentions, or possibly laws or grant restrictions. Written policies and procedures also serve as a method to document the design of controls and to communicate the controls to the staff.

Recommendations: The Executive Director should:

Recommendation 4: ensure written policies and procedures for contracting address all required areas contained in LSC's *Fundamental Criteria*.

Recommendation 5: ensure written policies and procedures for cost allocation are revised to fully describe the process as practiced by the program.

Recommendation 6: ensure indirect costs in the administrative office are allocated based on the direct time percentage for the grant.

Recommendation 7: develop written policies for derivative income that ensure such income is properly accounted for and allocated to funding sources.

FIXED ASSETS

ILS fixed assets written policies and procedures were mostly comparable to LSC *Fundamental Criteria* except for lack of policies on disposal of ILS property. Notwithstanding, grantee management was not following some of its own policies.

a. Inventories were not conducted at least once every two years in some branch offices as required by the *Fundamental Criteria*. Of the nine branch offices reviewed, ILS did not conduct regular biennial inventories for four of the branch offices. The Controller stated that this was caused by difficulty in coordinating schedules of staff conducting the inventory counts.

b. ILS inventory count sheets are not fully completed. A review of the Excel spreadsheet used for recording physical inventory noted that items marked by an "X" are items that are included in the count; items that are disposed of are marked "Disposed". However, some items on the inventory count sheets were not annotated and we were unable to determine if that meant they were missing at the time of count or not counted due to other reasons. Of the nine items reviewed, five items were not annotated on the physical inventory count sheet. Therefore, we could not determine if the items were counted or missing at the time the inventory was taken. We did confirm that the items not annotated were on hand and located in the Administration building.

c. ILS property records (Fixed Asset System) did not include a unique identifier, such as a tag number as required by LSC *Fundamental Criteria*. The unique identifier allows the grantee to easily trace items from the inventory count to the property record. The grantee's inventory count sheets had a tag number but the property records did not include the tag number. According to the Controller, the grantee did not think it was relevant to have the tag number in the Fixed Asset System as they thought items could be searched by other means such as date, description or amount of purchase.

Finally, the grantee did not reconcile the results of the physical inventory count to the property records. According to the Controller, the grantee was not aware that a reconciliation of physical inventory results to property records was required. In addition, there were no written policies and procedures to cover the physical inventory reconciliation.

Properly accounting for fixed assets enables the grantee to safeguard the assets, fully account for the assets purchased, and support reconciliations so that property asset balances are accurate.

Recommendations: The Executive Director should:

Recommendation 8: develop written policies on disposal of ILS property and reconciliation of physical inventory count with property records.

Recommendation 9: develop compensating inventory procedures if grantee staff is not available to conduct a full and independent inventory. Some compensating procedures could be to independently inventory high value and sensitive assets or recruit volunteers to conduct the physical inventory.

Recommendation 10: improve the physical inventory count process to ensure that all items on inventory count sheets have annotations to indicate the results of the inventory.

Recommendation 11: update the property records to include tag numbers as required by LSC *Fundamental Criteria* and also to enable the grantee to easily trace items from the inventory count sheets to the property records.

Recommendation 12: ensure that the results of physical inventory counts are reconciled with property records so as to address any differences between quantities determined by the inventory and those shown in the accounting records.

SUMMARY OF GRANTEE MANAGEMENT COMMENTS

Grantee management agreed with the findings and recommendations contained in the report. Grantee management stated its Accounting Manual will be updated to address deficient policies and procedures listed in the report. Management also submitted additional documentation and explanations to support some disbursements that the OIG questioned. Our evaluation of the additional information is discussed below. Management's formal comments can be found at Appendix II. Appendix II does not include the additional supporting documents provided by management.

OIG EVALUATION OF GRANTEE MANAGEMENT COMMENTS

The OIG considers grantee management's actions planned responsive to the findings and recommendations contained in the report. The actions planned by grantee management to revise and update its Accounting Manual should correct the issues identified in the report. The OIG considers all 12 recommendations open until notified in writing that the grantee's Accounting Manual has been updated and communicated to ILS staff. However, we do provide the following information for three of management's comments.

Disbursements

- Management provided a document as evidence that a disbursement, questioned by the OIG, for moving and storage expenses was sufficient to support the expenditure. However, the document provided did not pertain to the same transaction that the OIG identified and therefore the disbursement remains a questioned cost.

- While agreeing that the purchase orders were not prepared in advance, management asserted that all items ordered were reviewed by the grantee. Because of management's assertion and other related information, the OIG is no longer questioning the associated costs and will reduce the amount referred to LSC management by $2,809. However, the finding and recommendation remain unchanged.

Gas Credit Cards

- Management comments indicated that a system was in place for summer interns employed by the grantee's Migrant Farm Worker Law Center to reconcile gas credit card purchases for their personal vehicle and miles driven on official business. The comments contained a statement on how the system worked and examples of the forms used for the reconciliation. However, at the time of audit, we were not informed of such a system nor provided any supporting documentation for the system. At no time during our discussions with grantee management on this subject was the system disclosed to us. While the system described in management comments meets the intent of our recommendation to control the use of grantee gas credit cards for personal vehicles, the system still needs to be formally documented and applied to all grantee gas cards used to purchase gas for staff using personal vehicles conducting official business.

APPENDIX I

SCOPE AND METHODOLOGY

To accomplish the audit objective, the OIG identified, reviewed, and evaluated internal controls related to the following activities:

- Cash disbursements
- Contracting
- Cost Allocation
- Credit cards
- Property and Equipment
- Internal Management Reporting and Budgeting
- Client Trust Fund
- Derivative Income.

To obtain an understanding of the internal controls over these areas, policies and procedures were reviewed, including manuals, guidelines, memoranda, and directives setting forth current practices. Grantee officials were interviewed to obtain an understanding of the internal control framework and management and staff were interviewed as to their knowledge and understanding of the processes in place. To review and evaluate internal controls, the grantee's internal control system and processes were compared to the guidelines in the *Fundamental Criteria of an Accounting and Financial Reporting System (Fundamental Criteria)* contained in the Accounting Guide. We assessed the reliability of computer generated data provided by the grantee by reviewing source documentation for the entries selected for review. We determined that the data were sufficiently reliable for the purposes of this report. This review was limited in scope and was not sufficient for expressing an opinion on the entire system of grantee internal controls over financial operations.

To test controls and the appropriateness of expenditures, we reviewed a judgmentally selected sample of disbursements that included employee and vendor files, and credit card purchases. The sample was taken from the period January 1, 2012, through April 30, 2013, and represented 10.9 percent of the $1,992,660.90 disbursed for expenses other than payroll and consisted of 94 transactions totaling $182,949.30. To assess the appropriateness of expenditures, we reviewed supporting documentation such as invoices and vendor lists, and traced the transactions to general ledger details. Amounts indicated as being allocated to LSC were traced to LSC general ledger accounts. The appropriateness of those expenditures was evaluated on the basis of the grant agreements, applicable laws and regulations, and LSC policy guidance.

To review controls over contracts, we requested all contracts and/or agreements involving disbursements that were entered into during 2012 and 2013. We also relied on the ILS Check Register to identify the universe of contracts. Of a total of eighteen contracts identified, we judgmentally selected a sample of seven contracts. We reviewed documentation maintained in contract files to determine if adequate procedures were used for securing the contracts and verified that payments made to the vendor were comparable to contractual amounts. We also interviewed ILS management to assess compliance with the LSC *Fundamental Criteria*.

The cost allocation process was reviewed to determine if the system was in compliance with the *LSC Fundamental Criteria*. We also compared the cost allocation process actually in use to the written description provided by the grantee to determine if the cost allocation process was operating as documented in the grantee's Accounting Manual.

In addition to testing credit card purchases in the disbursement sample, the credit card use process was reviewed and compared to the written policies.

Controls over management, reporting and budgeting, and property and equipment were reviewed by examining current grantee practices and reviewing the written policies contained in the grantee's Accounting Manual.

To evaluate controls over client trust fund accounting and derivative income, we interviewed appropriate program personnel, examined related policies and procedures and traced transactions to general ledger details.

The on-site visit was conducted from May 1, 2013 through May 10, 2013. Audit work was conducted at the grantee's main office in Indianapolis, Indiana and at LSC headquarters in Washington, DC. Disbursements tested pertained to the period January 1, 2012 through April 30, 2013. Contracts reviewed covered the 2-year period of performance from January 1, 2012 through December 31, 2013.

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.

APPENDIX II

Grantee Management Comments

Indiana Legal Services, Inc.

NORMAN P. METZGER, EXECUTIVE DIRECTOR
JOSEPH E. SIMPSON, DIRECTOR OF ADMINISTRATION

September 26, 2013

Ronald D. Merryman
Assistant Inspector General for Audit
Office for the Inspector General
Legal Services Corporation
3333 K Street
3rd Floor
Washington, DC 20007

Re: Draft report on selected internal controls
Recipient # 515030

Dear Mr. Merryman,
I am in receipt of your draft report on the results of your audit of Selected Internal Controls at Indiana Legal Services, Inc., dated August 30, 2013. I appreciate the efforts of your on-site audit staff and the professional manner in which they conducted the audit. I find the results of the audit to be generally positive.

At your request, I am providing you with our comments which address the twelve recommendations contained in the draft report. I will address each of the recommendations individually and state those actions we plan to take or have taken to implement the recommendations.

Please contact me if you need additional information or wish me to clarify any of my comments.

Norman P. Metzger
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Indiana Legal Services, Inc. #515030
Comments to the OIG Report on Selected Internal Controls dated August 30, 2013

Indiana Legal Services, Inc. generally agrees with the findings and the recommendations described in your August 30th report. Each of the twelve recommendations made in the audit findings draft report will be addressed individually below.

Recommendation 1: The Executive Director should ensure that staff members follow ILS established policies and procedures.

Finding and ILS comment: *The OIG audit found that of ninety-four disbursements tested, twenty-six disbursements valued at $6,968 were not allowed, inadequately supported or not properly processed. Of the disbursements tested eight totaling $667 used LSC funds to purchase bereavement flowers and to pay late fee charges incurred on credit cards and gas cards.* The $667 should not have been charged to the LSC funds and ILS agrees that such charges are not allowable pursuant to 45 CFR Part 1630. Four of the disbursements that totaled $304 were to pay late fee charges incurred on credit cards and gas cards. Late fees arose because the turnaround time for the payment of the gas credit cards was fifteen days, making it difficult for ILS to process the invoice for payment by the due date. ILS will negotiate with the current credit card company to have the turnaround time to be one month or ILS will secure a different gas company's credit card that extends the due date to one month. Regardless, late charges will always be charged to non-restricted funds.

Finding and ILS comment: *Supporting documentation was missing for four disbursements (representing five transactions of LSC funds totaling $3,492).* ILS agrees that three of the disbursements totaling $614 did not have the necessary supporting documentation. LSC should allow such charges since they were used to pay for staff attendance at conferences and luncheons that had a legitimate business purpose, notwithstanding the names of the staff persons were not included with the receipt. The moving and storage expenses which OIG found to total $2,878 actually did have a statement of work signed by Ida Hayes, the office manager of the Indianapolis branch office, which detailed the number of hours the workers used to complete the work. Further, the actual charge for the moving services was $2,776.95 and should be treated as a cost properly supported with documentation. I have attached a copy of ILS check number 93526 in the amount of $2,776.95, the invoice from Stuart's Moving and Storage for that amount and the bills of lading for 2 separate days dated January 19, 2012 and January 20, 2012, both signed by Ms. Hayes.

Finding and ILS comment: *Purchase orders were not prepared in accordance with ILS purchasing procedures in 14 disbursements totaling $2,809.* Eight purchase orders totaling $1,185 denoted "see attached" referring to each of the invoices for the items purchased. Clearly those purchase orders were not prepared until the items were ordered from the vendor. Six purchase orders totaling $1,624 were dated after the order was placed with the vendor clearly indicating that these purchase orders were prepared after the purchase request. These 14 disbursements do not comply with ILS policies and procedures and each of the ILS office managers will be immediately instructed to cease these practices. Nonetheless, LSC should allow these disbursements to stand using LSC funds because ILS did receive the items and services in question.

Finding and ILS comment: *Of the ninety-four transactions tested, none of the invoices and other supporting documentation that were approved for payment were marked "paid".* All of the transactions tested had cancelled checks proving the vendors had been paid. ILS will, however, going forward annotate invoices and supporting documentation that the vendor was paid.

Recommendation 2: The Executive Director should develop written policies and procedures that govern the use of the gas cards and ensure proper accountability of the gas purchases.

Finding and ILS comment: *ILS did not have adequate controls of the use of the gas credit cards.* Specifically, ILS did not have written policies and procedures governing these gas credit cards. ILS does not have written policies and procedures in its accounting manual regarding gas credit cards. ILS will develop such written policies for inclusion in our accounting manual.

Recommendation 3: The Executive Director should develop a reimbursable system based on mileage claims that ensures gas purchases are for business purposes. An example would be the use of a travel reimbursement system that uses a fixed rate per mile and a form that captures the following information:

a) Purpose and location of the business trip
b) Business miles per trip
c) A computation of the business miles driven times the fixed rate per mile
d) Dollar amount of gas purchased using the grantee gas card (receipts required)
e) A computation of amount owed to or by the traveler (item c minus item d)
f) Signature blocks for both the traveler making the claim and the manager approving the claim.

Finding and ILS comment: *ILS did not have a process in place to ensure that the cards used to purchase gas were used only for business purposes.* ILS has three gas credit cards. One is controlled by the Director of Administration and two are controlled by the Director of the Migrant Farmworker Law Center. The ILS gas credit cards are used to fuel personal cars used for ILS business purposes. The gas credit cards are primarily used by summer interns employed by the Migrant Farmworker Law Center traveling to migrant farmworker camps. ILS does have in place a reimbursement system that is based on mileage claims submitted on travel reimbursement forms paying the interns $0.44 per business mile. The intern submits travel expense claims on the ILS forms provided and deducts from the total amount claimed the amounts that were charged to the credit card. The interns attach the receipts of the gas purchases to the claim form. The system recommended by the OIG audit is the system that is used by ILS currently. See an example that an intern claimed that is attached. That notwithstanding, the written policies and procedures ILS will develop governing the use of gas credit cards will include a reimbursement system based on mileage claims, which incorporates our current system at practice.

Recommendation 4: The Executive Director should ensure written policies and procedures for contracting address all required areas contained in LSC's *Fundamental Criteria*.

Finding and ILS comment: *ILS operating practices in some areas reviewed were not documented in the ILS accounting manual to comply with the Fundamental Criteria contained in the LSC accounting guide. ILS' current practices in use involving contracting allocation generally conform to the Fundamental Criteria but these practices need to be fully documented. The ILS contracting policies did not include all the necessary requirements of the LSC's Fundamental Criteria.* The ILS accounting manual will be revised in accordance with the provisions 3-5.16 of the *Fundamental Criteria* covering contracting and will include written procedures for various types of contracts, competition requirements, dollar thresholds for approval, documentation to support contracting decisions, contract modification, and contract oversight responsibilities. I should emphasize that, of the seven contracts reviewed by OIG, all were found to have adequate documentation on file, supporting contract decisions, and payments made to vendors pursuant to contract terms.

<u>Recommendation 5</u>: The Executive Director should ensure written policies and procedures for cost allocations are revised to fully describe the process as practiced by the program.

Finding and ILS comment: *ILS written procedures in the ILS accounting manual, while addressing its allocation system, did not fully describe the process practiced by ILS.* Direct costs were determined by the percent of time staff members were assigned to specific grants. ILS will ensure that its accounting manual contains written policies and procedures for cost allocation that reflects the practice that the percent of time staff members assigned to a grant are the same percentages allocated for costs charged to a grant.

<u>Recommendation 6</u>: The Executive Director should ensure indirect costs in the administrative office are allocated based on the direct time percentage for the grant.

Finding and ILS comment: *The OIG noted that allowable indirect costs incurred by the administrative office were almost all charged to LSC grant funds. The OIG wants ILS to insure that the indirect costs for the administrative overhead of a grant be allocated to that grant based on the direct time percentage for the grant.* ILS will review all of its contracts with funders to determine which of these grants permit charges for indirect costs for administration. For example, the Low Income Taxpayer Clinic funded by the IRS permits five percent of the grant to be charged to indirect costs. Likewise, the Equal Justice Works grant permits indirect administrative costs to be charged to the grant. ILS believes that its United Way and Area Agency contracts do not permit indirect administrative costs to be charged to their grants. ILS will explore with these agencies whether they will allow such indirect charges. Generally, these grants expect ILS to match such grants and it is out of that match that administrative indirect costs are allocated.

<u>Recommendation 7</u>: The Executive Director should ensure written policies for derivative income that ensure such income is properly accounted for and allocated to funding sources.

Finding and ILS comment: *ILS had a practice of allocating one hundred percent of interest and attorney's fees to the LSC. However, ILS does not have policies and procedures on allocating derivative income.* ILS acknowledges that ILS derivative income allocated to LSC requires such income to be treated as restricted income. ILS will update its accounting manual with new written policies and procedures that include allocation of derivative income to properly account for attorney's fees and interest. These written policies and procedures will be communicated to staff to ensure that it is management's intention that such income will be treated as restricted income and to properly account for such income by allocating it to its funding source.

<u>Recommendation 8</u>: The Executive Director should ensure written policies on disposal of ILS property and reconciliation of the physical inventory count with the property records.

Finding and ILS comment: *ILS fixed asset written policies and procedures were mostly comparable to LSC Fundamental Criteria except for the lack of policies for the disposal of ILS property.* The ILS accounting manual will be updated to include new written policies and procedures for the disposal of ILS property. ILS will reconcile its physical inventory count with its property records.

<u>Recommendation 9</u>: The Executive Director should develop compensating inventory procedures if grantee staff is not available to conduct a full and independent inventory. Some compensating procedures could be to independently high inventory value and sensitive assets or recruit volunteers to conduct the physical inventory.

Finding and ILS comment: *Inventories were not conducted at least once every two years in some offices as required by the Fundamental Criteria. Of the nine offices reviewed by the OIG, some did not experience bi-annual inventories as required by the ILS accounting manual. A partial explanation for not conducting bi-annual inventories was the difficulty of coordinating staff schedules for the inventory count.* Currently, only the ILS Indianapolis branch office has yet to receive its bi-annual inventory. The Indianapolis branch inventory will be completed by the end of the calendar year 2013. To the extent that bi-annual inventories were not completed in a timely basis because of the difficulty of coordinating staff schedules, ILS will develop a compensating inventory procedure. The compensating policies and procedures will be in writing and included in the updated ILS accounting manual. The compensating procedures will permit branch office staff, instead of just administrative office staff, to conduct the physical inventory of their office, especially when the inventory will include high value and sensitive assets. The ILS Controller will have the ILS auditor, Blue & Company, review and comment upon the proposed compensating written policies and procedures prior to implementing them.

<u>Recommendation 10</u>: The Executive Director should improve the physical inventory count process to ensure that all items on inventory count sheets have annotations to indicate the results of the inventory.

Finding and ILS comment: *ILS inventory count sheets were not fully completed.* The count sheets are in an Excel spreadsheet which ILS uses to record physical inventory. The fixed asset inventory is kept in the fixed asset software. ILS records the physical inventory by marking an X beside items that were found, D by items that were disposed of and, when items were not annotated, the items were not located. The executive director has directed the administrative staff to ensure that all items recorded in the inventory are counted and properly annotated. If items are not found, the executive director has directed the administrative staff to follow up with branch office staff to determine the reason that the property is missing. High value computers are kept and maintained at a server farm in

Columbus, IN pursuant to an agreement with that company. Those servers are not yet recorded in the physical inventory, but were in the fixed asset inventory. Going forward, IT staff will be instructed to tag those servers and count them on a bi-annual physical inventory. Such assets will be accounted for in the inventory notwithstanding they are not physically located in any of the ILS branch offices or the administration office.

Recommendation 11: The Executive Director should update the property records to include tag numbers as required by LSC Fundamental Criteria and also to enable the grantee to easily trace items from the inventory count sheets to the property records.

Finding and ILS comment: *ILS property records (fixed asset system) did not include a unique identifier such as a tag number required by LSC Fundamental Criteria.* ILS property records do include tag numbers. However, not all ILS property had a tag number affixed to it. For example, the ILS servers housed at the server farm in Columbus, IN, were not tagged. I have instructed the administration staff and the tech staff to tag all ILS property that is found in the ILS property records and the fixed asset system.

Recommendation 12: The Executive Director should ensure that the results of physical inventory counts are reconciled with property records so as to address any differences between quantities determined by the inventory and those shown in the accounting records.

Finding and ILS comment: *ILS did not reconcile the results of the physical inventory count to the property records.* ILS will update the ILS accounting manual to include written policies and procedures requiring the physical inventory to be reconciled with the physical inventory count of the property records. The policies will ensure that all assets purchased by ILS will be in the physical inventory and that the physical inventory count will be recorded to the fixed asset records and vice-a-versa.