LSC

Legal Services Corporation
Office of Inspector General

Inspector General
Jeffrey E. Schanz

August 14, 2008

Ms. Anita Santos-Singh
Executive Director
Philadelphia Legal Assistance Center
42 South 15th Street, Suite 500
Philadelphia, PA 19102

Dear Ms. Santos-Singh:

Attached is our final report on the results of our audit on Selected Internal Controls at Philadelphia Legal Assistance Center. We reviewed your response with regard to the findings in our draft report and believe the comments address all recommendations. Based on your comments, we consider Recommendations 2 and 3 closed. However, since the Accounting Manual is still being updated, we consider Recommendation 1 open. Because you have already provided us with your planned actions, you do not need to submit a separate corrective action plan. Please notify this office in writing when you have completed updating the Accounting Manual.

We want to thank you and your staff for the cooperation and assistance you provided us.

Sincerely,

[redacted]

Jeffrey E. Schanz
Inspector General

cc: <u>Legal Services Corporation</u>
Helaine Barnett, President

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LEGAL SERVICES CORPORATION
OFFICE OF INSPECTOR GENERAL

LSC

REPORT ON SELECTED INTERNAL CONTROLS –

PHILADELPHIA LEGAL ASSISTANCE CENTER

RNO 339000

Report No. AU08-04

AUGUST 2008

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TABLE OF CONTENTS

INTRODUCTION

In November, 2007, management of the Legal Services Corporation (LSC) referred for follow-up to the Office of Inspector General (OIG) instances of internal control weakness at certain LSC grantees identified in the Government Accountability Office (GAO) Draft Report entitled, *Legal Services Corporation – Improved Internal Controls Needed in Grants Management and Oversight* or indentified in a November 13, 2007 meeting between GAO and LSC staff. The final GAO report (GAO–08–37) was published on December 28, 2007.

LSC management requested that the OIG assess whether the issues specifically identified by GAO had been corrected at each of grantees referred to the OIG by management.

BACKGROUND

GAO assessed whether LSC's internal controls over grants management and oversight processes provide reasonable assurance that grant funds are used for their intended purposes. GAO analyzed records and interviewed LSC officials to obtain an understanding of LSC's internal control framework, including the monitoring and oversight of grantees, and performed limited reviews of internal controls and compliance at 14 grantees. GAO found control weaknesses at 9 of the 14 grantee sites it visited. These weaknesses included using LSC grant funds for expenditures with insufficient supporting documentation, and for unusual contractor arrangements, alcohol purchases, employee interest-free loans, lobbying fees, late fees, and earnest money.

OBJECTIVE

Our overall objective was to determine whether the conditions cited in the GAO report were corrected and controls were put in place by Philadelphia Legal Assistance Center (grantee) to detect or prevent similar situations from recurring. In addition, we evaluated other selected financial and administrative areas relating to the GAO findings and tested the related controls to ensure that expenditures were adequately supported and allowed under the LSC Act and regulations.

SCOPE AND METHODOLOGY

To accomplish our objective we reviewed controls over the client intake process, employee benefits and reimbursements, disbursements and internal management reporting/budgeting. To obtain an understanding of the internal controls over these areas, we reviewed grantee policies and procedures, including any manuals, guidelines, memoranda, and directives setting forth current grantee practices. We interviewed grantee officials to obtain an understanding of the internal control framework and interviewed grantee management and staff as to their knowledge and understanding of the processes in place.

We conducted fieldwork at the grantee's central administrative office in Philadelphia, PA. To test for the appropriateness of expenditures and the existence of adequate supporting documentation, we reviewed disbursements from a judgmentally selected sample of employee and vendor files. To assess the appropriateness of grantee expenditures, we reviewed invoices, vendor lists, and general ledger details. The appropriateness of grantee expenditures was based on the grant agreements, applicable laws and regulations, and LSC policy guidance. Our grantee reviews were limited in scope and were not sufficient for expressing an opinion on the entire system of grantee internal controls or compliance.

The on-site fieldwork was conducted from February 25, 2008 through February 29, 2008. Documents reviewed pertained to the period January 1, 2007 through February 21, 2008. Our work was conducted at the grantee's site and at LSC headquarters in Washington, DC.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

OVERALL EVALUATION

Philadelphia Legal Assistance Center management has taken action to correct the issues identified by GAO and implemented internal controls to prevent and detect such issues in the future. Grantee management has taken appropriate steps to address the specific issues raised by GAO dealing with undocumented salary advances to employees and insufficient supporting documentation for disbursements.

During our on-site fieldwork, the grantee had a draft written policy on salary advances and an authorization process requiring employees to sign a statement acknowledging the amount advanced and the monthly repayment amount. However, the draft policy on salary advances needs to be strengthened to further enhance internal controls.

Grantee disbursements tested were adequately supported, allowable and properly allocated to LSC. Internal controls over the client intake process, employee benefits and reimbursements, disbursements and internal management reporting/budgeting were operating in the manner expected to ensure compliance with the LSC Act and LSC regulations. However, we did identify three areas where internal controls could be strengthened. The grantee's Accounting Manual has not been updated since 1996 and does not incorporate current accounting and fiscal practices. The grantee does not treat all adjustments to the accounting records as journal entries, and when journal entries are made they are not reviewed or approved by a separate grantee employee. Finally, bank account reconciliations were not reviewed and approved by a responsible individual.

RESULTS OF AUDIT

SALARY ADVANCES

GAO reported the following weaknesses when reviewing this grantee: 1) grantee employees were not required to sign contracts for salary advances; 2) since controls over the loans were non-existent, GAO was unable to determine the completeness of a list of outstanding employee loans; and 3) GAO identified no authority to use LSC grant funds for interest free or other loans to grantee employees.

Our review of these issues found that since the GAO report, LSC management issued guidance to grantees not prohibiting salary advances to employees, but noting the importance of written policies and procedures governing such advances including timely repayments[1]. In addition we found that the grantee developed a draft policy and instituted changes to require employees to sign salary advance/loan agreements that specify the amount loaned and the amount to be repaid. Based on our review, all of the advances outstanding as of December 31, 2007, were now supported by signed agreements. The grantee further revised the agreement to document management's approval for new advances. The draft policy on salary advances satisfactorily addressed controls over salary advances except that it did not specifically require repayments be made by payroll deduction. Subsequent to our on-site fieldwork, the Director of Finance provided us with the current policy in place on salary advances. The policy now includes a provision requiring repayments by payroll deduction. Since we believe this policy adequately addresses our concern, no recommendation is necessary and the finding is considered closed.

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[1] Advisory from the President, Legal Services Corporation, to all LSC Executive Directors regarding "Fiscal Management and Use of LSC Funds" (March 20, 2008)

DISBURSEMENTS AND SUPPORTING DOCUMENTATION

Our review of a 135 judgmentally selected disbursements, valued at $113,299 disclosed that all disbursements were adequately supported, allowable, and properly allocated to LSC. The disbursements in our sample covered the period January 1, 2007 through February 21, 2008.

INTERNAL CONTROL REVIEW OF SELECTED AREAS

Our review of the internal controls over the client intake process, employee benefits and reimbursements, disbursements and internal management reporting/budgeting revealed that the controls are operating in the manner expected to ensure compliance with the LSC Act and LSC regulations. We did note three areas where internal controls could be strengthened:

1) Absence of Updated Accounting Manual

The grantee's Accounting Manual has not been updated since 1996 and does not incorporate policies and procedures describing current accounting and fiscal practices. In establishing an adequate internal control structure, each grantee must develop a written accounting manual that describes the specific procedures to be followed by the grantee in complying with the *Fundamental Criteria of an Accounting and Financial Reporting System* (*Fundamental Criteria*) contained in the Accounting Manual for LSC Recipients.

Grantee management has, nevertheless, implemented new practices strengthening internal controls over banking, petty cash, approval and timely payment of invoices, the payroll account and pre-audit file reviews. These revised practices need to be formalized and incorporated into the grantee's Accounting Manual. Grantee management also needs to incorporate existing procedures over internal management reporting into their Accounting Manual and develop written procedures governing consultant contracting.

Recommendation 1 - The Executive Director should revise and update the grantee's Accounting Manual to incorporate written policies and procedures describing the grantee's current accounting and fiscal practices.

Grantee Management Comments The Executive Director stated:

"The Executive Director will cause to be revised PLA's Accounting Manual to incorporate written policies and procedures describing PLA's current accounting and fiscal practices."

2) Adjusting Entries

The grantee does not treat all adjustments to the accounting records as journal entries, and when these adjustments are made they are not reviewed or approved by a separate grantee employee. According to the *Fundamental Criteria* each entry to the general journal should be fully described, adequately documented, sequentially numbered, and approved by an authorized individual. Unsupported or poorly referenced entries are difficult to trace and make it difficult to detect irregularities.

Recommendation 2 - The Executive Director should implement and follow procedures contained in the *Fundamental Criteria* to treat all accounting adjustments as journal entries so that the basis for these adjustments are adequately documented and approved by an authorized individual.

Grantee Management Comments The Executive Director stated:

> "The Executive Director will implement procedures contained in the *Fundamental Criteria of an Accounting and Financial Reporting System* contained in the Accounting Manual for LSC Recipients. The Executive Director and the Finance Director will adopt a system whereby the Executive Director can confirm, in writing or electronically, that she has reviewed and approves an adjustment to the accounting records."

3) Bank Account Reconciliations

Bank reconciliations were not conducted in accordance with the *Fundamental Criteria,* paragraph 3-5.2(d) which indicates that the statements shall be reconciled by an individual who has no access to cash, is not a regular check signer, and has no cash bookkeeping duties. In addition, the reconciliations shall be reviewed and approved by a responsible individual. The reconciliations were conducted by the Director of Finance because she was the only person handling the grantee's accounting function. The reconciliations should be approved by another responsible individual which would have added a needed internal control in this situation.

Recommendation 3 - The Executive Director should review and approve the bank reconciliations or appoint another responsible individual to perform this function.

Grantee Management Comments The Executive Director stated:

> "The Executive Director will appoint the Managing Attorney after he has been removed as a check signer to approve bank reconciliations in accordance with the *Fundamental Criteria*."

OFFICE OF INSPECTOR GENERAL EVALUATION OF GRANTEE MANAGEMENT COMMENTS

Grantee management agreed with all findings and recommendations. Actions taken or planned address the issues contained in this report. We consider Recommendations 2 and 3 closed. However, since the update to the Accounting Manual is not yet complete, we consider this finding open and will track Recommendation 1 until grantee management has completed the changes to the Manual. Because grantee management has already provided us with their planned actions, no separate corrective action plan is required.

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August 1, 2008

Ronald D. Merryman
Assistant Inspector General for Audit
Office of Inspector General
Legal Services Corporation
3333 K Street, NW, 3rd Floor
Washington, DC 20007-3522

RE: Comments on the OIG's Draft Report on Selected Internal Controls at Philadelphia Legal Assistance Center, Inc.

Dear Mr. Merryman:

Kindly accept this letter as Philadelphia Legal Assistance Center's (PLA) response to the OIG's Draft Report on Selected Internal Controls dated July 2008. The Draft Report has been reviewed by PLA management, PLA's Audit and Finance Committee and its Board of Directors. On July 17, 2008, upon recommendation of the Audit and Finance Committee, PLA's Board of Directors voted to adopt the three recommendations outlined in the OIG Draft Report. More specifically, the Board voted in favor of the following actions to implement the three recommendations:

Recommendation 1: The Executive Director will cause to be revised PLA's Accounting Manual to incorporate written policies and procedures describing PLA's current accounting and fiscal practices.

Recommendation 2: The Executive Director will implement procedures contained in the *Fundamental Criteria of an Accounting and Financial Reporting System* contained in the Accounting Manual for LSC Recipients. The Executive Director and the Finance Director will adopt a system whereby the Executive Director can confirm, in writing or electronically, that she has reviewed and approves an adjustment to the accounting records.

Recommendation 3: The Executive Director will appoint the Managing Attorney after he has been removed as a check signer to approve bank reconciliations in accordance with the *Fundamental Criteria*.

I am pleased to report that Recommendations 2 and 3 have already been implemented. We are still working to complete the first Recommendation. I hope that our response is satisfactory.

However, if there is any further follow-up required, please contact me at (215) 981-3808 or asantos@philalegal.org.

Sincerely,

[redacted]

ANITA SANTOS-SINGH
Executive Director