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Legal Services Corporation

Inspector General
Jeffrey E. Schanz

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March 23, 2017

Mr. Michael Figgins
Executive Director
Legal Aid Services of Oklahoma, Inc.
2915 Classen Blvd., Suite 500
Oklahoma City, OK 73106

Dear Mr. Figgins:

Enclosed is the Legal Services Corporation's Office of Inspector General's (OIG) final report for our audit of Selected Internal Controls at Legal Aid Services of Oklahoma. Your comments are included in the final report as Appendix II.

The OIG considers your proposed actions to address Recommendations 1 through 15 as responsive. The actions planned by grantee management to address the issues and revise and update its Accounting Manual should correct the issues identified in the report.

However, Recommendations 1, 2, 3, 5, 8, 10, 12, 14 and 15 will remain open until the grantee has updated its Accounting Manual and obtained the required Board of Directors' approval or fully implemented their planned actions related to the findings. Recommendation 4 will remain open until the grantee provides some type of evidence that the laptops have been located and an explanation why they could not be found when the OIG was on site.

Recommendation 9 will remain open until the grantee has provided the OIG with a revised or modified contract with the corrected service dates for the Complete Computers contract as stated in the report.

Recommendations 6, 7, 11 and 13 are considered closed.

Please provide us with your response to close out the 11 open recommendations along with the revised Accounting Manual within six months of the date of this final report.

LSC
America's Partner For Equal Justice

Sincerely,

Jeffrey E. Schanz
Inspector General

Enclosure

cc: Legal Services Corporation
Jim Sandman, President

Lynn Jennings,
Vice President for Grants Management

Legal Aid Services of Oklahoma, Inc.
Molly Aspan
Board Chairperson

Sent by E-mail to Board of Directors
Marianne Blair
Mark Bonney
Jack L. Brown
Oleda Duckett
Douglas S. Dodd
Frederic Dorwart
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Bruce Frazier
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LEGAL SERVICES CORPORATION

OFFICE OF INSPECTOR GENERAL

FINAL REPORT ON SELECTED INTERNAL CONTROLS

LEGAL AID SERVICES OF OKLAHOMA, INC.

RNO 737066

Report No. AU 17-04

March 2017

www.oig.lsc.gov

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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 Services of Oklahoma, Inc. (LASO or grantee) related to specific grantee operations and oversight. Audit work was conducted at the grantee's administrative office in Oklahoma City, OK and at LSC headquarters in Washington, DC.

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

> [T]he process put in place, managed and maintained by the recipients' 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 Services of Oklahoma, Inc. (LASO) is a non-profit organization that provides civil legal assistance to low-income persons throughout the state of Oklahoma. LASO's mission is to be a partner in the community by making equal justice for all a reality. LASO was established in 2001 as a result of Legal Aid Services of Eastern Oklahoma, Inc. and Legal Aid of Western Oklahoma merging to create a unified program for the state. LASO maintains 18 offices throughout the state of Oklahoma.

LASO receives grants and contributions from a variety of sources including governmental agencies and private contributions. According to audited financial statements for the year ended December 31, 2015, the grantee received a total of $11,177,380 in LSC and non-LSC funding. Approximately 40 percent of the grantee's total funding was provided by LSC in the amount of $4,463,724. Approximately, 60 percent was non-LSC funding in the amount of $6,713,656.

OBJECTIVE

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

AUDIT FINDINGS

To accomplish the audit objective, the OIG reviewed and tested internal controls related to cash disbursements, credit cards, cost allocation, contracting, fixed assets, general ledger and financial controls, derivative income, internal reporting and budgeting, and employee benefits and payroll. While many of the controls were adequately designed and properly implemented as they relate to specific grantee operations and oversight, some controls need to be strengthened and formalized in writing. The OIG identified the following areas that need improvement.

WRITTEN POLICIES AND PROCEDURES

Overall, the grantee's written policies and procedures in the areas of general ledger and financial controls, contracting, derivative income, fixed assets, credit cards, cash disbursements, budgeting, payroll, and employee benefits need to be strengthened or established to properly describe the controls and procedures. Section 3-4 of the Accounting Guide states that each grantee must develop a written accounting manual that describes the specific procedures to be followed in order to comply with LSC's *Fundamental Criteria of an Accounting and Financial Reporting System (Fundamental Criteria)*. For the most part, the grantee had adequate practices in place; however, the level of detail in the policies stated in the Accounting Manual need to be enhanced.

General Ledger and Financial Controls Policy

The grantee's Accounting Manual contained documented policies and procedures relating to the general ledger and financial controls that mostly adhered to LSC regulations and guidelines, but they were missing a written policy explaining the separation of LSC and non-LSC receipts and disbursements. The Accounting Manual also did not state how stale dated checks are handled.

Section 2-1.2 of the Accounting Guide states the grantee should establish and maintain an accounting system to record grants, contracts and contributions separately. The Accounting Guide further states that because LSC requires separate disclosure as part of the financial statements, LSC grantees should maintain a fund-based accounting system, at least for LSC funds.

Contracting Policy

The grantee's policies and procedures for contracting were comparable with most of the components of LSC's *Fundamental Criteria*. However, the grantee's Accounting Manual omitted information detailing the dollar threshold values for the types of contracts that require competition and the requirement that all documentation related to a contract be centrally filed.

Derivative Income Policy

The grantee receives two types of derivative income, attorneys' fees and interest income. The grantee has documented policies and procedures in regards to attorneys' fees that are mostly comparable to LSC's regulations and *Fundamental Criteria.* However, there were no documented policies and procedures related to interest income or future potential derivative income such as rent, or any portion of a reimbursement or recovery of direct payments to attorneys, proceeds from the sale of assets, or other compensation or income attributable to any LSC grant. Even though the interest income received by the grantee is generally minimal, there should be a written policy in place which details the methodology on how the grantee allocates interest back to the funding sources.

Fixed Assets Policy

The OIG's review of the grantee's policies and procedures over fixed assets found that they did not contain all the elements stated in LSC's *Fundamental Criteria.* The written policy included in the grantee's Accounting Manual omits the following with respect to fixed assets:

(1) procedures and controls over the disposal of assets;
(2) the depreciation method used; and
(3) required elements in the property records including the description of the property, date acquired, check number, original cost, fair value, method of valuation, salvage value, funding source, estimated life, depreciation method, identification number, and location.

Credit Card Policy

Currently, the grantee has one business credit card account with 15 authorized cardholders on that account. The grantee's Accounting Manual does not contain a policy to govern the issuance and use of credit cards. However, the grantee has drafted a policy which was to be presented to the Board of Directors at its September 2016 meeting. The OIG reviewed the draft policy and determined that it did not contain: 1) a credit card spending limit; 2) requirements for approval of credit card charges; 3) specified permissible charges; and 4) means for avoidance of late fees/finance charges. Grantee management was informed of the missing elements and assured the OIG that the draft policy would be updated to include those elements. We contacted the Controller and she stated the draft policy was approved at their September 2016 board meeting, however, the minutes have not yet been prepared.

Chapter 3-6 (Fraud Prevention Guide) of the Accounting Guide stipulates that grantees should set credit card spending limits for its users. Properly controlling the issuance of credit cards through written policies reduces the potential for misuse and protects the grantee's resources.

Cash Disbursements

The grantee's policies and procedures for disbursements did not include controls and procedures over the Master Vendor List. These policies and procedures should include the processes of vetting new vendors, deactivating vendors, editing information and purging the list of vendors whom the grantee no longer uses.

Budgeting

The OIG determined that the grantee does not have documented policies and procedures relating to budgeting in its Accounting Manual; however, the grantee does have an adequate budget process in practice. The written policy should address the steps in the budget process, who is involved in the budgeting process, who prepares, reviews, approves and uses the budget and budget analysis.

Payroll

The grantee's policies and procedures for payroll were comparable with the components of LSC's *Fundamental Criteria*. However, the grantee's Accounting Manual omitted some steps in the process of the payroll function. The Accounting Manual should include more detail in regards to the review and approval process performed by the Controller on the semi-monthly payroll register. Also, the grantee needs to incorporate its new self-initiated procedure related to the Director of Operations' review of the hourly rate document into the Accounting Manual. This new procedure is intended to verify the data entered in the accounting system by the Payroll Clerk.

Employee Benefits

The grantee has a school Loan Repayment Assistance Program (LRAP) in the Accounting Manual, but it is outdated. The outdated policy states that regular full-time employees with an annual salary of less than $30,000, may be eligible to participate in the program. It also stated that the grantee pays up to $2,707 annually towards the school debt. However, according to discussions with the Director of Operations, the policy in the accounting manual is incorrect. Currently, the program pays a maximum of $5,000 per year to attorneys with outstanding school debt.

As outlined above, the grantee's Accounting Manual needs improvement. Grantee management was not aware that it's Accounting Manual required a significant level of detail in order to meet LSC's *Fundamental Criteria* requirements. Grantee management stated they have not had a chance to update the Accounting Manual to reflect all the new or current practices.

Written policies and procedures serve as a method to document the design of controls and adequately communicate them to the staff. 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 the staff and ensuring that proper controls are followed.

Recommendation 1: The Executive Director needs to establish or update written policies for:

a. general ledger and financial controls,
b. contracting,
c. derivative income,
d. fixed assets,
e. credit cards,
f. cash disbursements
g. budgeting,
h. payroll, and
i. employee benefits.

The written policies put into place should adequately describe the current grantee processes and controls in sufficient detail and be in accordance with LSC's Accounting Guide and *Fundamental Criteria.*

FIXED ASSETS

Inaccurate Inventory Listing

During the OIG's review and testing of property and the master inventory list, we found many discrepancies and could not locate all property items. The OIG reviewed the grantee's internal controls over fixed assets and found that there were adequate controls in place to properly track capitalized assets. However, during the physical inventory check of items not capitalized, the OIG found the master inventory list had not been updated, and was inaccurate. The following issues were noted:

- 24 electronic devices were selected from the master inventory list in order to verify their existence and compare asset tag numbers. The results from this revealed that 19 items had discrepancies which included:
    - 1 item that could not be identified or located by IT staff;
    - 3 items already disposed of but still on the list;
    - 4 items had asset tags which were different than those on the inventory list;

- 4 items were transferred to another office but on the inventory list still showing the headquarters as the asset location;
- 7 laptops are considered missing because they are unable to be tracked to a specific person or location.

- We physically observed 21 items at the grantee's headquarters, which included 10 electronic devices and 11 furniture items that were traced to the master inventory list. Six of the 21 items in the office were not found on the master inventory list.

The master inventory list also had discrepancies in repeating tag numbers for different items, and not all the fields on the list were populated with required information. Those fields included the type of item, brand, model, and serial number.

Section 2-2.4 of the LSC Accounting Guide states that the grantee should be mindful of items that may contain sensitive information (e.g., a computer with client confidential information), items with values lower than $5,000, and the need to inventory these items and dispose of them appropriately. For property control purposes, a physical inventory should be taken and the results reconciled with the property records at least once every two (2) years. Any differences between quantities determined by the physical inspection and those shown in the accounting records shall be investigated to determine the cause(s) of the difference. Then, the accounting records should be reconciled to the results of the physical inventory with an appropriate note included in the financial statements, if determined to be material by the grantee's auditor.

The Director of Operations expressed surprise that some of the items could not be located. For items with asset tags affixed to them that are different than what the inventory list contained, he stated that the Information Technology department was responsible for its inventory and updating the master inventory list, but that was not done. The Deputy Director of Information and Technology stated he had been trying to determine the best way to go about doing the inventory and tracking all items that had been purchased and assigned to employees prior to his hiring. As such, the OIG noted that at the time of the audit, he had taken no action to update the inventory list.

Failure to maintain an adequate inventory listing could result in difficulty in accounting for and tracking property. An inadequate inventory listing could also result in items being lost or stolen without management's knowledge. Also, without an adequate and complete tracking system for all electronic items, there is no assurance that the grantee is properly safeguarding the equipment and information contained therein.

Recommendations: The Executive Director should:

Recommendations 2: update the grantee's master inventory list with adequate information, ensuring all fields are completed with accurate information.

Recommendation 3: ensure that a complete physical inventory is conducted in all locations and reconciled with the property records.

Recommendation 4: investigate what happened to the missing laptops, and if they cannot be located, the laptops should be removed from the inventory.

DISBURSEMENTS

In general, the OIG found that the grantee had adequate controls over most areas of disbursements except approvals. As part of our testing, the following issues were noted:

Inadequate Approvals

As part of the grantee's disbursement process, invoices are reviewed and approved by the Executive Director or the Director of Operations prior to generating a disbursement check. The OIG found 12 disbursements out of a sample of 85, totaling $136,362.79, whose invoices did not have prior approval before processing the disbursement check. Not approving invoices in accordance with the grantee's policy is a significant control deficiency showing that this control is not operating effectively.

The OIG also found 38 disbursements with approved invoices but those approvals were not dated. Without a documented date of approval, grantee management cannot determine if the invoices were timely approved and whether proper procedure was followed. The Executive Director said grantee management failed to notice that authorized approvers were not documenting dates of their approval.

Section 3-5.4 of the Accounting Guide, Cash Disbursements, states that approval should be required at an appropriate level of management before making a commitment of resources. Failure to follow the purchase approval process may result in purchases being made without the knowledge of appropriate management or at unacceptable prices or terms. Also, without signatures being dated there is no way to verify if approvals were made timely.

Lack of Segregation of Duties

Our review of the Accounts Payable Clerk's job duties and responsibilities and the grantee's MIP accounting system user access rights report showed that there is a lack of segregation of duties over the maintenance of the master vendor list. The Accounts Payable Clerk, whose primary duties include initiating and processing payments, also has user rights to the master vendor list to create new vendors and to edit, delete and process vendor information within the grantee's accounting system. The grantee's accounting system does have the capability to prepare an audit trail report, but that function is not used to monitor master vendor list activity.

Chapter 3-4 of the Accounting Guide, Internal Controls Structure, states that 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.

Without adequate segregation of duties between the Accounts Payable function and maintenance of the master vendor list, the grantee may not be able to detect unauthorized changes to vendor information which may further lead to fraud, waste or abuse of the grantee's scarce resources.

<u>Recommendations</u>: The Executive Director should ensure:

<u>Recommendation 5</u>: purchases are reviewed and approved at an appropriate level of management before processing disbursements.

<u>Recommendation 6</u>: approvals are dated in order to document when approvals occurred and whether the approvals were made timely.

<u>Recommendation 7</u>: Accounts Payable Clerk's duties are properly segregated with respect to their master vendor list responsibilities and access.

CONTRACTING

<u>Lack of Contract Approval</u>

Our review of 20 contracts revealed that six were not approved. Also, the approvals for one contract were unknown because the contract was not provided. In addition, there were seven contracts that had approvals that were not dated. As such, there is no record on when the contract was actually approved if at all. LASO management stated that the lack of approvals, as well as undated signatures on contracts, was due to management oversight.

<u>Contract Payments Not Consistent with Contract Terms</u>

The OIG found that invoices received from the contractor for server hosting did not agree with the dollar amounts to be paid as stipulated in the contract. The contract stated an amount of $2,850/month to be paid for the contractor's services, however, upon review of invoices, the contractor was being paid an additional $6,525 monthly hosting fee and monthly fees for configurations and support ranging from $85 to $95 an hour. Neither the $6,525 monthly hosting fee nor the monthly fees for configurations was stated in the contract. We were also informed that there were no contract modifications or revisions stating these additional terms.

The LASO Director of Information Technology could not provide a reason as to why invoices for the server hosting contract did not match the contractual agreement. Based on the contract terms versus actual payments made to the vendor by LASO, the OIG estimates that during the period of review, the grantee paid $47,118 more than what was stated and agreed upon in the contract. However, from subsequent discussions with the grantee after the initial draft report was issued, the OIG was provided a reasonable explanation why the contract terms didn't agree with the invoices. The dates on the contract were incorrect and did not cover the actual dates that services were to be provided.

Lack of Competition

Of the 20 contracts reviewed, all contracts were sole source. However, there were no sole source justifications prepared or on file for any of the contracts. Seventeen of those contracts were supposed to be competitively bid because they exceeded the $3,000 threshold which triggers the competitive bidding process according to the grantee's competition policy. The Director of Operations stated that sole sourcing contracts was the contracting method used by the grantee prior to his employment. However, sole source justifications were not documented.

The following table summarizes the 20 contracts sampled:

Contracts	Total Amount Disbursed from 1/1/2015 to 06/30/2016	Type of Contract	Missing Documentation	Proper Approvals	Approvals Dated
Contractor 1	$53,362.80	Contract Attorney	Sole Source Justification	No	Yes
Contractor 2	$ 23,051.25	Contract Attorney	2015 Contract, Sole Source Justification	Yes	No
Contractor 3	$ 32,143.88	Contract Attorney	Sole Source Justification	Yes	Yes
Contractor 4	$ 46,323.61	Contract Attorney	2016 Contract, Sole Source Justification	No	Yes
Contractor 5	$ 12,879.21	Contract Attorney	2015 Contract, Sole Source Justification	Yes	Yes
Contractor 6	$ 6,858.66	Contract Attorney	Sole Source Justification	Yes	Yes
Contractor 7	$ 1,028.02	Contract Attorney	Sole Source Justification,	No	No
Contractor 8	$ 36,895.50	Contract Attorney	Sole Source Justification, 2015 Contracts,2016 Contract	No	No
Contractor 9	$ 6,034.57	Contract Attorney	Sole Source Justification	Yes	Yes
Contractor 10	$ 21,524.40	Contract Attorney	2015 Contract, Sole Source Justification	Yes	Yes
Contractor 11	$ 3,045.00*	Janitorial	Sole Source Justification	No	Yes
Contractor 12	$ 6,750.00	Janitorial	Sole Source Justification	No	Yes
Contractor 13	$ 3,990.00*	Janitorial	Invoice Support	Yes	Yes
Contractor 14	$ 7,200.00	Janitorial	Sole Source Justification	Yes	No
Contractor 15	$ 4,345.00*	Janitorial	Sole Source Justification	Yes	No
Contractor 16	$ 4,675.00	Janitorial	Sole Source Justification	Yes	No
Contractor 17	$ 55,500.00	IPA	Sole Source Justification	Yes	No
Contractor 18	$ 30,311.49	Phone Leasing	Missing Contract	Unkown	Unknown
Contractor 19	$ 32,700.00	Legal Server Hosting	Sole Source Justification	Yes	Yes
Contractor 20	$101,317.50	Serving Hosting	Invoice Support, Sole Source Justification	Yes	Yes

Note: We state “unknown” here because the grantee does not have the contract on file for us to determine whether the contract was competed or awarded sole source.

‘*The contract award amount was less than $3,000 and therefore did not require competition.

Section 3-5.16 of the Accounting Guide, Contracting, states the process used for each contract action should be fully documented and the documentation should be maintained in a central file. In addition, documents to support the competition should be retained in the contract file and any deviation from the approved contracting process should be fully documented, approved and also maintained in the contract file. Finally, the required approval level (including items that need to be approval by LSC) 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 with potential for abuse. In addition, since not all contracts are the same, for large contracts, competition helps ensure the best value for the grantee and proper documentation helps ensure that an approved contract has followed all established procedures.

Recommendations: The Executive Director should ensure that:

Recommendation 8: all 6 contracts that were not approved are reviewed, approved and properly dated. Also, the 7 contracts that were not dated need to be noted with the approximate date of sign off.

Recommendation 9: Contract service dates shown on the actual contract for Complete Computers be revised or modified to reflect the actual servies dates intended to be covered.

Recommendation 10: contracts are competed, when required to obtain the best available price and service as stated in the grantee’s Accounting Manual and LSC’s *Fundamental Criteria*. If a contract is appropriately sole sourced, the grantee should prepare a sole source justification and maintain the file.

GENERAL LEDGER AND FINANCIAL CONTROLS

Accounting System Passwords

During an interview with grantee management, it was stated that the users to the MIP accounting system have access to the system by use of their own user name and passwords. However, the system is not not set up to for password expiration and requirement to be changed after a certain period of time. Grantee management could not provide a reason as to why user passwords do not expire.

Without proper controls in place that require passwords to the accounting system to expire and be changed, there could be unauthorized use and transactions made by individuals not authorized to use the system.

The LSC *Fundamental Criteria* provides that each grantee must develop security controls for all computers and the data contained therein that ensure proper protection against theft, loss, unauthorized access, and natural disaster.

Recommendation 11: The Executive Director should implement a procedure that requires passwords to the accounting system to expire and be changed at regular intervals.

DERIVATIVE INCOME

Allocation of Attorneys' Fees

The attorneys' fees allocation methodology in practice is not in conformity with LSC regulations. In practice, the grantee assigns a funding code to each case which remains throughout the duration of work performed by the attorney, thus only one grant/fund is used per case. The fees generated from that case are then awarded to the funding source assigned to that case and not allocated by the hours charged by the attorneys. All of the fees are attributed to one funding source, instead of being allocated in proportion to the funding sources used to charge attorney time expended for a particular case.

45 CFR §1609.4 provides that:

> (a) Attorneys' fees received by a recipient for representation supported in whole or in part with funds provided by the Corporation shall be allocated to the fund in which the recipient's LSC grant is recorded in the same proportion that the amount of Corporation funds expended bears to the total amount expended by the recipient to support the representation.

During the period under review, the grantee received a total of $191,092.62 in court awarded attorneys' fees. Our review of all 48 cases from this period revealed that 6 cases in the amount of $8,750 had time charged to LSC, but none of the attorneys' fees from those cases were allocated back to LSC. This occurred because the non-LSC funding source was charged the majority of the hours for these cases. Based on LSC regulations, the OIG determined that $549 of attorneys' fees from these cases should have been allocated to LSC.

Properly recording attorneys' fees in accordance with LSC regulations allows the LSC fund to be allocated its apportioned share, which in turn can be used to provide legal services in accordance with LSC requirements.

Recommendation 12: The Executive Director must ensure that attorneys' fees are allocated in accordance with the requirements specified in 45 CFR §1609.4.

EMPLOYEE BENEFITS

Monitor Loan Balances

The grantee has a Loan Repayment Assistance Program (LRAP) in which the grantee pays a maximum of $5,000 per year to attorneys with outstanding student loan debt. However, the grantee does not have a process in place to determine if the funds they have awarded to the participants are actually being used to pay down the student's outstanding loan. There is also no monitoring done by the grantee to ensure that the loan balance is being paid down. Lastly, the grantee has not set a maximum amount or cap on the total payment a person can receive from this program. The grantee stated they did not know that monitoring or a cap was actually needed.

45 CFR Part 1630.3 provides that:

> (a) *General criteria.* Expenditures by a recipient are allowable under the recipient's grant or contract only if the recipient can demonstrate that the cost was**: (1)** Actually incurred in the performance of the grant or contract and the recipient was liable for payment; **(2)** Reasonable and necessary for the performance of the grant or contract as approved by the Corporation; **(3)** Allocable to the grant or contract.

By not setting a maximum total payment amount and monitoring to ensure that the payout does not exceed that amount, the grantee could be paying more than the outstanding loan balance. By confirming whether employees are actually paying down their outstanding student loans, the grantee can ensure that the LRAP funds are being used for their intended purposes.

Recommendations: The Executive Director should:

Recommendation 13: implement a process to monitor employee outstanding loan balances and ensure balances are being paid down and do not exceed the outstanding loan balance.

Recommendation 14: set a maximum total dollar amount that can be paid to each employee for LRAP.

PAYROLL

Lack of Segregation of Duties

During an interview with grantee management, it was noted that the Payroll Clerk enters all Human Resources (HR) related information into the payroll module for the HR staff. This information includes any pay rate changes, address changes, overtime pay, payroll deductions and exemptions, and anything related to HR. Other than to ensure that the pay rates are proper, the Director of HR does not check the other HR related information entered by the payroll clerk. The grantee stated it was easier for the Payroll Clerk to enter this information since she is more familiar with how to enter the payroll and personnel information.

Allowing the Payroll Clerk to enter HR information without detailed review could result in fraud or misappropriation of payroll funds.

<u>Recommendation 15</u>: The Executive Director should ensure that the HR and Payroll functions are adequately segregated and restricted. HR information should be entered in the accounting system by someone other than the Payroll Clerk, or additional compensating controls and review needs to be put in place over the HR information currently entered into the accounting system by the Payroll Clerk.

SUMMARY OF GRANTEE MANAGEMENT COMMENTS

Grantee management agreed with all the findings and accepted all 15 recommendations in the report. Grantee management's formal comments can be found in Appendix II.

OIG EVALUATION OF GRANTEE MANGEMENT COMMENTS

The OIG considers the actions taken or proposed responsive to all 15 of the recommendations. However, Recommendations 1, 2, 3, 5, 8,10,12,14 and 15 will remain open until the grantee has updated its Accounting Manual and obtained the required Board of Directors approval or fully implemented their planned actions related to the findings. Recommendation 4 will also remain open until the grantee has provided some evidence that the 7 laptops have been located and an explanation on why they couldn't be found at the time of the audit as well as their current location.

The OIG had subsequent discussions with grantee management on Recommendation 9. Grantee management determined that the dates on the contract in question were incorrect and should be revised or modified. As such, they will ensure that contract service dates shown on the actual contract for Complete Computers are revised or modified to reflect the actual services dates intended to be covered. This finding will remain open until the grantee provides the OIG documentation showing that the proposed service dates on the Complete Computers contract has been modified to reflect the actual service dates.

Recommendations 6, 7, 11 and 13 are considered closed.

SCOPE AND METHODOLOGY

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

- Cash Disbursements;
- Credit 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 the areas reviewed, the grantee's policies and procedures were reviewed including manuals, guidelines, memoranda and directives, setting forth current grantee's 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. This review was limited in scope and not sufficient for expressing an opinion on the entire system of the grantee's internal controls over financial operations.

We assessed the reliability of computer generated data the grantee provided by reviewing available supporting documentation for the entries selected for review, making comparisons of data with other independent source documents, conducting interviews and making physical observations to determine data consistency and reasonableness. We determined the data were sufficiently reliable for the purposes of this report.

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

To test for the appropriateness of expenditures and the existence of adequate supporting documentation, disbursements from a judgmentally selected sample of employee and vendor files were reviewed. The sample consisted of 85 disbursements and credit card transactions totaling $396,532.36. The sample represented approximately 7 percent of the $5,755,334.52 disbursed for expenses other than payroll during the period January 1, 2015 to June 30, 2016.

Controls over derivative income were reviewed by examining current grantee practices and reviewing the written policies contained in the grantee's accounting manual, where applicable. We interviewed appropriate program personnel and performed recalculations of some revenue accounts.

To evaluate adequacy of the cost allocation process, we selected 10 disbursements from the check register and vouched the information to the source documents, such as invoices and check stubs. We vouched the information in the general ledger details report to the information in the general ledger to verify completeness and accuracy.

To evaluate the adequacy of the payroll functions and processes, we interviewed the controller. We found that the payroll clerk enters both payroll and personnel information into the accounting system, causing an issue with the segregation of duties. We recommended that the payroll clerk no longer enter personnel information into the accounting system.

The on-site fieldwork was conducted from August 15, 2016 through August 24, 2016. Our work was conducted at the grantee's program administration office in Oklahoma City, OK and at LSC headquarters in Washington, DC. We reviewed documents pertaining primarily to the period January 1, 2015 through June 30, 2016.

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

LEGAL AID SERVICES
OF OKLAHOMA, INC.

January 31, 2017

John M. Seeba
Assistant Inspector General for Audit
Office of Inspector General
Legal Services Corporation
3333 K Street, NW, 3rd Floor
Washington, DC 20007-3558

Dear Mr. Seeba:

Legal Aid Services of Oklahoma is in receipt of the draft report based on your August 2016 visit. Our response to the recommendations are below.

Recommendation 1: The Executive Director needs to establish or update written policies for:

a. **General Ledger and Financial Controls**
    a. **Stale dated checks**
    LASO has a process which is compliant with state laws and LSC guidelines, however does not describe this process in the Accounting Manual. A procedure is being developed for inclusion in the Accounting Manual.
    b. **Fund-based accounting system:**
    LASO has drafted a policy to present to the Board of Directors no later than June 2017 to require use of a fund-based accounting system. LASO uses Abila MIP Fund Accounting and believes that the current practice is consistent with LSC guidelines.
b. **Contracting policy:**
The contracting policy will be updated with the recommendations outlined by OIG. The policy will be presented to the Board at the June 2017 meeting.
c. **Derivative income policy:**
LASO has drafted a policy to present to the Board of Directors no later than June 2017, expanding the current policy on Attorney Fees to include all sources of derivative income.
d. **Fixed assets, credit cards:**
LASO is developing inventory procedures to include the fields requested by OIG. To be completed by 6/30/2017.
e. **Cash Disbursements (Master Vendor List)**
LASO will develop a policy and/or procedure to address the concerns and include those in the Accounting Manual.
f. **Budgeting**

LASO will expand the existing budget policy for review and approval of the Financial Oversight Committee and the Board of Directors.

g. Payroll
LASO will include additional procedures in the Accounting Manual to address the Comptroller's and the Director of Operations' payroll review.

h. Employee Benefits (LRAP)
The LRAP policy, approved by the Board in September 2016, updated the existing policy. It addresses the issues raised by OIG.

Recommendation 2: The Executive Director should update the grantee's master inventory list with adequate information, ensuring all fields are completed with accurate information

A "hard" inventory will be completed by 6/30/2017. A master inventory will be updated and will include the fields outlined by OIG.

Recommendation 3: The Executive Director should ensure that a complete physical inventory is conducted in all location and reconciled with the property records

An update to the inventory will be completed by 6/30/2017. Each office will take a "hard" inventory and will send accurate update to Director of Operations, or designee.

Recommendation 4: The Executive Director should investigate what happened to the missing laptops, and if they cannot be located, the laptops should be removed from the inventory.

The seven missing laptops have been located.

Recommendation 5: The Executive Director should ensure that purchases are reviewed and approved at an appropriate level of management before processing disbursements

Several of these items required approval of the Executive Director but were signed by another manager, while others contained approvals on supporting documents but not an approval signature on the actual invoice. LASO staff is reviewing its practices and will conduct training to address this concern by March 31, 2017.

Recommendation 6: The Executive Director should ensure that approvals are dated in order to document when approvals occurred and whether the approvals were made timely.

Staff who approve invoices have been instructed to date all approvals.

Recommendation 7: The Executive Director should ensure that the Accounts Payable Clerk's duties are properly segregated with respect to their master vendor list responsibilities and access.

LASO has removed the ability for the A/P clerk to add or modify vendor records.

Recommendation 8: The Executive Director should ensure that all 6 contracted that were not approved are reviewed, approved and properly dated. Also, the 7 contracts that were not dated need to be noted with the approximate date of sign off

Will be resolved by 2/28/2017.

Recommendation 9: The Executive Director should ensure that the grantee adhere to all of the terms as stated in the serving hosting contract. If additional services of difference prices are required, then the grantee should initiate a contract modification or enter into a new contract stating the new terms as agreed upon by both parties

LASO regrets the misinformation conveyed in August. Upon further research, we were able to ascertain that a contract modification was signed August 2013 for $6,525 ($29/month X 225 users) for an application hosting project that we were testing for running our case management system (Prime) in the cloud using 2X software on an application virtualization platform. This contract was ended after 6 months with mutual agreement when LASO decided to move to Legal Server. (Contract Attached)

Recommendation 10: The Executive Director should ensure that contracts are competed, when required to obtain the best available price and service as stated in the grantee's Accounting Manual and LSC's Fundamental Criteria. If a contract is appropriately sole sourced, the grantee should prepare a sole source justification and maintain the file.

Contracts in excess of $3,000.00 will be secured in the following manner:

- Contract Attorney – solicited through local bar announcement. Extension of contract is dependent upon performance, need, and funding.
- Sole Source – Documentation of justification will be maintain with the contract document. Extension of contract is dependent upon performance, need, and funding.

Policies and procedures will be updated accordingly (see Recommendation 1b).

Recommendation 11: The Executive Director should implement a procedure that requires passwords to the accounting system to expire and be changed at regular intervals

The Abila MIP options have been updated to require a password change every 90 days.

Recommendation 12: The Executive Director must ensure that attorneys' fees are allocated in accordance with the requirements specified in 45 CFR 1609.4

LASO is developing a new process and procedure to prorate the attorneys' fees related to cases which were funded from more than one grant. This will be completed by March 31, 2017.

Recommendation 13: The Executive Director should implement a process to monitor employee outstanding loan balances and ensure balances are being paid down and do not exceed the outstanding loan balance.

Reflected in the LRAP policy adopted at the September 2016 meeting. (See Recommendation 1h.)

Recommendation 14: The Executive Director should set a maximum total dollar amount that can be paid to each employee for LRAP

The maximum LRAP benefit paid to an employee will be $50,000. Any waiver to the maximum, would require Board approval.

Recommendation 15: The Executive Director should ensure that the HR and Payroll functions are adequately segregated and restricted HR information should be entered in the accounting system by someone other than the Payroll Clerk, or additional compensating controls and review needs to be put in place over the HR information currently entered into the accounting system by the Payroll Clerk.

Periodic reviews of payroll (at least 3 times per year), will be conducted in the following manner:

- The Comptroller, or designee, will run a comprehensive payroll report for a specific pay period.
- Report will be given to the Director of Operations, or designee, for review.
- The report will be verified for accuracy with documentation/HR programs.
- Should questions arise in reviewing the report, the Director of Operation will consult with the Comptroller for answers.
- Questions will be resolved in a manner that allows the Director of Operations to "sign off" on the submitted payroll report, indicating its accuracy.
- Should the report be accurate, the Director of Operations will "sign off".

LASO will incorporate this process into the procedural document discussed in Recommendation 1g.

Please thank your staff for all of the hard work that they have done on this audit and contact Michael Figgins or myself if you have questions or concerns.

Sincerely,

Melissa Lange

Melissa Lange
Comptroller

Attachments