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Legal Services Corporation

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## MEMORANDUM

DATE: July 10, 2014

TO: Jim Sandman  
President, LSC

FROM: Jeffrey E. Schanz  
Inspector General, LSC

SUBJECT: Final Report on the Follow-up on the Audit of Report No. AU09-05,  
Legal Services Corporation Consultant Contracts

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Enclosed is the Office of Inspector General's (OIG) final report on the Follow-up on the Audit of Report No. AU09-05 Legal Services Corporation Consultant Contracts. The OIG has reviewed management's comments on the findings and recommendations contained in the draft report. Management's comments are included in the final report as Appendix II.

Management has agreed to all the findings and recommendations in the report. Actions taken on Recommendations 1, 2, and 3 are considered responsive and will be considered closed. Planned actions on Recommendations 4 and 5 are responsive, however, the two recommendations will remain open until OIG is notified in writing that the proposed action has been completed or implemented.

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

cc: Ron Flagg, General Counsel  
David Richardson, Comptroller

**LEGAL SERVICES CORPORATION  
OFFICE OF INSPECTOR GENERAL**

**FOLLOW-UP ON THE AUDIT OF  
REPORT NO. AU09-05 LEGAL  
SERVICES CORPORATION'S  
CONSULTANT CONTRACTS**

Report No. AU14-07

July 2014

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## INTRODUCTION

This audit is a follow-up on the effectiveness of management actions taken to correct the issues reported in our 2009 audit report entitled "Audit of LSC's Consultant Contracts" relating to implementing controls over the consultant contracting process.

LSC's contracting policies and procedures are contained in Chapter 1 of the LSC Administrative Manual. This chapter was last amended in December 2009. It is organized as follows:

- Part I – Definitions and Policies
- Part II – Procedures for Procurement of Goods
- Part III – Procedures for Contracting for Services
- Sample LSC Contract Approval Form
- Contract Originator's Contracting Procedure Outline

In general, LSC's contracting policies and procedures require that contracting for services undertaken on behalf of LSC be subject to competition and undergo various levels of review and approval. The policies and procedures also require that a purchase order be issued for each contract. The use of a Contract Approval Form is mandatory to document that required steps are performed and required approvals are obtained. LSC's contracting policies and procedures outline documentation requirements and require that the Comptroller's Office maintain contracting records for audit purposes. Lastly, a quarterly procedural sufficiency report to the President is required to ensure compliance with LSC's contracting policies and procedures.

LSC's consultant contracts originate in the requesting office, including contracts initiated at the direction of the Board of Directors and processed by the Office of Legal Affairs (OLA). Consultant contracts are for the procurement of services in which contractors use their time, skills and expertise. For the period of our review, LSC made contract payments valued at approximately \$1.69 million.

### Prior Audit

On July 7, 2009, the OIG issued an audit report entitled "Audit of LSC's Consultant Contracts." The OIG reported, among other things, that the design of controls over consultant contracts were generally adequate, however application of the controls was not enforced. LSC's written policies and procedures over the consultant contracting process were not regularly followed. Specifically:

- competition requirements were not followed;
- required approvals were not obtained;
- required basic information was not used in some contracts;
- forms to control the contracting process were not used;

- purchase orders were not always prepared; and
- contracting records were not properly maintained.

Eight of the 13 recommendations made by the OIG related to clarifying and following the policies and procedures used by all LSC personnel involved in the contracting process and addressed the issues listed above.

LSC management reported to the OIG that all actions on the 13 recommendations were completed. As a result, the OIG closed all 13 recommendations.

## **OBJECTIVE**

The overall objective was to determine if LSC management's actions corrected the deficiencies cited in the original report pertaining to following LSC's established policies and procedures to contract for consultants. Specifically, we determined whether internal controls and policies now in place as a result of the original audit were properly designed and followed.

## **OVERALL EVALUATION**

Management did not correct several of the deficiencies identified in the original report. While the design of controls over consultant contracts were generally adequate, the controls were not always applied. As a result, LSC's consultant contracting practices did not always follow the established policies and procedures.

Specifically, some contracts were awarded without:

- either engaging in competition or documenting the applicable exceptions to the competition requirement;
- obtaining the required approvals;
- files having all required documentation;
- including basic information; or
- properly documenting contract amendments and having them approved by the Office of Legal Affairs (OLA).

We also found that quarterly reports assessing the contracting process were not adequately prepared and that purchase orders were either not processed or improperly processed. Our detailed findings are presented below.

## **AUDIT RESULTS**

While LSC management agreed with all recommendations in the prior audit report and reported that appropriate actions were taken, operating personnel were not always following appropriate policies and procedures. Also, quarterly reporting to verify that the contracting system was working as designed was either not properly implemented, not accurate, or not acted upon when issues were identified. As a result, the OIG considers all findings in this report as repeat findings.

### **Contracting Process and Procedures Were Not Always Followed**

Policies and procedures for processing and controlling consultant contracts were not adequately implemented. Although adequate policies and procedures are contained in the LSC Administrative Manual, Chapter 1, Parts I and III, they were not always followed. All nine contracts reviewed had one or more deficiencies. The deficiencies and the number of contracts identified with the deficiencies are as follows.

- The rationale for using a sole source contract was not adequately documented for three sole source contracts. (LSC Administrative Manual, Chapter 1, Part I, Paragraphs C-8a and C-8b, and Part III, Paragraphs B-2c and B-2d)
- A contract approval form was not properly executed for one contract. (LSC Administrative Manual, Chapter 1, Part I, Paragraph B-2)
- Basic information, such as a schedule for completion of the work, and a specification that the contractor is an independent contractor and not an employee of LSC, was not included in one contract. (LSC Administrative Manual, Chapter 1, Part III, Paragraph B-3)
- Contractors were not required to submit invoices directly to the Comptroller for nine contracts. (LSC Administrative Manual, Chapter 1, Part III, Paragraph B-4c)
- One contract was awarded even though at least three responses from the RFP were not received and the reason was not documented. (LSC Administrative Manual, Chapter 1, Part III, Paragraph B-2b)
- Documentation on file for six contracts was not sufficient to constitute a complete history of contracting actions, including the RFP or statement of work, the list of bidders solicited, the response from each bidder, and the analysis performed on the bids received. (LSC Administrative Manual, Chapter 1, Part I, Paragraph B-3)

- In one instance, contract terms were modified without a documented amendment or documented review of changes by the Office of Legal Affairs. (LSC Administrative Manual, Chapter 1, Part III, Paragraph B-4b)

Office of Financial and Administrative Services (OFAS) operating personnel indicated they did not have a clear understanding of what contract documents were required to be maintained in the Comptroller's office contracting records. Our review of the LSC Accounting Procedures Manual<sup>1</sup> (APM) disclosed that procedures on how OFAS staff members were to implement the contracting requirements contained in the LSC Administrative Manual were not fully documented. There was no checklist or other document used by the Comptroller's office to ensure that required contracting records were adequately prepared, provided for review, and maintained. Following proper contracting policies and procedures helps protect LSC's interests and helps ensure that LSC receives the best value for services received.

**Recommendations:** The Comptroller should:

Recommendation 1. Update the LSC Accounting Procedures Manual to include OFAS policies and procedures that implement the contracting requirements of the LSC Administrative Manual, Chapter 1, Parts I and III. The two manuals should be in agreement.

Recommendation 2. Develop and implement a checklist to use in determining and documenting the procedural sufficiency of each consultant contract. The completed checklist for each consultant contract should be retained in OFAS contracting files.

### **Quarterly Reporting**

The Comptroller did not provide written quarterly reports to the LSC President on all consultant contracts signed during each quarter. LSC management agreed with the initial report's recommendation to require periodic reporting to the President of all consultant contracts executed along with the Comptroller's certification that procedural sufficiency has been attained. LSC management stated in its response to the prior audit, "we will adopt a reporting requirement for consultant contracts that includes the Comptroller certification and notice to the President of the Corporation."

The LSC Administrative Manual, Chapter 1, Part III, Paragraph B-5, requires that written quarterly reports be prepared by the Comptroller and provided to the President on all consultant contracts signed during that quarter. The quarterly report is required to document the Comptroller's assessment as to whether the contracting procedures

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<sup>1</sup> The Accounting Procedures Manual is a guide internal to OFAS and used by OFAS staff in processing and recording transactions through LSC's financial management system. While the Accounting Procedures Manual provided some guidance, it was not complete and did not reflect the current practice for processing purchase orders.

outlined in the LSC Administrative Manual are being adhered to, and if not, what actions are needed to achieve full compliance with the procedures.

The Comptroller stated that, although he did not provide written quarterly reports to the President, he did provide monthly encumbrance reports to the President. However, the encumbrance reports do not serve the same purpose as the quarterly procedural sufficiency reports. The purpose of the encumbrance report provided to the President is to identify the outstanding balance on contracts for which purchase orders were issued while the purpose of quarterly procedural sufficiency reports is to identify whether LSC's contracting policies and procedures were followed for all contracts issued during the quarter. Also, the encumbrance reports did not include the Comptroller's assessment of procedural sufficiency or suggested corrective actions for any noncompliance noted. The Comptroller provided no specific reason for not preparing and distributing the quarterly report as indicated in management's response to the original audit.

Quarterly reporting protects LSC's resources by assuring that proper contracting policies and procedures are followed, any deviations are identified in a timely manner, and corrective action is taken.

Recommendation 3. The Comptroller should provide written quarterly reports to the LSC President on all consultant contracts signed during each quarter as required by the LSC Administrative Manual, Part III, Paragraph B5. The reports should include the Comptroller's assessment of whether the contracting procedures outlined in the LSC Administrative Manual are being adhered to, and if not, what actions are needed to correct any deficiencies.

### **Purchase Order Processing**

Purchase orders for the consultant contracts reviewed were either not issued or not issued properly. LSC did not issue purchase orders for two of the contracts and for four other contracts, a payment was processed prior to issuing a purchase order. The LSC Administrative Manual, Chapter 1, Part III, Paragraph B-4a, requires that a purchase order be issued upon confirmation that a contract has been properly executed, and Part I, Paragraph C-5, requires that no invoice be paid until the purchase order has been approved.

For the two contracts paid in full without purchase orders, the staff member responsible for preparing purchase orders was not notified that the contracts were approved and executed. For the four contracts where a payment was made prior to issuing the purchase order, the first payments on the contracts were made outside of the purchase order system. As explained by the Comptroller, these four contracts were examples where contract originators presented invoices for payment before the contract had been signed and returned by the contractor.

Two additional items contributed to improperly processed purchase orders. First, the Accounting Procedures Manual did not fully describe the policies and procedures for

processing purchase orders. Second, OFAS operating personnel did not ensure that purchase orders were issued prior to paying the invoices.

Following established requirements for processing purchase orders before contract payments are made helps ensure contracts are properly executed and paid in accordance with approved terms.

**Recommendations:** The Comptroller should:

Recommendation 4. establish procedures that ensure purchase orders are properly issued and processed.

Recommendation 5. update the LSC Accounting Procedures Manual to include current OFAS policies and procedures for processing purchase orders.

### **AUDIT COMMENT**

During the course of the audit, LSC management took two actions to implement the controls already in place and to further strengthen some of these controls. First, LSC provided mandatory training for all staff members who are involved in the contracting process. The training reinforced current policies and procedures, and provided some guidance on documenting contract actions. Second, LSC management initiated a formal review of its current policies and procedures.

### **SUMMARY OF MANAGEMENT COMMENTS**

Management has agreed to and has either implemented or is in the process of implementing the OIG recommendations. For Recommendation 1, the Comptroller provided revisions to the LSC Accounting Procedures Manual to ensure that policies and procedures were now in agreement with the LSC Administrative Manual. In response to recommendation two, a checklist was developed to include in the contract file to document procedural sufficiency. For Recommendation 3, the Comptroller will provide a written memo to the LSC President regarding whether contracting procedures were or were not followed and if corrective actions are needed. Finally, for Recommendations 4 and 5, OFAS is currently in the process of revising Chapter 1 of the LSC Administrative Manual which will affect the Accounting Procedures Manual. In addition, training will be provided in July 2014 to OFAS staff who process purchase orders and invoices to ensure procedures are understood and followed correctly.

### **OIG EVALUATION OF MANAGEMENT COMMENTS**

The OIG has reviewed management's comments to the draft report findings and recommendations and has determined that the actions OFAS has planned or completed are responsive to the recommendations. Based on documentation provided by OFAS,

Recommendations 1 through 3 are complete and will be considered closed. Recommendations 4 and 5 will remain open until the OIG has been notified in writing that the applicable policies and procedures have been updated and added to the applicable manuals.

## SCOPE AND METHODOLOGY

To accomplish the audit objectives, the OIG identified, reviewed, evaluated and tested the internal controls related to the award and administration of contracts.

To obtain an understanding of the internal controls over these areas, policies and procedures were reviewed, including any relevant manuals, guidelines, memoranda, emails, and directives setting forth current LSC practices. LSC 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, LSC's internal control system and processes were compared to applicable laws and regulations. We assessed the reliability of computer generated data provided by LSC management by reviewing source documentation for the entries selected for review. We determined that the data were sufficiently reliable for the purposes of this report. This review was limited in scope and not sufficient for expressing an opinion on the entire system of LSC internal controls over financial operations.

To test controls and the appropriateness of contracts, we reviewed a non-statistical sample of nine contracts totaling \$630,931 selected from LSC's transaction listing by account report – consultant contracts. The sample was taken from the period July 1, 2009 through May 31, 2013, and represented approximately 37 percent of the \$1,690,982.73 disbursed for contracts other than retainer agreements with outside counsel. To assess the appropriateness of contracts, we reviewed documentation maintained in contract files, and conducted interviews of management and staff. The appropriateness of those contracts was evaluated on the basis of the LSC's contracting policies and procedures.

While 12 contracts were initially selected, 3 contracts were not reviewed for purposes of this audit. Although LSC's transactions listing indicated that the three items were consulting contracts, our review indicated they were not and thus not within the scope of our review. The first transaction was for donated consultant services, the second transaction was a relatively low dollar amount for video editing, and the third transaction was to co-sponsor a publication.

The audit fieldwork was conducted from June 13, 2013 through April 22, 2014. Our work was conducted at LSC's headquarters in Washington, DC. Documents reviewed pertained to the period July 1, 2009 through May 31, 2013.

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



## FINANCIAL & ADMINISTRATIVE SERVICES

### MEMORANDUM

**TO:** John Seeba

**FROM:** David Richardson *dlr*

**CC:** Jim Sandman  
Ron Flagg

**DATE:** June 27, 2014

**SUBJECT:** Office of Inspector General (Report No. AU09-05)

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Thank you for the opportunity to comment on your draft report on your audit of LSC's consultant contracts (Report Number AU09-05). We have reviewed the report and accept all of its recommendations.

**Recommendation 1.** Update the LSC Accounting Procedures Manual to include OFAS policies and procedures that implement the contracting requirements of the LSC Administrative Manual, Chapter 1, Parts I and III. The two manuals should be in agreement.

**Response:** The LSC Accounting Procedures Manual has been revised to include a section on the Purchase Order process and directs the user to the Administrative Manual for additional information.

**Recommendation 2.** Develop and implement a checklist to use in determining and documenting the procedural sufficiency of each consultant contract. The completed checklist for each consultant contract should be retained in the OFAS contracting files.

**Response:** A checklist has been developed. A copy of a blank form is attached, and I have included one that has been completed for a new contract.

**Recommendation 3.** The Comptroller should provide written quarterly reports to the LSC President on all consultant contracts signed during each quarter as required by the LSC Administrative Manual, Part III, Paragraph B5. The report should include the Comptroller's assessment of whether the contracting procedures outlined in the LSC Administrative Manual are being adhered to, and if not what actions are needed to correct any deficiencies.

**Response:** We will provide a memo quarterly regarding an assessment of contracting procedures that were followed, and, if procedures were not followed, we will notify the President and explain how to correct the deficiencies. An example of a quarterly memo is attached based on the May 2014 encumbrance report.

**Recommendation 4.** Establish procedures that ensure purchase orders are properly issued and processed.

**Recommendation 5.** Update the LSC Accounting Procedures Manual to include current OFAS policies and procedures for processing purchase orders.

**Response to 4 and 5:** We are in the process of revising Chapter 1 of the LSC Administrative Manual, which will affect the Accounting Procedures Manual. In the meantime, a revision to the current LSC Administrative Manual, Chapter 1, has been completed and included in the Accounting Procedures Manual. This revision describes current practices regarding issuing purchase orders and provides instruction on how to process the exception and whether there is a need for a purchase order or not.

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**Training will be provided in July to OFAS staff who process purchase orders and invoices to ensure that all of the procedures are being followed correctly.**

**Thank you for providing this information. We look to improve our internal controls, and your report and our implementation of its recommendations to us are helpful in that regard.**

**Please let me know if you need further information.**