Office of Inspector General
Legal Services Corporation

Inspector General
Jeffrey E. Schanz

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September 30, 2019

Sheri Fox
Executive Director
Legal Aid of East Tennessee
607 West Summit Hill Drive SW
Knoxville, TN 37902

Dear Ms. Fox:

Enclosed is the Legal Services Corporation (LSC) Office of Inspector General's (OIG) final report for our audit on Selected Internal Controls at Legal Aid of East Tennessee. We included your comments in Appendix II of the final report.

The OIG considers proposed actions to Recommendations 1, 5, 7, 9, 13, 14, 15, 18, 20, 28, 30 and 31 as fully responsive. For Recommendation 1, we determined that the grantee's response satisfied the recommendation even though they partially concurred with it. These twelve recommendations are considered closed.

The OIG considers the proposed actions to Recommendations 2, 3, 4, 6, 11, 12, 16, 17, 19, 21, 22, 23, 24, 25, 26, 27, 29 and 32 as responsive. However, these recommendations will remain open until the OIG is notified in writing that the proposed actions have been completed and the supporting documentation and Board approved policies pertaining to Recommendation 2, 11, 16, 17, 21, 23, 24 and 32 are provided to the OIG.

The OIG considers the proposed actions to Recommendations 8 and 10 as partially responsive. The grantee also did not provide a corrective action plan specific to Recommendations 8 and 10. These recommendations will remain open until the OIG is provided a corrective action plan that specifically addresses these recommendations.

The OIG is referring the following questioned costs totaling $8,075 to LSC Management for their review and action:

- The OIG is referring questioned costs totaling $1,836 of attorneys' fees that were supported by LSC funds but allocated to other funding sources.

- The OIG is referring questioned costs totaling $3,419 of overpayment to employees that was charged to LSC.

- The OIG is referring questioned costs totaling $2,820 of unallowable expenses pursuant to 45 CFR Part 1630.

Please send us your response to close out the twenty open recommendations, along with supporting documentation within six months of the date of this final report. We thank you and your staff for your cooperation and look forward to receiving your submission by March 30, 2020.

Sincerely,

Jeffrey E. Schanz

Jeffrey E. Schanz
Inspector General

Enclosure

cc: Legal Services Corporation
Jim Sandman, President

Lynn Jennings,
Vice President for Grants Management

Legal Aid of East Tennessee
Amanda Dunn, Board Chairperson

Sent by E-mail to Board of Directors
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LEGAL SERVICES CORPORATION

OFFICE OF INSPECTOR GENERAL

FINAL REPORT ON SELECTED INTERNAL CONTROLS

LEGAL AID OF EAST TENNESSEE

RNO 643020

Report No. AU 19-04

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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 of East Tennessee related to specific grantee operations and oversight. Audit work was conducted at the grantee's administrative office in Chattanooga, TN and LSC headquarters in Washington, DC.

In accordance with the 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:

> The 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

Legal Aid of East Tennessee (LAET or grantee) is a nonprofit organization that provides legal representation, counseling, and other civil legal services for low income persons that reside in Tennessee. LAET serves 26 counties and operates out of branch offices in Chattanooga, Cleveland, Knoxville, Johnson City, Maryville and Morristown.

LAET operates with more than 40 funding sources to ensure that the elderly, victims of domestic violence, and low-income families receive civil legal assistance. According to the audited financial statement report for the fiscal year ending December 31, 2017, LAET's funding totaled $5,267,612. LSC provided approximately 48 percent of the total revenue or $2,510,631. The remaining $2,756,981 of LAET's funding was comprised of contributions or grants from public and private sources and through voluntary servicers.

OBJECTIVE

The overall objective was to assess the adequacy of selected internal controls related to specific grantee operations, oversight, program expenditures, and fiscal accountability in place at the grantee. The LSC OIG evaluated select 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 FINDINGS

To accomplish the audit objective, the OIG reviewed and tested internal controls related to disbursements, contracting, fixed assets, debit cards, cost allocation, derivative income, internal reporting and budgeting, general ledger and financial controls, employee benefits, and payroll. The controls were adequately designed and properly implemented as they relate to specific grantee operations over payroll and internal management reporting and budgeting. However, LAET needs to strengthen practices over derivative income, disbursements and employee benefits as well as strengthen practices and formalize in writing the internal controls within their Accounting and Internal Control Manual (or manual) in the areas of contracting, fixed assets, debit cards, cost allocation and general ledger and financial controls as detailed below. Additionally, the OIG reviewed a volunteer arrangement for which LAET does not have an adequate agreement in place; the arrangement constitutes a potential conflict of interest.

DERIVATIVE INCOME

LAET's written policies and procedures regarding derivative income were comparable to the *Fundamental Criteria* in the LSC Accounting Guide. However, attorneys' fees were not allocated in accordance with LAET's described practice or Regulation 45 CFR § 1609.4.

Attorneys' Fees Not Allocated in Accordance with LSC Regulations

The grantee received three attorneys' fees during the scope of our audit, totaling $2,720. The OIG tested all three fees and found they were incorrectly allocated according to the time and funding codes indicated on the Legal Server records. Legal Server is a case management software used widely by the civil legal aid community which facilitates the collection, reporting and storage of data. Grantee staff uses Legal Server to track and report cases as well as actual time worked per case. We noted the following:

- One attorneys' fee of $1,000 was allocated to a non-LSC funding source but should have been allocated to LSC in its entirety.
- The second attorneys' fee of $1,520 was allocated entirely to a non-LSC funding source but should have been partially allocated to LSC. Of the time charged to the case, 55 percent was charged to LSC. Therefore, $836 should have been allocated to LSC.

- The third attorneys' fee of $200 should have been allocated to a specific non- LSC funding source. However, it was incorrectly allocated to a different non-LSC funding source. This particular attorneys' fee was for representation supported by a non-LSC funding source and did not affect LSC; however, it reflects that LAET's treatment of attorneys' fees is not in accordance with their policy.

The LAET accounting consultant (formerly LAET Chief Financial Officer) stated that she did not review the actual time entry records to perform the allocations. The attorneys informed her of their time and she made the allocations accordingly. The Director of Finance stated that she was not conversant with the allocation process as she was still new to her position and the organization.

45 CFR § 1609.4(a) states: "Attorneys' fees received by a recipient or an employee of a recipient for representation supported in whole or in part with funds provided by LSC shall be allocated to the fund in which the recipient's LSC grant is recorded in the same proportion that the amount of LSC funds expended bears to the total amount expended by the recipient to support the representation." Properly allocating attorneys' fees allows LSC to be accorded its apportioned share of income, which in turn can be used to provide legal services in accordance with LSC requirements.

The OIG is questioning two of the three attorneys' fees totaling $1,836 that were supported by LSC funds but allocated to other funding sources. The OIG will refer the questioned attorneys' fees to LSC management for review and action.

Recommendation 1: The Executive Director should ensure that LAET personnel are fully trained and implement LSC Regulation CFR 45 § 1609.4(a) requirements related to the allocation of income derived from attorneys' fees.

EMPLOYEE BENEFITS

LAET offers a Vacation Buy-Back program that allows its employees the opportunity to be compensated for up to 37.5 hours of accrued vacation leave annually. Upon compensation, the hours are to be deducted from the employees' accrued vacation leave. According to LAET's written policies, the standard work week is 37.5 hours and the maximum accrued annual leave available for carryover is 300 hours (40 days) per calendar year. Any time accrued over 300 hours will be converted to sick leave on December 31st each year. If an employee elects to participate in the Vacation Buy-Back program, the number of hours for which they are compensated will be deducted from their accrued annual leave. For example, if an employee has 300 hours of accrued annual leave and elects to be compensated for five days (37.5 hours), through the Vacation Buy-Back program, they will be able to carry over 262.5 hours of annual leave to the next year. LAET outsources its payroll administration to a contractor and the Director of Finance is responsible for submitting appropriate payroll information to the payroll contractor in a timely fashion for payroll processes to be performed.

We determined that LAET's written policies and described procedures for the program appear to be in conformance with LSC's *Fundamental Criteria*. However, in practice, internal controls over the program were inadequate and not comparable to the written policies. We selected and reviewed four different samples. Table 1 provides an overview of the participants and samples reviewed.

Table 1 – Summary of Vacation-Buy Back Participants and samples selected

Vacation Buy-Back Group	2017	2017 (terminated)	2016	2016 (terminated)
Number of Participants	34	7	29	5
Sample	5[1]	7	5[2]	5

We noted the following discrepancies.

<u>Vacation Buy-Back Hours not Deducted</u>

We judgmentally selected and reviewed five of LAET's 29 employees who participated in the 2016 Vacation Buy-Back Program. We noted that all five employees did not have their 2016 Vacation Buy-Back hours deducted from their vacation accruals. In following up with LAET, their Payroll contractor stated that the deductions for all participants in 2016 were entirely omitted. According to the Director of Finance, LAET's Payroll contractor is responsible for deducting Vacation Buy-Back hours from employees' accrued vacation leave. She stated they did not notice this issue until February 2019 when the OIG brought it to their attention. However, no adjustments were made to correct this omission.

<u>Vacation Buy-Back Hours not Deducted Timely</u>

We judgmentally selected and reviewed five of LAET's 34 employees who participated in the 2017 Vacation Buy-Back program. All five employees did not have their Vacation Buy-Back hours deducted timely from their accruals. Each employee took a total of 37.5 hours as vacation buy-backs; however, the deductions were performed in November 2018, one year after these employees were compensated for the 2017 Vacation Buy-Back. One[1] of the five employees had been terminated and as such, the deduction was never done.

LAET's Paralegal/HR Assistant stated the Payroll contractor failed to deduct the 2017 Buy-Back hours timely. LAET's Payroll contractor noted that they erroneously did not deduct the hours from applicable employees' accruals. According to the Payroll contractor, manual adjustments were made to deduct the hours in November 2018. The OIG confirmed the deductions by reviewing the time-off register for 2018.

[1] One employee was selected as part of the 2017 test but was also part of the 2017-terminated group.
[2] Two employees were selected as part of the 2016 test but were also part of the 2016-terminated group.

Paid Time-Off Hours Misclassified

Employees who participated in the 2017 Vacation Buy-Back had their buy-back hours converted to sick accruals rather than being deducted from their vacation accruals. We reviewed 11 employees and found that five employees had a total of 150.4 hours converted to sick leave instead of being deducted from their vacation accruals. The grantee identified the error and corrected it in November 2018.

LAET's Payroll contractor stated they erroneously accounted for the 2017 Vacation Buy-Back hours by misclassifying them as conversions to sick accruals rather than deducting them in the January 2018 manual adjustments. These adjustments were done for employees with vacation accruals in excess of LAET's 300-hour limit as of January 2018. The contractor's Payroll Specialist stated manual adjustments were made in November 2018 to convert the Buy-Back hours back to vacation accruals and deduct them properly.

Terminated Employees Overpaid for Vacation Buy-Backs

Ten employees compensated for Vacation Buy-Back hours were later terminated from the grantee; however, their compensated hours were not deducted from their accrued vacation hours.

- Five employees, compensated for the 2016 Vacation Buy-Back, were later terminated from the grantee, but did not have these hours deducted from their vacation accruals. They were paid again for these vacation hours upon termination. They were overpaid an amount of $3,822 for the 2016 Buy-Back; $1,317 of these costs were charged to LSC.

- Five of seven employees terminated during 2018 were compensated for 2017 Vacation Buy-Back hours, however the hours were not deducted from their vacation accruals. These employees were compensated for all or a portion of their remaining vacation accruals upon termination. In total, they were overpaid an amount of $2,740 for the 2017 Buy-Back; $2,102 of these costs were charged to LSC.

LAET's Payroll contractor failed to make the adjustments in time to prevent overpayment as the terminated employees had already been compensated by the time the contractor was aware of these errors. According to LAET's Executive Director, LAET has not yet attempted to recover these funds as they were unaware of the overpayment.

Due to the lack of prudence under the circumstances and significant deviations from LAET's established practices, the total amount of overpayment that was charged to LSC qualifies as an unallowable cost and will be questioned pursuant to 45 CFR §1630.5(b)(3) and (4). As such, $3,419 will be referred to LSC management for review and action.

Part 45 CFR §1630.5(b)(3) and (4) stipulate standards governing the allowability of costs under LSC grants or contracts, specifically (3) whether the recipient acted with prudence under the circumstances, considering its responsibilities to its clients and employees, the public at large, the Corporation, and the Federal government and (4) significant deviations from the recipient's established practices, which may unjustifiably increase the grant or contract costs.

Failure to timely deduct the Vacation Buy-Back hours of those who participate in the program can result in duplicate compensation, especially for employees who are terminated from the organization prior to adjustments being made to correct the omission. Such errors can result in questioned cost proceedings.

LAET's Executive Director should:

Recommendation 2: implement controls that ensure Vacation Buy-Back hours are deducted from applicable employees' vacation accruals timely and properly.

Recommendation 3: deduct the Vacation Buy-Back hours identified by the OIG and any other past Vacation Buy-Back hours that have been taken by existing employees from their accrued vacation time.

Recommendation 4: to the extent consistent with law, attempt to recover funds from terminated employees that were overpaid.

VOLUNTEER ARRANGEMENT

The Director of Finance's father (volunteer) performs voluntary work within the finance department. The grantee provided a confidentiality agreement between LAET and the volunteer. We found the agreement was lacking pertinent information. Additionally, we noted that the volunteer arrangement presented a possible conflict of interest.

Inadequate Volunteer Agreement

The agreement did not explicitly state that the party was a volunteer or describe the work, time commitment or other relevant factors such as training, equipment and work location of the volunteer. LAET's Executive Director agreed that the volunteer agreement could be enhanced to provide more detail.

The LSC Accounting Guide, Section 3-4.2, stipulates the duties and responsibilities of all the grantee's personnel must be detailed in written job descriptions. Job descriptions for accounting personnel must specify, at a minimum, those individuals who, for example, approve invoices for payment, prepare grant and contract reports, maintain accounting records, or prepare management reports.

A detailed written volunteer agreement provides both the organization and the volunteer a clear understanding of the mutual expectations. It also eliminates confusion regarding roles, responsibilities, and expectations between both parties.

Conflict of Interest

The Director of Finance oversees her father, who is serving as a volunteer in LAET's finance department. The OIG believes this arrangement creates potential for a conflict of interest and/or increases the appearance or likelihood of collusion. It also creates a deficiency in segregation of duties. The Director of Finance stated her father performs bank reconciliations of accounts for which she is a debit cardholder[3]. With her father reconciling the bank account for the debit card, there is potential for collusion. LAET's Director of Finance and Executive Director stated that they were not aware of the potential conflict of interest and lack of segregation of duties.

The LSC Accounting Guide, Section 3-4.3, states accounting duties should be segregated to ensure no individual simultaneously has both the physical control and recordkeeping responsibility for any asset, including, but not limited to, cash, client deposits, supplies and property. Duties must be segregated so that no individual can initiate, execute, and record a transaction without a second independent individual being involved in the process.

The LSC Accounting Guide, Appendix VII Accounting Procedures and Internal Control Checklist, states the essence of an effective system of internal control is the segregation of duties in such a way that the persons responsible for the custody of assets and conduct of operations have no part in the keeping of, and do not have access to, the records which establish accounting control over the assets and the operations. Duties of individuals should be so divided as to minimize the possibility of collusion, perpetration of irregularities, and falsification of the accounts. The objective is to provide the maximum safeguards practicable in the circumstances, giving due consideration to the risks involved and the cost of maintaining the controls.

A conflict of interest exists when an employee or family member can benefit personally, directly or indirectly, from his or her relationship with a person in a position with responsibility for the grantee's operations and assets. All employees have an obligation to avoid conflicts of interest or the appearance thereof in order avoid any situation that affects or could potentially affect his or her independent, unbiased judgment in the discharge of his or her duties to the grantee. A lack of segregation of duties could result in an individual being placed in a position of being able to both commit and conceal an irregularity.

LAET Executive Director should:

Recommendation 5: enhance the confidentiality agreement to ensure it contains:

- the terms of the volunteer engagement;
- the duties to be undertaken by the volunteer;

[3] This conflict of interest and lack of segregation of duties is more fully described within the Debit Cards section of the report.

- the requirement that the volunteer abide by the organizations' rules of conduct, policies and regulations;
- the ownership of any copyright or intellectual property created by the volunteer during his or her duties; and,
- the fact that the volunteer will not be receiving any pay or benefits.

Recommendation 6: evaluate the current duties assigned to LAET's volunteer, the Director of Finance's father, and ensure duties assigned to him do not cause a conflict of interest, appearance and likelihood of collusion, or a deficiency in segregation of duties. The Director of Finance's father should not perform bank reconciliations for bank accounts in which the Director of Finance is a debit cardholder.

DISBURSEMENTS

LAET's written policies and procedures regarding disbursements complied with the *Fundamental Criteria*. However, upon interviews and testing, the OIG found that the grantee's practice did not consistently comply with its written policies and procedures or with LSC's *Fundamental Criteria.* The OIG reviewed and tested 157 disbursements totaling $349,023 and noted the following issues: unallowable costs allocated to LSC, lack of segregation of duties, lack of supporting documentation and lack of request for expense forms.

Unallowable Costs Charged to LSC

Three disbursements totaling $2,820 were deemed unallowable per LSC regulations. The disbursements were for trophies or other awards and bar dues paid to a nonprofit bar association not mandated as a condition to practice law and were allocated to LSC. We found that the grantee for the most part was mindful of allocating costs that are deemed unallowable by LSC appropriately, however the costs in question were allocated to LSC. The Director of Finance stated that she is aware of the regulations pertaining to LSC allowable costs and carefully reviews transaction documentation for fund codes to ensure unallowable costs are not charged to LSC.

Expenditures for gifts and awards, are unallowable per LSC regulations and qualify as questioned costs. Furthermore, 45 CFR Part 1630 states that expenditures by a recipient are allowable if the recipient can demonstrate that the cost was reasonable and necessary for the performance of the grant. This unallowable amount will be questioned pursuant to 45 CFR Part 1630. As such, $2,820 will be referred to LSC management for review and action.

LSC *Program Letter 18-3, October 17, 2018* lists common costs that are unallowable by LSC and include flowers, alcohol, holiday cards and gifts for staff, board members, and/or private attorneys such as cakes, shot glasses, or other promotional items or tokens of appreciation such as pens, t-shirts, or coffee mugs.

CFR Part 1630.7 stipulates that LSC funds may not be used to pay membership fees or dues to any private or nonprofit organization, whether on behalf of a recipient or an individual.

Lack of Segregation of Duties

There is a lack of segregation of duties over the master vendor list and other accounting duties. Both the Director of Finance and the Accounting Specialist can add, edit, and delete vendors. The Director of Finance can also approve payments, generate and sign checks. This creates a risk that the Director of Finance is able to perform complete accounting functions without an independent review. We also discovered that the grantee has not reviewed the master vendor list for inactive vendors and removed those vendors accordingly in years.

The Director of Finance stated that although she is authorized to sign checks she does not. She was aware the master vendor list had not been purged and agreed that this was needed.

Without adequate segregation of duties between the accounts payable function and the maintenance of the master vendor list, LAET may not be able to detect unauthorized changes to vendor information, which may lead to fraud, waste, or abuse of the organization's resources.

The Accounting Guide for LSC Recipients Section 3-4(3) states: "Accounting duties should be segregated to ensure that no individual simultaneously has both physical control and record keeping responsibility for any asset, including, but not limited to, cash, client deposits, supplies and property. Duties must be segregated so that no individual can initiate, execute, and record a transaction without a second independent individual being involved in the process."

Lack of Supporting Documentation

We found 57 disbursements totaling $96,791 that did not have adequate supporting documentation. There was no documentation supporting the mileage recorded in monthly travel logs and some disbursements were missing travel expense reports, travel authorization forms, invoices and receipts. The employees use travel logs to document details related to business travel such as the date of the travel, the origin, destination, purpose of the trip and documentation supporting the mileage. We found inconsistencies with the mileage support provided on these travel logs. Some employees recorded odometer readings while others did not record their readings. We also noted one mileage reimbursement that was accompanied by a Google map print out as support for the mileage claimed. The Executive Director stated that the approval process is electronic, and that support provided via email is sometimes not attached to other supporting documentation.

LAET's policies describe the grantee's disbursement filing system. They state that supporting documentation for disbursements should be filed with a photocopy of the actual check disbursed for payment or reimbursement. The policies further state that the travel logs will set out the date of travel, the origin, destination, purpose of the trip and documentation supporting the distances recorded. The grantee's individual request and travel forms further defines the types of support that must be attached.

Appendix II of the LSC Accounting Guide stipulates that each check must be supported by appropriate documentation and provides examples of invoices, contracts, travel reports etc. Additionally, section 3-5.7 stipulates that documentation supporting the reason for each disbursement shall be kept in the files. Lack of adequate supporting documentation, or the improper filing of source documents, could result in unauthorized disbursements or inappropriate approvals.

Lack of Approvals

We found that 74 disbursements totaling $154,399 lacked documentation of appropriate approval. This included invoices, request for expense forms/check request form, monthly travel logs and other travel reimbursement documents.

As mentioned above, the Executive Director stated that approval is not always attached to disbursements because the approval process is electronic.

The LSC Accounting Guide states that the approval of a disbursement by an authorized individual should be documented. Failure to follow a prior approval process may result in employees being reimbursed, or funds being expended, for goods and services that are not reasonable or have not been approved or actually incurred. There is also the risk of purchases being made at unacceptable prices or terms or without the knowledge of appropriate management.

Lack of Use of Request for Expense Forms

During testing, we noted several types of forms serving as a type of request for expense/purchase form. The most relevant, as created by the Director of Finance, was a check request form. We found that a total of 51 disbursements totaling $79,769 did not have an appropriate check request form or request for expense form.

The Director of Finance explained that upon her arrival in July 2018, she implemented a check request form. She is responsible for approving purchases but noted that the check request form is not always used. The grantee has written policies and procedures that state that a request for expense/purchase form must be filled out by the person making a request and submitted to the person in charge of purchasing in each office, who will be so designated by each Managing Attorney.

When the grantee does not adhere to and implemt their own written policies and procedures consistently, expectations regarding the actual practices to which employees are to adhere may be unclear.

The Executive Director should ensure that:

Recommendation 7: LSC funds are not used for unallowable purchases.

Recommendation 8: duties involving maintenance of the master vendor list and vendor payment processing are adequately segregated, and that the master vendor list is regularly purged and maintained to reflect active vendors' current information.

Recommendation 9: documentation supporting miles claimed on monthly travel logs, original invoices, receipts, and all travel related documents are maintained with disbursements. Electronic documentation should be printed out and maintained with the checks.

Recommendation 10: approvals are documented (whether on invoice, check request form, request for expense/purchase forms or travel reimbursement forms) by an authorized individual before invoices are paid to ensure funds are being expended for goods and services:

a. that are reasonable;
b. that have been incurred;
c. that are made at acceptable prices and terms; and
d. with the knowledge of appropriate management.

Recommendation 11: the grantee streamlines and enforces its policies and procedures regarding requests for expense/purchase forms to be completed by the requestor.

DEBIT CARDS

LAET has three debit cards in use but does not have written policies and procedures relating to them. In addition, LAET's internal controls over debit cards were found to be inadequate. We found inadequate practices regarding user agreement forms, segregation of duties, daily limits and controls over the maintenance of receipts and supporting documentation.

No User Agreement Form for Debit Cards

LAET does not require cardholders to sign a user agreement form for use of the grantee's debit card. The Director of Finance stated she would prefer to close the debit cards and use credit cards instead as they are more secure. She agreed that the cardholder should be required to sign a user agreement form to acknowledge the terms of use for grantee's debit cards.

The LSC Accounting Guide, Section 3-5.1, states that the financial authority of supervisory personnel should be clearly defined and evidenced by documentation identifying the authority delegated to supervisory and other personnel to initiate and approve financial transactions. Appendix VII, Section G3, recommends that the grantee consider developing a form that contains credit and debit card policies for employees to review and sign.

Properly controlling the use and documenting the issuance of debit cards through written policies and sound recordkeeping practices reduces the potential for misuse.

Lack of Segregation of Duties in Reconciliations

LAET debit cardholders with accounts payable functions are performing reconciliations of bank statements that include transactions made with their own debit cards.

The Director of Finance stated she and her father, who volunteers at LAET, perform the reconciliations. During prior periods, the former Chief Financial Officer and the former Director of Finance were performing the reconciliations. She stated that the Human Resources Administrator gathers receipts from the cardholders to match them against the bank statements. She also stated that none of the contracted temporary accounting employees were fully trained to perform reconciliations and are performed this way due to understaffing of the accounting department.

The LSC Accounting Guide *Fundamental Criteria*, Section 3-5.2(d), states bank statements shall be reconciled monthly to the general ledger by a person who has no access to cash, who is not a regular check signer, and has no cash bookkeeping duties. The Accounting Guide, Appendix VII, Section J.4, states the duties of the person preparing the bank reconciliation should exclude posting to the books of the account, handling cash and signing checks.

Proper reconciliation procedures increase the likelihood of irregular disbursements and recording errors being discovered on a timely basis. The reconciliation procedure is a fundamental control technique and failure to use it may be interpreted as negligence, especially in an environment where full segregation of duties is not practicable.

Excessive Spending Limit on Debit Cards

The OIG found that each debit cardholder has a daily spending limit of $5,000, which appears excessive for daily use. The Executive Director stated the daily spending limit is necessary so that funds are readily available to make purchases or payments in case of emergencies.

The LSC Accounting Guide, Section 3-6.10, states grantees should limit credit card users and set credit card spending limits as a key practice that can help prevent fraud. Excessive spending limits increase the risk that a large amount of funds will not be recovered in the event theft or fraud occurs. Card limitations are a fraud prevention practice that ensures if a card is stolen, only a certain amount can be charged each day until the theft is reported.

Inadequate Maintenance of Receipts and Supporting Documentation

During interviews, the OIG found that the responsibility of maintaining receipts and performing reconciliations had not been assigned. We also found inadequate controls over the maintenance of receipts and supporting documentation. The OIG judgmentally selected and reviewed 70 debit card transactions totaling $44,747. Table 2 provides a summary of the exceptions out of the 70 debit card transactions we reviewed.

Table 2- Summary of Exceptions over the Maintenance of Receipts and Supporting Documentation

Receipts Not Provided	The grantee did not provide the OIG with receipts or any supporting documentation for six transactions totaling $983.
Inadequate Support	A total of 38 transactions amounting to $16,534 did not have adequate support detailing the purpose for the transaction.
Unknown Initiator of Transactions	Some transactions were made for the cardholder, others for another employee, and others for the office. However, the OIG was unable to determine for whom 28 transactions totaling $9,935 were made.
Request Not Made to Authorized Cardholder	A total of 43 transactions amounting to $35,697 did not have a documented request made to the cardholder for the transaction to occur.

The Executive Director stated she was not aware that all receipts and supporting documentation, such as the purpose for the transaction, should be maintained. She stated that a lot of the support was in email form and she was unaware it should be printed and that hardcopies should be maintained with the debit card statements. She stated that when an individual that is not a cardholder makes a request to a cardholder for the payment or purchase of something, it is usually verbal or in email. She also stated that she did not know that physical documentation should be maintained of such requests and that sometimes the debit card is used for emergency situations. For that reason, a formal request or purpose/support for the transaction is not always made prior to the transaction.

The Director of Finance stated there was never specific staff assigned the responsibility of maintaining the receipts, and that usually the cardholders maintained their own receipts. She stated that due to the accounting department being short-staffed, the Human Resources Administrator will gather the receipts at month-end to begin the reconciliation process.

According to the LSC *Fundamental Criteria* and <u>Accounting Guide</u>, section 3-5.4 states that the receipt of goods and the accuracy of invoices should be verified and documented. Furthermore, it describes an organized method shall be established to accumulate and file all documents relating to a disbursement for future reference. Improper filing of source documents could result in unauthorized disbursements. Without adequate internal verification, cash may be disbursed for goods and services not received, in advance of receipt, or in the wrong amount.

Inadequate Written Policies and Procedures

LAET's Accounting and Internal Control Manual does not include policies or procedures regarding credit or debit cards. The Director of Finance stated she is aware that their Accounting and Internal Control Manual does not have policies or procedures regarding debit cards, and that the grantee is in the process of updating the manual. She stated that her predecessor implemented the use of debit cards and that she would prefer the use of credit cards as they are more secure.

The LSC Accounting Guide, Section 3-4.5, stipulates each recipient must develop a written accounting manual that describes the specific procedures to be followed by the recipient in complying with the *Fundamental Criteria*. Written policies and procedures serve as a method to document the design of controls and adequately communicate them to staff.

The Executive Director should:

Recommendation 12: require each debit cardholder to sign a written user agreement form stipulating that it is the individual's responsibility to use the card for business purposes only and the cardholder will be held accountable for any personal charges made on the card. In addition, the Executive Director should ensure such forms are maintained in the grantee's records.

Recommendation 13: ensure bank reconciliation duties are segregated so that debit cardholders with accounts payable functions are not performing their own reconciliations.

Recommendation 14: reevaluate the $5,000 daily debit card spending limits for each cardholder to ensure the cap is reasonable given the business purpose.

Recommendation 15: ensure that all receipts and supporting documentation are maintained and filed with the debit card statements. Additionally, ensure that requests from non-cardholders are documented and approved by the cardholder and maintained with the debit card statements with supporting documentation.

Recommendation 16: develop written policies and procedures related to debit or credit cards. Specifically, the policies and procedures should detail:

- the issuance of credit or debit cards;
- activation and deactivation of credit or debit cards;
- authorized users;
- number of credit or debit card accounts and/or cardholders;
- approval processes for credit or debit card transactions;
- supporting documentation required for each transaction;
- the cardholder reconciliation processes;
- payment procedures;
- permissible charges;
- handling impermissible charges;

- incurring late fees/finance charges; and
- credit or debit card user agreement form.

CONTRACTING

LAET’s written policies regarding contracting mostly comply with the relevant criteria by including descriptions of the required approval level for contracts of various dollar thresholds. The policies also set dollar thresholds and documentation requirements for contracts of various types. However, the OIG noted some discrepancies in written policies. In addition, while interviewing LAET staff and performing test work to assess LAET’s procedures in practice, the OIG noted exceptions relating to the contract listing and documentation.

Inadequate Written Policies and Procedures

The grantee’s Accounting and Internal Control Manual does not detail contracting procedures for various types of contracts such as consulting, personal service, and sole source, as described in section 3-5.16 of LSC’s Accounting Guide. We also noted that the grantee’s Accounting and Internal Control Manual still refers to LSC PAMM (Property Acquisition and Management Manual) for guidance, which was superseded in 2017 by the new 45 C.F.R. Part 1631.

LAET's Director of Finance and the Executive Director stated the Accounting and Internal Control Manual has not been updated since 2016, but that they are in the process of reviewing and updating it as needed. Additionally, the Executive Director stated that LSC’s Office of Compliance and Enforcement has requested a copy of the grantee’s manual to review.

The LSC Accounting Guide, Section 3-4.5, stipulates each recipient must develop a written accounting manual that describes the specific procedures to be followed by the recipient in complying with the *Fundamental Criteria*. Section 3-5.16 states management should identify contracting procedures for each of the various types of contracts, dollar thresholds, and competition requirements. Contracts that should receive additional oversight include consulting, personal service, and sole-source.

Written policies and procedures serve as a method to document the design of controls and adequately communicate them to staff.

Contract Action and Documentation Not Maintained in a Central File

During interviews, the Director of Finance stated that digital copies of contracts are kept in a folder located on a shared network drive and that the former Director of Finance maintained contract documentation digitally. However, the current Director of Finance was unable to locate the electronic copies on the shared network drive. Furthermore, the Director of Operations, who sometimes handles IT contracts, did not have access to the drive. Hard copies are not maintained in a centralized location but rather various locations depending on who initiated the contract.

The described practice of saving electronic copies of the contracts is not documented in the grantee's Accounting and Internal Control Manual. In addition, maintaining contracts in different office locations is not in accordance with the grantee's written policy.

The Director of Finance stated that contracts are not maintained in a centralized location because they are initiated by different employees in different office locations. She stated some electronic copies were uploaded to the shared network drive by her predecessor; however, she did not know the exact locations. She also did not know who was responsible for uploading electronic copies of the contracts.

LAET's Accounting and Internal Control Manual states "a copy of the bids and the contract along with the documentation is maintained in a central file in the office of the Director of Finance." The LSC Accounting Guide Section 3-5.16, stipulates 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.

Adequate documentation helps to support the initiation of contracts, ensures that grant funds are being used appropriately and that the approved contract has followed all established procedures.

Incomplete Contract Record and Lack of Documentation

The OIG performed contracting test work on 12 judgmentally selected vendors. The judgmental selection included two vendors identified by grantee management as contractors, as well as additional vendors from the check register who, the OIG believes, should have a contract due to their large transaction amounts and multiple payments. These 12 vendors were paid a total of $335,952 during the audit scope period. The OIG requested current contracts or agreements for those vendors and noted the following exceptions:

- The grantee did not obtain or maintain contracts for six of the 12 vendors selected for testing. The services provided by the vendors were lawncare, cleaning, parking and consulting. (The consultant was a retired Chief Financial Officer from LAET.) The amount paid to the vendors during our audit scope totaled $68,291.
- For the remaining six vendors, the grantee maintained contracts; however, the following exceptions were noted:
    - Three of the six contracts, with payments made during the audit scope totaling $181,767, were missing signatures from the vendor;
    - One of the six contracts, with payments made during the audit scope totaling $24,500, was missing signatures from LAET; and,
    - Two of the six contracts on file, with payments during the audit scope totaling $25,099 , did not specify the start date of the contracts. The two contracts are also mentioned above as missing signatures.

- Ten of the 12 contracts were subject to competitive bidding; however, only two contracts had documentation of sole-source justification or bids. Eight contracts, with payments made during the audit scope totaling $127,125, were missing documentation of bids or sole-source justifications.
- Eleven of the 12 contracts reviewed, with payments made during the audit scope totaling $164,693, did not have adequate documented approvals.

The Director of Finance stated most of the contracts were initiated prior to her employment with LAET. She stated her predecessor was responsible for the administration of contracts and she was unsure how the contracts were administered or maintained. The Executive Director stated she was aware that they did not enter into any contracts for services such as lawn care and cleaning services, but also stated that she did not see the need to do so.

The LSC Accounting Guide, Key Elements, Section 3-5.16, stipulates the process used for each contract action should be fully documented and documentation maintained in a central file. Any deviation from the approved contracting process should be fully documented, approved, and maintained in a 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. It also states that the required approval level (including items that need LSC approval) should be established for each contract type and dollar threshold, including when the Board of Directors should be notified and/or give approval.

Contracting is a high-risk area for potential abuse. Without a formal contract, the statement of work and other contract terms cannot be adequately communicated, monitored and enforced, which may hinder management's ability to prevent or detect the risk of fraud, waste or abuse. Failure to maintain proper documentation lessens assurance that the approved contract has followed all established procedures. Improper contracting actions could be taken without proper approval, which could subject the grantee to questioned cost proceedings.

The Executive Director should:

Recommendation 17: ensure the Accounting and Internal Control Manual is updated to include oversight requirements for consulting, personal service, and sole-source contracts, as well as the procedures required for different types of contracts. Additionally, the Executive Director should ensure that the updated Accounting and Internal Control Manual reflects that the LSC PAMM is no longer in effect and was superseded by the 45 CFR Part 1631.

Recommendation 18: ensure that actual practices regarding the maintenance of contracts conform to the policies described in the Accounting and Internal Control Manual as well as the LSC Accounting Guide.

Recommendation 19: establish and maintain a centralized filing system for all contracts that contains all pertinent documents related to the solicitation of bids including receipt and evaluation of bids, sole-source justification, vendor selection, a signed contract or agreement, required approvals, and any agreed upon modifications to a contract or agreement.

Recommendation 20: ensure contract agreements, especially those recurring in nature, are written, signed, dated and maintained for business arrangements. The contracts should fully document the agreed upon terms, price, and payment terms. Contracts should be reviewed periodically to ensure written terms are defined and current.

Recommendation 21: ensure the process for each contract action is fully documented in writing such as sole-source justification and documentation of competition, if competitively bid. Contracts should receive the appropriate approvals as stated in the grantee's Accounting and Internal Control Manual. The approvals should be documented and filed with the contract.

COST ALLOCATION

LAET's written policies and procedures appeared to be compliant with LSC regulations and guidelines. However, during testing and interviews, the OIG found that the grantee is not adhering to the written cost allocation methodology and does not have a adequate cost allocation methodology in use.

Allocations Not Performed

The grantee is not utilizing the cost allocation methodology stipulated in its Accounting and Internal Control Manual and no indirect costs have been allocated since July 2018, when the current Director of Finance was hired. However, the Director of Finance was able to locate allocation percentages prepared by her predecessor for 2016 and 2017. We judgmentally selected 3 transactions, that were indirect in nature, from 2016 and 2017 to determine whether the grantee is performing the cost allocation in direct alignment with the written allocation methodology. The grantee did not allocate any of the indirect costs according to its written cost allocation plan or according to the percentage rates for 2016 and 2017. The indirect costs were allocated directly to grant sources instead of allocating based upon the reviewed percentage rates.

According to the Director of Finance, she and the former Chief Financial Officer were not able to obtain an understanding of how her predecessor was performing allocations. She stated that due to a high staff turnover and a lot of time spent on training, prospective candidate interviews, and catching up on other tasks, they have not been able to implement a new methodology or actually perform the allocations. She is aware this needs to be done and they are hoping to have a plan by the time the Independent Public Accountants arrive in the beginning of the year.

The LSC Accounting Guide states that recipients receiving funds from multiple sources which support work performed under more than one grant, contract, or other funding agreement should allocate common costs among the funds on the basis agreed to by the applicable organization. It also stipulates that in the absence of an approved method, the allocation should be fair, consistent, and in an equitable manner to the individual cost centers, and funds and documented in writing with sufficient detail for the auditor, LSC, OIG, GAO, and others to easily understand, follow, and test the formula.

The grantee did not implement the cost allocation plan outlined in their manual and they fell behind in allocating costs: they had not performed allocations since July 2018. Ultimately, the failure to allocate cost may result in an inability to document compliance with federal requirements and the reliability of management reports can be significantly impaired.

Recommendation 22: The Executive Director should ensure that:

- a cost allocation methodology is formulated, implemented and updated in the grantee's Accounting and Internal Control Manual. This updated cost allocation methodology should be adequately documented with sufficient detail for the auditor, LSC, OIG, GAO, and others to easily understand, follow, and test the formula.
- the Director of Finance performs the allocations that have been outstanding since July 2018. Thereafter, allocations should be performed timely and adhere to 45 CFR §1630.

FIXED ASSETS

The grantee's written policies and procedures regarding fixed assets do not adhere to the *Fundamental Criteria* in LSC's Accounting Guide. The OIG examined documentation and inspected property in the grantee's office and determined that acquisitions, disposals, and maintenance over fixed assets were mostly compliant with the LSC Accounting Guide in practice. However, exceptions were noted in the property records.

Inadequate Written Policies and Procedures

LAET has inadequate written policies and procedures for fixed assets. The written policies do not contain all the elements required by LSC's *Fundamental Criteria.* Specifically, LAET's Accounting and Internal Control Manual does not include the following:

- List of elements required by the *Fundamental Criteria* for property records:
  a) description of the property;
  b) date acquired;
  c) check number used to pay for the item;
  d) original cost;
  e) fair value (if donated);
  f) method of valuation (if donated);
  g) salvage value, if any;
  h) funding source;
  i) estimated life;
  j) depreciation method;

k) identification number; and
l) location.

- Policies and procedures for tracking electronic devices containing sensitive information that are not capitalized.
- Policies and procedures for the disposition of electronic devices containing sensitive information.
- Policies and procedures for the disposition of personal property or real estate purchased with LSC funds.
- Policies and procedures describing the depreciation methods to be used.
- Policies and procedures stating what a request for prior approval should contain.

The Director of Finance was new to the organization when the Accounting and Internal Control Manual was drafted. The Director of Operations stated that the former Director of Finance drafted the manual along with a volunteer. She stated that they mainly referred to other organizations' manuals, and that he likely overlooked these criteria in doing so.

The LSC Accounting Guide, Section 3-4.5, stipulates each recipient must develop a written accounting manual that describes the specific procedures to be followed by the recipient in complying with the *Fundamental Criteria*. Written policies and procedures serve as a method to document the design of controls and adequately communicate them to staff.

Written Policy Does Not Reflect Current Practice

LAET's written policies and procedures regarding the property record system do not reflect the procedures that are implemented in practice. The grantee tracks electronic devices with serial numbers and appears to have adequate procedures for the disposition of such devices. However, the written policies do not reflect these procedures.

The Director of Operations stated he does not recall updates being made to the property record system policies in the Accounting and Internal Control Manual since it was drafted by the former Director of Finance. He is unsure of why the manual was not updated to reflect the current practice.

The LSC Accounting Guide, Section 3-4.5, stipulates each recipient must develop a written accounting manual that describes the specific procedures to be followed by the recipient in complying with the *Fundamental Criteria*.

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. Approved, documented policies and procedures represent grantee management's intentions on the handling of processes and serve as a method of documenting the design of controls, communicating them to staff and ensuring proper controls are followed.

Inadequate IT Equipment Record

LAET does not have an up-to-date IT equipment record. Some items appear on an IT equipment listing formerly used by the grantee, but now retired. The OIG confirmed their existence, but the items were not reconciled to the listing that is currently used. In addition, LAET's IT equipment records do not include an item location field to track electronic devices containing sensitive information. The tracking system for such devices is solely maintained by the grantee's IT contractor.

We reviewed the grantee's internal controls over tracking and safeguarding of electronic devices containing sensitive information. We selected a non-statistical sample of 16 electronic devices to trace from LAET's IT equipment records to their physical location, and a non-statistical sample of 5 items observed in person to trace to the IT equipment records. We found the following exceptions:

- Two laptops were not in the location specified in LAET's IT equipment records however the grantee was able to demonstrate their existence. The OIG confirmed the existence of both laptops; one was physically observed on site, and the other was observed in a photograph that was sent by the grantee to the OIG following fieldwork.
- Three laptops were physically identified but could not be traced to the records to verify completeness.
- One video conference system could not be traced by the serial number on the equipment to the one on the grantee's records. The serial number on the video conference system did not match the serial number in the records.

LAET's Director of Operations was unsure why items on the retired IT equipment listing were not reconciled to the current record; he believed the listing was created by personnel who were no longer with the organization. He stated the item location to track electronic devices containing sensitive information is maintained in the IT contractor's real-time monitoring software. He called the IT Systems Administrator to assist the OIG in tracking the equipment during fieldwork.

According to the Director of Operations, the two laptops that could not be traced from the records to the item location were reassigned to different personnel or re-stationed to a different office. The OIG confirmed existence of both laptops. He stated the three laptops observed in person that could not be traced to the records were purchased after the last physical inventory conducted in March 2018 and in turn, were not reconciled to records during LAET's annual update. He stated the IT Systems Administrator documents electronic software serial numbers as the serial numbers of some devices in the records as he may have not been aware that they differ from the serial number on the physical sticker.

The LSC Accounting Guide, Section 2-2.4, stipulates the recipient should be mindful of items that may contain sensitive information (for example, a computer with client confidential information) with values lower than $5,000 and the need to inventory these items. Best practices include ensuring such devices are tracked and can be easily traced to their physical location.

Inadequate property records may result in difficulty tracking items resulting in the inability to fully account for fixed asset purchases as well as support depreciation amounts and property asset balances. Without an adequate and complete tracking system for all electronic items containing sensitive information, there is no assurance that the grantee is properly safeguarding equipment and the information stored on it..

The Executive Director should ensure that:

Recommendation 23: written policies and procedures for fixed assets include the list of elements required by LSC's *Fundamental Criteria* for property records, procedures for tracking electronic devices containing sensitive information that are not capitalized, procedures for the disposition of electronic devices containing sensitive information, procedures for the disposition of personal property or real estate purchased with LSC funds, procedures describing the depreciation methods to be used, and procedures stating what a request for prior approval should contain.

Recommendation 24: the Accounting and Internal Control Manual reflects the property record system procedures that are currently implemented in practice: including the tagging system for relevant assets, tracking of IT equipment, and disposition procedures for electronic devices containing sensitive information.

Recommendation 25: all relevant devices are reconciled to the current IT equipment record.

Recommendation 26: electronic devices containing sensitive information are easily traceable with a location for each relevant item included in the IT equipment record.

GENERAL LEDGER AND FINANCIAL CONTROLS

LAET's written policies and procedures regarding the general ledger and financial controls are mostly comparable to the criteria in LSC's Accounting Guide. However, the OIG found inadequate practices over bank signatories, segregation of duties, outstanding checks and bank reconciliations. Furthermore, the OIG also noted a discrepancy pertaining to regulations on the purchase amount requiring LSC approval.

Terminated Employees Authorized as Bank Signatories

We noted that six terminated employees are still included as authorized check signers for one of LAET's bank accounts. According to the Director of Finance, the Executive Director is in the process of getting new authorizations signed, for this reason the terminated employees are still listed. The Executive Director stated she is working to resolve the issue, and that LAET will likely need a Board resolution.

Both the grantee's Accounting and Internal Control Manual and The LSC Accounting Guide *Fundamental Criteria*, Section 3-5.2, stipulate that authorized check signers who are no longer with the program should have their authorization to sign checks canceled promptly on the bank records. Failure to cancel terminated employees' authorization to sign checks may result in unauthorized transactions, fraudulent transactions and embezzlement of funds.

Inadequate Segregation of Duties

Segregation of duties in the accounting system appeared adequate in most areas, except for check writing and cash disbursements. In a review of the user access rights, the OIG noted that all employees who have access to the system have permission rights to add, edit and process these activities in the accounting system.

According to the Director of Finance, these user permission rights were implemented prior to her employment with LAET. She acknowledged the fact that there is a lack of segregation of duties and stated she plans to coordinate with the IT Systems Administrator to edit the user permission rights to segregate duties involving accounting and authority.

LSC's Accounting Guide, Section 3-4 (3), states accounting duties should be segregated to ensure that no individual simultaneously has both the physical control and the recordkeeping responsibility for any asset, including, but not limited to cash, client deposits, supplies and property. Duties must be segregated so that no individual can initiate, execute, and record a transaction without a second independent individual being involved in the process.

Inadequate segregation of duties can result in failure to prevent and detect error, fraud, theft and collusion.

Outstanding Checks

We found that two out of thirteen outstanding checks listed in LAET's February 2017 reconciliation were not resolved timely. These checks were still outstanding per the February 2018 statement. LAET's Director of Finance stated that due to understaffing, current staff may have been overwhelmed with their duties, which likely caused them to overlook this.

LAET's Accounting and Internal Control Manual states LAET voids outstanding checks after six months, and the Director of Finance maintains a copy of all invoices. Not monitoring and resolving outstanding checks timely may result in undetected fraudulent signatures or endorsements, alterations of checks, improper use of voided checks, and improper recording of bank transfers.

Inadequate Controls over Bank Reconciliations

We found that internal controls over LAET's bank reconciliation process were not in accordance with LSC's *Fundamental Criteria*. We noted inadequate segregation of duties and lack of evidence documenting performance and review of bank reconciliations. The OIG tested 12 judgmentally selected bank reconciliations and found the following exceptions:

- One employee who had been reconciling the accounts was also initiating electronic transactions, performing bookkeeping duties, and was a regular check signer. This employee performed seven of the reconciliations the OIG tested.
- Eleven of the 12 bank reconciliations had multiple exceptions, such as missing preparer's documentation, not prepared timely, no evidence of review, not reviewed timely or there was no evidence of reconciliation to the General Ledger. Table 3 provides an overview of these 11 reconciliations.

Table 3: Overview of Bank Reconciliation Exceptions

Sample #	Not Signed or Dated by Preparer	Not Performed Timely	No Evidence of Review	Not Reviewed Timely	Date of Review Not Documented	No Evidence of Reconciliation to the General Ledger
1				X		
2		X		X		
3						
4			X			
5		X			X	
6		X	X			
7		X	X			
8	X	X		X		X
9	X	X		X		
10	X	X	X			
11	X	X	X			X
12	X	X		X		
Totals	**5**	**9**	**5**	**5**	**1**	**2**

- Five of the 12 reconciliations were missing documentation of who prepared the reconciliation; and, all five were also missing the date of preparation.
- Nine of the 12 reconciliations were not performed timely. Four of which were performed while or after the OIG was on-site and five were performed more than 31 days after the bank statement date.
- Five of the 12 reconciliations were not reviewed.
- Five of the 12 reconciliations were not reviewed timely
- One of the 12 reconciliations that was reviewed was missing the date of review

- Two of the 12 reconciliations did not have evidence of reconciliation to the general ledger.

LAET’s Director of Finance stated it was difficult to establish proper segregation of duties over bank reconciliation due to understaffing. According to the Director of Finance, LAET’s former Director of Finance did not perform the reconciliations timely as he was overwhelmed with his duties. She stated LAET had been eight months behind on bank reconciliations when she joined the organization, and that it has been a challenge to get them up to date with continued staffing shortages.

LSC’s Accounting Guide, Section 3-5.2(d), stipulates bank statements shall be reconciled monthly to the general ledger by a person who has no access to cash, who is not a regular check signer, and has no cash bookkeeping duties; and the reconciliation shall be reviewed and approved by a responsible individual. Such review shall be appropriately documented by signature and date.

Proper reconciliation procedures substantially increase the likelihood of discovering irregular disbursements and recording errors on a timely basis. Documented approvals provide segregation of duties in the recordkeeping and authorization processes that protect against misappropriation and provide a check against errors.

Inadequate Written Policies and Procedures

LAET’s Accounting and Internal Control Manual states "expenditure of LSC funds in excess of $10,000 must be approved by LSC." This amount does not reflect the current LSC approval threshold which was revised to $25,000. In addition, the manual states the Director of Finance performs bank reconciliations. Since the Director of Finance also has a debit card and initiates EFTs, this appears to create a lack of segregation of duties. However, we learned that in practice, the bank reconciliations are not performed by the Director of Finance. LAET’s Director of Finance and Executive Director stated the Accounting and Internal Control Manual has not been updated since 2016, but they are in the process of reviewing and updating it.

45 CFR Part 1630, Section 1630.6(b), stipulates that without LSC's prior written approval, a recipient may not expend $25,000 or more of LSC funds on (i) a single purchase or single lease of personal property, (ii) a single contract for services, (iii) a single combined purchase or lease of personal property and contract for services and (iv) capital improvements. Section 3-4(5) of the LSC Accounting Guide states each recipient must develop a written accounting manual that describes the specific procedures to be followed by the recipient in complying with the *Fundamental Criteria*.

Written policies and procedures serve as a method of documenting the design of controls and communicating them to the staff.

LAET's Executive Director should ensure:

Recommendation 27: authorization to sign checks is promptly canceled when an employee leaves the organization.

Recommendation 28: duties are segregated within the organization's accounting system so that no individual can initiate, execute, and record a transaction without a second independent person being involved in the process.

Recommendation 29: grantee personnel adhere to the grantee's written policy of voiding outstanding checks after six months.

Recommendation 30: bank statements are reconciled monthly to the general ledger by an employee who has no access to cash, is not a regular check signer, and has no cash bookkeeping duties; in addition, a single employee should not have the authority to initiate electronic transactions and perform bookkeeping duties.

Recommendation 31: the bank reconciliation process is performed timely, reconciled to the general ledger, and documented on the reconciliation sheet by signature and date.

Recommendation 32: LAET's Accounting and Internal Control Manual is updated to reflect the current $25,000 threshold for expenditures requiring prior LSC approval. Furthermore, the Accounting and Internal Control Manual should be updated to reflect a clear segregation of duties over bank reconciliations.

GRANTEE MANAGEMENT COMMENTS

In their response, LAET management reported that they had addressed or were in the process of addressing many of the 32 recommendations contained in the report. They agreed with 29 of the recommendations and partially agreed with one recommendation. For two recommendations, LAET management held their response pending consultation with legal counsel. Grantee management stated the following:

- LAET concurred in part with the recommendation relating to attorneys' fees. They indicated that their personnel have been trained and are implementing 45 CFR § 1609.4 requirements for allocating attorneys' fees. They stated that the entries in question were coding errors.

- LAET concurred with the recommendation to implement controls that ensure Vacation Buy-Back hours are deducted from applicable employees' vacation accruals timely and properly. They stated that the related procedure has already been added to the payroll section of the Accounting and Internal Control Manual and that the procedure is being followed. LAET management stated that the matter noted in the the report was due to miscommunication between the former Director of Finance and their contract payroll provider.

- LAET stated that before fully responding to the two recommendations related to deducting past Vacation-Buy Back hours and recovering funds from terminated employees that were overpaid, they will retain and consult with legal qualified outside counsel to determine if recommended action is permitted by federal and state laws.

- LAET concurred with the recommendation to enhance their confidentiality agreement and stated that their Volunteer Agreement has been updated to include items mentioned in the recommendation. A copy of the revised Volunteer Agreement was enclosed.

- LAET management stated that they confirmed that LAET's volunteer has never reconciled any bank statements for which the Director of Finance is a cardholder. They listed the volunteer's duties and stated that none of them have caused a conflict of interest, the appearance or likelihood of collusion, or a deficiency in segregation of duties. They also stated that going forward the duties will be listed in the new Volunteer Agreement that the volunteer will be asked to sign. They concurred with the recommendation.

- LAET concurred with the recommendation to ensure that LSC funds are not used for unallowable purposes and acknowledged that the errors in allocating expenses occurred during the transition of Finance Directors. They stated that corrections have been made through journal entries which moved expenses from Fund Code 001 for LSC to Fund Code 004 for unrestricted funds.

- LAET indicated concurrence and stated that they are updating the vendor list by marking as "inactive" those vendors that have not had activity since 2015.

- LAET concurred with the recommendation related to maintaining supporting documentation for travel related disbursements and stated that all documentation is maintained with disbursements.

- LAET indicated concurrence and stated that all approvals are being documented with disbursements.

- LAET concurred with the recommendation to streamline and enforce policies and procedures regarding expense/purchase form completion. Management stated that they have reviewed and updated their Accounting and Internal Control Manual (subject to Board approval) and are consistently enforcing policies requiring employees to complete an expense/purchase form, attaching all supporting documentation before the purchase is authorized or payment made.

- LAET indicated concurrence and stated that they require debit cardholders to sign a Cardholder Agreement. The Cardholder Agreement was enclosed with their response.

- LAET concurred with the recommendation to ensure that bank reconciliation duties are appropriately segregated and stated that their former Chief Financial Officer is working as an independent contractor for LAET and is responsible for reconciling the bank statements associated with the debit cards.

- LAET indicated concurrence and stated that the Executive Director has evaluated the $5,000 debit card daily spending limit and found it to be reasonable given the business purposes for which the cards are used and because only the Director of Finance and Executive Director are cardholders.

- LAET concurred with the recommendation related to maintenance documentation, including that of approval, for debit card transactions. Grantee management stated that all documentation is being maintained with debit card statements, and they have developed and will be using a Credit/Debit Card Pre-Approval Request Form that will be maintained with the debit card statements. LAET included a copy of the form with their response.

- LAET concurred with the recommendation to develop written policies and procedures related to debit or credit cards. Grantee management stated that they have added a section to their Accounting and Internal Control Manual with policies and procedures related to debit cards. They have submitted it to to an LSC official for review and comment. They stated that the policies and procedures are also being made part of the Cardholder Agreement that each cardholder must sign and enclosed a copy with their response.

- LAET indicated concurrence and stated that their Accounting and Internal Control Manual has been updated with the referenced issues in the recommendation related to contracts; and the manual has been approved by an LSC official and has been sent to another LSC Official for further review and comment.

- LAET stated that contracts are now being stored in a central location on LAET's internal drive, and hard copies are maintained in the offices of the appropriate individuals. They concurred with the related recommendation.

- LAET indicated concurrence and stated that they will establish and maintain an electronic centralized filing system for all new contracts entered into after the date of their response and will store in that centralized filing system all pertinent documents related to the solicitation of bids including receipt and evaluation of bids, sole-source justification, vendor selection, a signed contract or agreement, required approvals, and any agreed upon modifications to a contract or agreement. With regard to the existing contracts and agreements, LAET stated that they have begun the process of gathering and organizing the documentation for storage electronically and in the Director of Finance's office or the office(s) of other designated managers as appropriate.

- LAET concurred with and stated that they have implemented the recommendation relating to ensuring contract agreements, especially those recurring in nature, are written, signed, dated, maintained and reviewed periodically.

- LAET concurred with the recommendation to ensure that the process for each contract action is fully documented in writing such as sole-source justification and documentation of competition; and that approvals should be documented and filed with the contract. They stated that they have updated their Accounting and Internal Control Manual and sent to an LSC official for comment and approval prior to submission to LAET's Board of Directors.

- LAET indicated concurrence and stated that the cost allocation methodology has been updated in their Accounting and Internal Control Manual and submitted to an LSC official for review and comment. They also stated that all the allocations have been made since July 2018 and allocations are currently being done on a monthly basis.

- LAET concurred with the recommendation related to enhancement of written policies and procedures for fixed assets. Grantee management stated that they have updated their Accounting and Internal Control Manual to address the referenced issues and submitted the updates to an LSC Official for review and comment.

- LAET stated that they have consulted with their outsourced IT provider and are in the process of reconciling all relevant devices to the current IT equipment record. They concurred with the recommendation.

- LAET indicated concurrence and stated that their IT record indicates the location of each workstation and to whom it belongs. Additionally each computer is joined to the domain and requires password authentication in order to log into the domain. Data is backed up and replicated across three servers.

- LAET indicated concurrence and stated that authorized check signers who are no longer with the organization will have their authorization cancelled.

- LAET stated that they ensured the proper segregation of duties when they hired an Accounting Assistant in February 2019 and concurred with the related recommendation.

- LAET indicated concurrence and stated that they made adjustments in the 2018 Audit to account for checks that remained outstanding during and/or as the result of the transition in Finance Directors during 2018.

- LAET indicated concurrence and stated that bank statements are being reconciled by their former Chief Financial Officer, ·who retired from LAET in 2011 and is now working for LAET as an independent contractor. They stated that the contractor does not have access to cash, is not a regular check signer, and does not have bookkeeping duties. They also stated that they are evaluating the feasibility of hiring an employee to perform bank reconciliations on a permanent basis.

- LAET stated that the transition in LAET's Finance Department created a backlog of work that is being brought current. They added an Accounting Assistant and an independent contractor to their Finance Department last year. Grantee management concurred with the recommendation and stated thatthese efforts, among others, should allow them to perform reconciliations in a timely fashion.

- LAET indicated concurrence and stated that the Accounting and Internal Control Manual has been updated to address the recommendation relating to the $25,000 threshold for expenditures requiring prior LSC approval and segregation of duties over bank reconciliations. They noted that they submitted the updated Accounting and Internal Control Manual to an LSC official for review and comment.

OIG EVALUATION OF GRANTEE MANAGEMENT COMMENTS

The OIG considers the proposed actions for Recommendations 1, 5, 7, 9, 13, 14, 15, 18, 20, 28, 30 and 31 as fully responsive and closed.

The grantee responded to Recommendation 1 by stating that LAET personnel have been trained in and are implementing 45 CFR. § 1609.4 requirements by booking attorneys' fees correctly using case information from Legal Server, which is responsive to the recommendation. They also stated that the entries in question involved coding errors.[4] However, the OIG questioned costs totaling $1,836 of attorneys' fees that were supported by LSC funds but allocated to other funding sources. This amount will be referred to LSC management for review and action.

The grantee responded to Recommendation 5 by updating their Volunteer Agreement to include items listed in the recommendation and provided the revised Volunteer Agreement.

The grantee responded to Recommendation 7 by stating that errors in allocating expenses occurred during a transition period, while the Director of Finance was learning her new role.They also stated that corrections have been made through journal entries which moved expenses from fund code 001/or LSC to fund code 004 AOC and/or unrestricted funds and systems are in place to minimize the risk of future errors. The OIG questioned costs totaling $2,820 of unallowable expenses pursuant to 45 CFR Part 1630. This amount will be referred to LSC management for review and action.

The grantee responded to Recommendation 9 by stating that they concurred with the recommendation related to maintaining supporting documentation for travel related disbursements and stated that all documentation is maintained with disbursements.

The grantee responded to Recommendation 13 by stating that their former Chief Financial Officer is an independent contractor and responsible for reconciling the bank statement associated with the debit cards. This eliminates the situation of a debit cardholder performing their own reconciliation.

The grantee responded to Recommendation 14 by indicating that the Executive Director had reevaluated the $5,000 daily debit card spending limit and found it to be reasonable given the business purpose of the cards and that only the Director of Finace and Executive Director are cardholders.

The grantee responded to Recommendation 15 by indicating that all documentation is being maintained with debit card statements. They have developed and will be using a

[4] We determined that the grantee's response satisfied the recommendation even though they partially concurred with it.

Credit/Debit Card Pre-Approval Request Form that will be maintained with the debit card statements. They provided a copy of the form.

The grantee responded to Recommendation 18 by stating that contracts are now being stored in a central location on LAET's internal drive, and hard copies are maintained in the offices of the appropriate individuals.

The grantee responded to Recommendation 20 by stating that they have implemented the recommendation relating to ensuring contract agreements, especially those recurring in nature, are written, signed, dated, maintained and reviewed; and that the process will be followed going forward.

The grantee responded to Recommendation 28 by stating that they ensured proper segregation of duties within the organization's accounting system by hiring an Accounting Assistant for the Finance Department in February 2019.

The grantee responded to Recommendation 30 stating that their bank statements are being reconciled by an independent contractor who does not have access to cash, is not a regular check signer, and does not have bookkeeping duties.

The grantee responded to recommendation 31 stating that they added an Accounting Assistant and an independent contractor to its Finance Department last year. These efforts should allow them to perform reconciliations in a timely fashion.

The OIG considers the proposed actions to Recommendations 2, 3, 4, 6, 11, 12, 16, 17, 19, 21, 22, 23, 24, 25, 26, 27, 29 and 32 as responsive. The proposed actions to address the issues and update the the policies and procedures should satisfy the issues identified in the report. However, these recommendations will remain open until the OIG is notified in writing that the proposed actions have been completed and the supporting documentation is provided.

Recommendation 2, 11, 16, 17, 21, 23, 24 and 32 will remain open until the OIG is provided with the updated and Board approved Accounting and Internal Control Manual documenting procedures related to deduction of Vacation Buy-Back hours, debit cards, contracts, fixed assets, expenditures requiring LSC approval and segregation of duties over bank reconciliations.

Recommendation 3 and 4 will remain open until the OIG is provided with supporting documentation of the outcome of LAET's consultation with legal counsel.

The OIG questioned costs totaling $3,419 of overpayments to employees that were charged to LSC. This amount will be referred to LSC management for review and action.

Recommendation 6 will remain open until OIG is provided with a copy of the signed Vounteer Agreement.

Recommendation 12 will remain open until OIG is provided with a copy of the signed Cardholder Agreements.

Recommendation 19 will remain open until the OIG is provided with written notice that the electronic centralized filing system has been established.

Recommendation 22 will remain open until the OIG is provided with supporting documentation of the updated cost allocation methodology.

Recommendation 25 will remain open until the OIG is provided with written notice and documentation demonstrating that the reconciliation is complete.

Recommendation 26 will remain open until the OIG is provided with evidence that electronic devices containing sensitive information are included in the IT equipment record.

Recommendation 27 will remain open until the OIG is provided with a copy of the bank documentation reflecting the current check signers.

Recommendation 29 will remain open until the OIG is provided with supporting documentation reflecting adjustments of the outstanding checks.

The OIG considers the proposed actions for Recommendation 8 and 10 as partially responsive.

The grantee responded to Recommendation 8 by stating that the vendor list is being updated. However, they did not address how they will ensure that duties involving maintenance of the master vendor list and vendor payment processing are adequately segregated. This recommendation will remain open until OIG is informed in writing that updating of the vendor list is complete and supporting documentation is provided demonstrating how the grantee will ensure duties involving maintenance of the master vendor list and vendor payment processing are adequately segregated.

The grantee responded to Recommendation 10 by stating that all approvals are being documented with disbursements; however, the recommendation is to ensure that approvals are documented before invoices are paid. This recommendation will remain open until the OIG is provided with support demonstrating how the grantee will ensure approvals are documented before invoices are paid.

APPENDIX I

SCOPE AND METHODOLOGY

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

- Disbursements;
- Debit Cards;
- Contracting;
- Cost Allocation;
- Derivative income;
- General Ledger and Financial Controls;
- Internal Management Reporting and Budgeting;
- Fixed Assets;
- Employee Benefits; and
- Payroll.

To obtain an understanding of the internal controls over areas listed above, we reviewed grantee policy and procedures, including manuals, guidelines, memoranda and directives, setting forth current grantee 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 LSC Accounting Guide.

We assessed the reliability of computer-generated data the grantee provided by reviewing available supporting documentation for the entries selected for review, conducting interviews and making physical observations to determine data consistency and reasonableness. We determined that the computer processed data is reliable and sufficient for the purposes of this report in the areas reviewed.

To test for the appropriateness of expenditures and the existence of adequate supporting documentation, disbursements from a judgmentally selected sample of vendor files were reviewed. The sample consisted of 157 disbursement transactions totaling $349,023. The sample represented approximately 20 percent of the $1,728,429 disbursed for expenses other than payroll and debit cards during the period January 1, 2016 through October 31, 2018. We reviewed the check register and compared the information to source documents as well as the general ledger. We found that all 157 transactions we selected for our sample were traceable to the general ledger.

In addition to disbursements, we sampled nine debit card statements consisting of 70 transactions totaling $44,747. We assessed the appropriateness of the expenditures and the existence of approvals and adequate supporting documentation.

To evaluate and test internal controls over the employee benefits, payroll, contracting, internal management reporting and budgeting, general ledger and financial controls, as well as derivative income, we interviewed appropriate program personnel, examined related policies and procedures as applicable and selected specific transactions to review for adequacy.

To evaluate the adequacy of the cost allocation process, we discussed the process with grantee management and made a physical observation of the information in the grantee's accounting system to confirm if costs were allocated in conformity with the documented allocation process.

Controls over purchase, record, inventory, and disposal of property and equipment were reviewed by examining current grantee practices in comparison with LSC regulations and policies outlined in the LSC Accounting Guide. The samples selected for the internal control review were derived by non-statistical sampling techniques. Our results cannot be projected to the universe and are not intended to make inferences about the population from which our samples derived. The on-site fieldwork was conducted from January 23, 2019 through January 31, 2019.

Our work was conducted at the grantee's administrative office in Chattanooga, TN and at LSC headquarters in Washington, DC. Documents reviewed pertained to the period January 1, 2016 through October 31, 2018. The audit was conducted in accordance to 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 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.

LAET
Legal Aid Of East Tennessee
JUSTICE FOR ALL

LEGAL AID OF EAST TENNESSEE

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September 23, 2019

Ms. Roxanne Caruso
Assistant Inspector General for Audit
Office of the Inspector General
Legal Services Corporation
3333 K Street, NW, 3rd Floor
Washington, DC 20007-3558
rcaruso@oig.lsc.gov

RE: Legal Aid of East Tennessee, RNO 643020

Dear Ms. Caruso:

Below are Legal Aid of East Tennessee's (LAET) responses to the Office of Inspector General (OIG) Draft Report on Selected Internal Controls, Report No. AU XX-XX, which initially was sent to me on August 10, 2019, with revised versions sent on September 5 and September 10, 2019. We are responding to the September 10, 2019 version of the report.

The OIG Team, led by Grace Nyakoe, conducted an on-site audit from Wednesday, January 23, 2019, through Thursday, January 31, 2019. The relevant audit period was for the audit period of January 1, 2016, through October 31, 2018. During the visit, the Audit Team, including several trainees, was courteous and respectful.

As the Audit Team and others were aware, the visit occurred during a period of significant transition in LAET's Finance Department. More specifically, LAET's former Finance Director left unexpectedly in April of 2018, well before the film's annual audit had been completed and before a replacement could be hired and trained. LAET promptly retained an Interim Finance Director and, by July of 2018, our new permanent Finance Director Melissa Brumfield was on board and working to complete the annual audit and otherwise transition into her new role.

As you can see from our responses, LAET has addressed or is in the process of addressing many of the 32 recommended actions, including making updates to our Accounting and Internal Control Manual (LAET Accounting Manual), which was last updated in 2016. This process was underway when the OIG Audit Team arrived, and we are happy to report that the revised LAET Accounting Manual is almost complete and likely will be presented to the Board of Directors for review and adoption at the November 21 Board meeting, if not before. In addition, LAET plans to submit the revised manual to Kevin Moran, Fiscal Compliance Analyst, LSC's Office of Compliance and Enforcement, for his review and comment prior to presentation to LAET's Board of Directors.

Recommendation 1: The Executive Director should ensure that LAET personnel are fully trained and implement LSC Regulations CFR 45 1609.4 (a) requirements related to the allocation of income derived from attorneys' fees.

LAET concurs in part with the above recommendation. LAET personnel have been trained in and are implementing 45 C.F.R. § 1609.4 requirements by booking attorneys' fees correctly using case information from Legal Server. The entries in question involved coding errors.

Recommendation 2: The Executive Director should implement controls that ensure Vacation Buy-Back hours are deducted from applicable employees' vacation accruals timely and properly.

LAET concurs with the above recommendation. This procedure has already been added to the payroll section of the Accounting and Internal Controls Manual and is being followed. The reference in the OIG Audit Report to vacation buy-back hours not being deducted from applicable employees' vacation accruals was a matter of miscommunication between the former Director of Finance and LBMC, Inc., LAET's contract payroll provider.

Recommendation 3: The Executive Director should deduct the Vacation Buy-Back hours identified by the OIG and any other past Vacation Buy-Back hours that have been taken by existing employees from their accrued vacation time.

Before fully responding to this recommendation, LAET must retain and consult with qualified outside counsel to determine if the recommended action is permitted under federal and state laws, other applicable rules and recommendations, and various contract restrictions that may be applicable including those in the 2019 Collective Bargaining Agreement that applies in four of LAET's 26 counties.

Recommendation 4: The Executive Director should, to the extent consistent with law, attempt to recover funds from terminated employees that were overpaid.

LAET will retain and consult with qualified outside counsel to determine if the recommended action is permitted under federal and state laws, other applicable rules and recommendations, and various contract restrictions that may be applicable including those in the 2019 Collective Bargaining Agreement that applies in four of LAET's 26 counties.

Recommendation 5: The Executive Director should enhance the confidentiality agreement to ensure it contains:

- the terms of the volunteer agreement.
- the duties to be undertaken by the volunteer;
- the requirement that the volunteer abide by the organizations' rules of conduct, policies and regulations;
- the ownership of any copyright or intellectual property created by the volunteer during his or her duties; and,
- the fact that the volunteer will not be receiving any pay or benefits.

LAET concurs with the above recommendation and has updated its Volunteer Agreement to include the items mentioned in the list above, among others. A copy of the revised Volunteer Agreement is enclosed.

Recommendation 6: The Executive Director should evaluate the current duties assigned to LAET's volunteer, the Director of Finance's father, and ensure duties assigned to him do not cause a conflict of interest, appearance and likelihood of collusion, or a deficiency in segregation of duties. The Director of Finance's father should not perform bank reconciliations for bank accounts in which the Director of Finance is a debit cardholder.

LAET concurs with the above recommendation, and the Executive Director has confirmed that the Director of Finance's father, volunteer Russell Brumfield, has never reconciled any bank statement for which Ms. Brumfield is a cardholder (Regions Bank Account 4591). Because of the backlog of work created after the unexpected departure of the former Finance Director and the added work created by two OIG visits and the annual audit, Mr. Brumfield reconciled only a few statements in the Fall of 2018, including the Unrestricted and Trust bank statements. Mr. Brumfield has not reconciled any bank statements since the fall of 2018 and will not do so in the future.

Mr. Brumfield's past volunteer responsibilities have included the following tasks, none of which created a conflict of interest, the appearance or likelihood of collusion, or a deficiency in segregation of duties.

- *Gathering back-up documentation for some of the bank statements.*
- *Summarizing travel information into a pivot table at the end of each month to assist with the task of reimbursing employee travel expenses.*
- *Providing invaluable and critical support during union negotiations by developing a comprehensive set of spreadsheets involving salary scales and budget comparisons.*
- *Providing technical consultation/process improvement recommendations as needed by the Finance Department.*

Mr. Brumfield's duties going forward will be listed in the new Volunteer Agreement that Mr. Brumfield will be asked to sign. A copy of the revised Volunteer Agreement is enclosed.

Recommendation 7: The Executive Director should ensure that LSC funds are not used for unallowable purposes.

LAET concurs with the above recommendation. LAET acknowledges that errors in allocating expenses occurred during the transition that resulted when the former Finance Director unexpectedly left LAET in April of 2018 during the annual audit. An Interim Finance Director was retained until a new Finance Director could be hired. Melissa Brumfield became LAET's Director of Finance in July of 2018 during the audit. The audit was followed very shortly by two OIG visits and while Ms. Brumfield was learning her new role as the head of finance for an LSC grantee. Corrections have been made through journal entries which moved expenses from Fund code 001 for LSC to fund code 004 AOC and/or unrestricted funds and systems are in place to minimize the risk of future errors.

<u>Recommendation 8:</u> The Executive Director should ensure that duties involving maintenance of the master vendor list and vendor payment processing are adequately segregated, and that the master vendor list is regularly purged and maintained to reflect active vendors' current information.

LAET concurs with the above recommendation. The Finance Department is updating the vendor list by marking as, "Inactive" those vendors that have not had any activity since 2015. LAET's accounting software, Abila MIP, does not allow users to permanently delete vendors in the system.

<u>Recommendation 9:</u> The Executive Director should ensure that documentation supporting miles claimed on monthly travel logs, original invoices, receipts, and all travel related documents are maintained with disbursements. Electronic documentation should be printed out and maintained with the checks.

LAET concurs with the above recommendation. All documentation is being maintained with disbursements.

<u>Recommendation 10:</u> The Executive Director should ensure that approvals are documented (whether on invoice, check request form, request for expense/purchase forms or travel reimbursement forms) by an authorized individual before invoices are paid to ensure fund are being expended for goods and services.

a. that are reasonable.
b. that have been incurred.
c. that are made at acceptable prices and terms; and
d. with the knowledge of appropriate management.

LAET concurs with the above recommendation. All approvals are being documented with disbursements.

<u>Recommendation 11:</u> The Executive Director should ensure that the grantee streamlines and enforces its policies and procedures regarding requests for expense/purchase forms to be completed by the requestor.

LAET concurs with the above recommendation. LAET has reviewed and updated its Accounting and Internal Controls Manual (subject to Board approval) and is consistently enforcing its policies requiring employees to complete an Expense/Purchase Form, attaching all supporting documentation before the purchase is authorized or payment made. (NOTE: some purchases are exempt from this process but subject to other policies, e.g., the purchase of standard office supplies.) A copy of the Expense/Purchase Request Form is enclosed.

Recommendation 12: The Executive Director should require each debit cardholder to sign a written user agreement form stipulating that it is the individual's responsibility to use the card for business purposes only and the cardholder will be held accountable for any personal charges made on the card. In addition, the Executive Director should ensure such forms are maintained in the grantee's records.

LAET concurs with the above recommendation and is requiring debit cardholders to sign the enclosed Cardholder Agreement.

Recommendation 13: The Executive Director should ensure that bank reconciliation duties are segregated so that debit cardholders with accounts payable functions are not performing their own reconciliations.

LAET concurs with the above recommendation. LAET'S former Chief Financial Officer who retired in 2011 is working as an independent contractor for LAET and has been reconciling the bank statements associated with the debit cards (Regions Operating Account 4591) since July 2018. The Regions account ending in 4591 is the only account with debit cards attached. LAET currently does not have any credit cards.

Recommendation 14: The Executive Director should reevaluate the $5,000 daily debit card spending limits for each cardholder to ensure the cap is reasonable given the business purpose.

LAET concurs with this recommendation. The Executive Director has evaluated the $5,000 debit card daily spending limit and found it to be reasonable given the business purposes for which the cards are used and because only the Director of Finance and Executive Director are cardholders.

Recommendation 15: The Executive Director should ensure that all receipts and supporting documentation are maintained and filed with the debit card statements. Additionally, the Executive Director should ensure that requests from non-cardholders are documented and approved by the cardholder and maintained with the debit card statements with supporting documentation.

LAET concurs with the above recommendation. All documentation is being maintained with debit card statements, and LAET has developed and will be using a Credit/Debit Card Pre-Approval Request Form that will be maintained with the debit card statements. A copy of the form is enclosed for reference.

Recommendation 16: The Executive Director should develop written policies and procedures related to debit or credit cards. Specifically, the policies and procedures should detail:

- the issuance of credit or debit cards;
- activation and deactivation of credit or debit cards;
- authorized users;
- number of credit or debit card accounts and/or cardholders;
- approval processes for credit or debit card transactions;
- supporting documentation required for each transaction;
- the cardholder reconciliation processes;

- payment procedures;
- permissible charges;
- handling impermissible charges;
- incurring late fees/finance charges; and
- credit or debit card user agreement form.

LAET concurs with the above recommendation. This section has been added to LAET's Accounting and Internal Control Manual and has been submitted to Kevin Moran from LSC for review and comment. These policies and procedures are being made part of the Cardholder Agreement that each cardholder must sign. Copy enclosed.

Recommendation 17: The Executive Director should ensure that the Accounting and Internal Control Manual is updated to include oversight responsibilities for consulting, personal service, and sole-source contracts, as well as the procedures required for different types of contracts. Additionally, the Executive Director should ensure that the updated Accounting and Internal Control Manual reflects that the LSC PAMM is no longer in effect and was superseded by the 45 CFR Part 1631.

LAET concurs with the above recommendation. The Accounting and Internal Control Manual has been updated on the referenced issues and has been approved by Craig Dober from LSC. Additionally, the Accounting and Internal Control Manual has been updated with these referenced issues and sent to Kevin Moran at LSC for further review and comment.

Recommendation 18: The Executive Director should ensure that actual practices regarding the maintenance of contracts conform to the policies described in the Accounting and Internal Control Manual as well as the LSC Accounting Guide.

LAET concurs with Recommendation 18. Contracts are now being stored in a central location on LAET's internal drive, and hard copies are maintained in the offices of the appropriate individuals including the Director of Finance, the Director of Development and Compliance, the Human Resources Specialist, and the Executive Director.

Recommendation 19: The Executive Director should establish and maintain a centralized filing system for all contracts that contains all pertinent documents related to the solicitation of bids including receipt and evaluation of bids, sole-source justification, vendor selection, a signed contract or agreement, required approvals, and any agreed upon modifications to a contract or agreement.

LAET concurs with the above recommendation. LAET will establish and maintain an electronic centralized filing system for all new contracts entered after the date of this response and will store in that centralized filing system all pertinent documents related to the solicitation of bids including receipt and evaluation of bids, sole-source justification, vendor selection, a signed contract or agreement, required approvals, and any agreed upon modifications to a contract or agreement. With regard to existing contracts and agreements, LAET has begun the process of gathering and organizing this documentation for storage electronically and in the Director of Finance's office or the office(s) of other designated managers as appropriate.

Recommendation 20: The Executive Director should ensure that contract agreements, especially those recurring in nature, are written, signed, dated and maintained for business arrangements. The contracts should fully document the agreed upon terms, price, and payment terms. Contracts should be reviewed periodically to ensure written terms are defined and current.

LAET concurs with the above recommendation. This process has been implemented and will be followed going forward.

Recommendation 21: The Executive Director should ensure that the process for each contract action is fully documented in writing such as sole-source justification and documentation of competition, if competitively bid. Contracts should receive the appropriate approvals as stated in the grantee's Accounting and Internal Control Manual. The approvals should be documented and filed with the contract.

LAET concurs with the above recommendation. The Accounting and Internal Control Manual has been updated and sent to Craig Dober with LSC for comment and approval prior to submission to LAET's Board of Directors.

Recommendation 22: The Executive Director should ensure that:

- a cost allocation methodology is formulated, implemented and updated in the grantee's Accounting and Internal Control Manual. This updated cost allocation methodology should be adequately documented with sufficient detail for the auditor, LSC, OIG, GAO, and others to easily understand, follow, and test the formula.
- the Director of Finance performs the allocations that have been outstanding since July 2018. Thereafter, allocations should be performed timely and adhere to 45 CFR §1630.

LAET concurs with the above recommendation. The cost allocation methodology has been updated in the Accounting and Internal Control Manual and has been submitted to Kevin Moran at LSC for review and comment. All of the allocations have been made since July 2018 as noted in the 2018 audit by Mitchell, Emert, and Hill. Allocations are currently being done on a monthly basis.

Recommendation 23: The Executive Director should ensure that written policies and procedures for fixed assets include the list of elements required by LSC's Fundamental Criteria for property records, procedures for tracking electronic devices containing sensitive information that are not capitalized, procedures for the disposition of electronic devices containing sensitive information, procedures for the disposition of personal property or real estate purchased with LSC funds, procedures describing the depreciation methods to be used, and procedures stating what a request for prior approval should contain.

LAET concurs with this recommendation. The Accounting and Internal Control Manual has been updated to address the referenced issues and has been submitted to Kevin Moran at LSC for review and comment.

Recommendation 24: The Executive Director should ensure the Accounting and Internal Control Manual reflects the property record system procedures that are currently implemented in practice: including the tagging system for relevant assets, tracking of IT equipment, and disposition procedures for electronic devices containing sensitive information.

LAET concurs with this recommendation. The Accounting and Internal Control Manual has been updated to address the reference matters and has been submitted to Kevin Moran at LSC for review and comment.

Recommendation 25: The Executive Director should ensure that all relevant devices are reconciled to the currently IT equipment record.

LAET concurs with the above recommendation. LAET has consulted with its outsourced IT provider and is in the process of reconciling all relevant devices to the current IT equipment record. The IT equipment record for relevant and/or managed workstations is documented with the IT Systems Administrator and The IT Company (aka Transition LLC). Reports can be generated upon request with a list of computers that can be accessed by IT. All workstations have a proper naming convention respective to the organization, the workstation's location, and the computer type.

- *Example: LAET-KNX-DT001 | Legal Aid – Knoxville – Desktop*
- *Example: LAET-CHT-LT001 | Legal Aid – Chattanooga – Laptop*

With the IT Company's managed services software, IT is able to see who last logged into each computer and remote in to provide support, apply updates, patches, etc. Once the report is generated and exported to Microsoft Excel, it will generate the following information: Computer Name, Company, Location, Assigned LAET Employee (User), Type of Computer, Brand, Serial Number, and Model. Details around location are manually modified by IT Systems Administrator. With this information documented, the IT equipment record is reconciled.

Recommendation 26: The Executive Director should ensure that electronic devices containing sensitive information are easily traceable with a location for each relevant item included in the IT equipment record.

LAET concurs with Recommendation 26. LAET has consulted with its outsourced IT provider The IT Company and is in the process of ensuring that all relevant devices are reconciled to the current IT equipment record. The IT equipment record indicates the location of each workstation and who it belongs to, otherwise known as the last known user. Workstations purchased under specific grants are approved by management and documented by the LAET Finance Department in Abila MIP, LAET's accounting software. Each workstation can be accessed onsite or remotely by IT upon request and when the workstation is connected to the internet. Additionally, each computer is joined to a domain and requires password authentication in order to log into the domain. All data can be stored on the computer's hard drive and on an IT managed network share. This is known as the Documents Redirect Folder (Documents) and the G: Drive. These network shares are connected and backed up to IT managed servers placed in three locations: Knoxville (Main), Chattanooga, and Johnson City. All data is backed up and replicated across all three servers.

<u>Recommendation 27:</u> The Executive Director should ensure that authorization to sign checks is promptly cancelled when an employee leaves the organization.

LAET concurs with the above recommendation. Authorized check signers who are no longer with LAET will have their authorization cancelled. The Human Resource Specialist is required to notify the Director of Finance of any pending terminations to ensure that the departing employee's access to any and all bank accounts can be canceled, along with any associated debit/credit cards.

<u>Recommendation 28:</u> The Executive Director should ensure that duties are segregated within the organization's accounting system so that no individual can initiate, execute, and record a transaction without a second independent person being involved in the process.

LAET concurs with the above recommendation. LAET ensured the proper segregation of duties when it hired an Accounting Assistant for the Finance Department in February 2019.

<u>Recommendation 29:</u> The Executive Director should ensure that grantee personnel adhere to the grantee's written policy of voiding outstanding checks after six months.

LAET concurs with the above recommendation. The Finance Department made 2018 Audit adjustments to account for checks that remained outstanding during and/or as the result of the transition in Finance Directors during 2018.

<u>Recommendation 30:</u> The Executive Director should ensure that bank statements are reconciled monthly to the general ledger by an employee who has no access to cash, is not a regular check signer, and has no cash bookkeeping duties; in addition, a single employee should not have the authority to initiate electronic transactions and perform bookkeeping duties.

LAET concurs with this recommendation Bank statements are being reconciled by the LAET's former Chief Financial Officer Judy Moffett, who retired from LAET in 2011 and is now working for LAET as an independent contractor. Ms. Moffett does not have access to cash, is not a regular check signer, and does not have bookkeeping duties. LAET is evaluating the feasibility of hiring an employee to perform bank reconciliations on a permanent basis.

<u>Recommendation 31</u>: The Executive Director should ensure that the bank reconciliation process is performed timely, reconciled to the general ledger, and documented on the reconciliation sheet by signature and date.

LAET concurs with this recommendation. The transition in LAET's Finance Department created a backlog of work that is being brought current. In addition, LAET added an Accounting Assistant and an independent contractor to its Finance Department last year. These efforts, among others, should allow LAET to once again perform reconciliations in a timely fashion.

Recommendation 32: The Executive Director should ensure that LAET'S Accounting and Internal Control Manual is updated to reflect the current $25,000 threshold for expenditures requiring prior LSC approval. Furthermore, the Accounting and Internal Control Manual should be updated to reflect a clear segregation of duties over bank reconciliations.

LAET concurs with the above recommendation. The Accounting and Internal Control Manual has been updated to address these matters and has been submitted to Kevin Moran at LSC for review and comment.

Please let me know if you have any questions or need any additional information.

Sincerely,

Sheri A. Fox

Sheri A. Fox
Executive Director

Enclosures