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AUDIT ADVISORY

To: All Executive Directors
Recipient Independent Public Accountants

From: Roxanne Caruso *Roxanne Caruso*
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Subject: Common Quality Control Review Findings and Recommendations
to Ensure Independent Public Accounting Firms Conduct Rigorous
Annual Audits of LSC Grantees- Fiscal Years 2021 and 2022

Date: October 23, 2023

Legal Services Corporation (LSC) recipients are required by federal appropriations law to have an annual financial statement audit conducted by an independent public accounting (IPA) firm, which includes compliance testing. This important statutory requirement helps promote program integrity, accountability, and transparency. LSC's Office of Inspector General (OIG) provides general oversight of this process. One of our key oversight activities is to annually conduct quality control reviews (QCRs) of select IPAs of LSC recipients. This advisory presents (1) the summary results of QCRs conducted on fiscal year 2021 and 2022 recipient financial statement audits and (2) recommendations based on these results to improve the quality of LSC recipient financial statement audits. In particular, we recommend that IPAs focus on better familiarizing themselves with LSC regulations and compliance requirements, and documenting performance of the suggested audit procedures outlined in the LSC Compliance Supplement.¹ IPAs and Executive Directors should use this information in planning and conducting next year's audits. We ask that you share this advisory broadly within your organization.

We would also like to take this opportunity to remind you that the new Compliance Supplement has been issued and is effective for recipient financial statement audits with fiscal years ending on or after September 30, 2023. The 2023 Compliance Supplement

¹ The Compliance Supplement refers to Appendix A of the OIG Audit Guide for Recipients and Auditors, Compliance Supplement for Audits of LSC Recipients.

includes updated audit objectives and procedures as well as updates to the LSC regulations. The 2023 Compliance Supplement can be found [here](#).²

Background

Since 1996, LSC's annual federal appropriations acts have required that each person or entity receiving financial assistance from LSC be subject to an annual financial statement audit, conducted by an IPA. Each recipient contracts directly with an IPA to conduct the required audit in accordance with Generally Accepted Government Auditing Standards (GAGAS), Generally Accepted Auditing Standards (GAAS), Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance), and the OIG Audit Guide for Recipients and Auditors, which includes Appendix A: Compliance Supplement for Audits of LSC Recipients.

In line with federal appropriations law, the OIG provides guidance to IPAs and recipients as well as general oversight of the IPA process. Our oversight activities include conducting QCRs, which are independent reviews of financial statement audits conducted either on-site at IPAs' offices or virtually by McBride, Lock and Associates, LLC, a Certified Public Accounting firm contracted by the OIG. The primary purpose of a QCR is to determine whether the financial statement audit work, compliance audit work, and the associated review of internal controls over both financial reporting and compliance are conducted in accordance with applicable standards and OIG guidance.

Summary of Key QCR Findings

During this cycle, we conducted a total of 35 QCRs. The following are the overall results:

- Twelve met standards with no exceptions.
- Twenty-three met standards with one or more exceptions.

Based on our review of the QCR results, we found room for improvement in IPAs' analyses and documentation of recipient compliance with LSC requirements. We also found that one IPA did not fully comply with Uniform Guidance, and another did not fully adhere to Generally Accepted Auditing Standards.

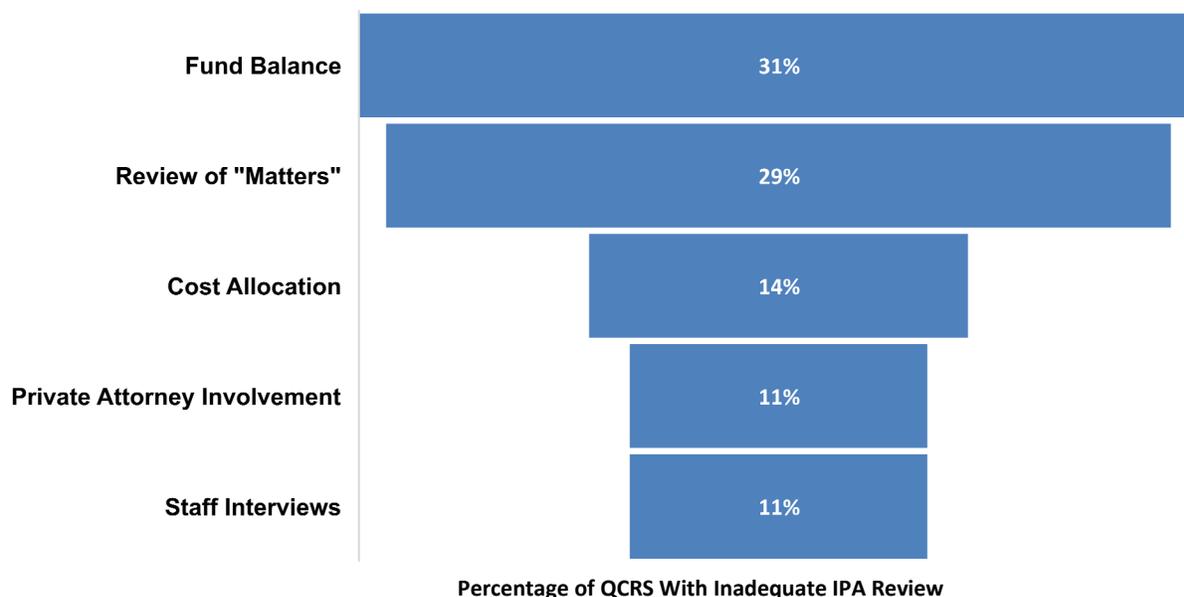
Some IPAs Did Not Adequately Review and/or Document Evaluation of Compliance with LSC Requirements

The most common issues noted in the QCRs related to IPAs inadequately applying the suggested audit procedures contained in the Compliance Supplement to evaluate recipients' compliance with LSC requirements, as well as inadequate documentation to support the IPA's conclusions and findings.

² The updated Audit Guide and Appendixes can be found here: <https://www.oig.lsc.gov/ipa-resources/audit-guidance>

The following chart illustrates the most common areas for which QCRs noted findings concerning the adequacy of the IPAs' review.

Five Most Common Areas Lacking Adequate Review



The most common LSC area lacking adequate review by IPAs concerned fund balance. LSC permits its recipients to retain fund balances on Basic Field funds up to 10 percent of LSC support from one fiscal year to the next, without obtaining approval from LSC. Fund balances of Basic Field funds exceeding 10 percent require a formal request to retain the portion of the fund balance that exceeds 10 percent. QCRs often noted issues resulting from miscalculating the prior-year carryover amount as well as improper revenue recognition. Excess fund balances are addressed in Part 1628 – Recipient Fund Balances of the Compliance Supplement.³ The Compliance Supplement includes various suggested audit procedures related to the review of carryover funds including calculating the recipient’s prior-year fund balance. Also, recipients and IPAs should be aware of LSC’s recent [Program Letter 23-2](#) which contains guidance on revenue recognition and its relation to fund balances.

Another area where we found repeated instances of inadequate review concerned “matters.” “Matters” are defined in 45 C.F.R. § 1620.2 (b) as “an action which contributes to the overall delivery of program services but does not involve direct legal advice to or legal representation of one or more specific clients.”⁴ Some IPAs attempted to document a review of “matters” in their case file testwork. However, the case file testwork analyzed during the QCRs did not provide adequate review according to the LSC definition of “matters.” The Compliance Supplement includes suggested audit procedures to review program activities that fall within the category of “matters” to ensure compliance with the recipient’s written priorities.

³ Additional information on fund balance can be found at [eCFR :: 45 CFR Part 1628 -- Recipient Fund Balances](#)

⁴ Additional information including examples can be found at [eCFR :: 45 CFR 1620.2 -- Definitions.](#)

In addition to the causes outlined above, QCR findings primarily resulted from either inadequate documentation of the efforts performed or inattention to the detail of audit procedures outlined in the Compliance Supplement. It was also noted that on occasion auditors demonstrated a lack of understanding of LSC regulations and their requirements.

One IPA's Work Did Not Adequately Demonstrate Compliance with Uniform Guidance

In one instance the major program⁵ efforts were not properly identified, and appropriate audit efforts were not performed. The IPA did not document a risk assessment of Federal applicable federal programs to determine whether they were considered "low risk." The lack of appropriate determination of major programs could potentially result in an inappropriate scope of Federal programs audited.

One IPA's Work Did Not Adequately Demonstrate Compliance with Generally Accepted Auditing Standards

In one instance, a recipient's contracted accountant provided the financial statements directly to the IPA. The IPA did not document whether the recipient accepted these statements. The absence of such acceptance would result in a lack of assurance necessary in management's representation to the auditor regarding its responsibility for the preparation and fair presentation of the financial statements.

Recommendations for IPAs to Consider in Conducting Rigorous and Efficient Annual Recipient Audits

Based on the results of our reviews, we have compiled a list of general recommendations that require IPA attention as they start conducting the next round of audits and recommendations to help IPAs ensure they address the five most common areas with QCR findings. The general recommendations are recommendations for IPAs to consider broadly when performing testwork related to the Compliance Supplement. The recommendations to address the most common findings are based on the specific issues noted in each of the areas.

LSC recipients are unique entities and are governed by federal regulations and LSC guidance. By taking these recommendations into account, IPAs can minimize the risk of undetected or unintentional noncompliance with these regulations and guidelines, by both the auditors and the LSC recipients they serve. Additionally, implementing these recommendations can better ensure IPAs produce more rigorous audits and can improve audit and cost efficiencies by reducing the amount of follow up documentation needed in future QCRs.

⁵ A major program is defined by 2 C.F.R. § 200.518 as a Federal award that is determined through Uniform Guidance specified risk assessment processes that are subject to more detailed audit coverage.

General Recommendations That Require IPA Attention

We recommend that IPAs:

1. Ensure that financial statement and compliance audit work, as well as the associated review of internal controls, are conducted in accordance with applicable standards and OIG guidance.
2. Gain a thorough understanding of the LSC program and the nature of LSC requirements during the planning phase of the audit to adequately evaluate compliance with the requirements and document the results.
3. **Completely** perform the suggested audit procedures contained in the Compliance Supplement and **fully document** their assurance that they have addressed each direct and material Compliance Supplement element.

Recommendations to Address the Most Common QCR Findings

We offer the following recommendations to address the most commonly identified findings, based on QCRs conducted in fiscal years 2021 and 2022.

1. *Fund Balance* – Ensure that the recipient has adequate controls, including an adequate analysis of prior period carryover funds, to determine whether an excess fund balance waiver should be requested from LSC. Additionally, if a waiver has been requested, ensure that the recipient accounts for expenditures in compliance with the requirements of the waiver. Document the results.
2. *Review of “Matters”* – Strengthen testing of recipients’ compliance with Part 1620 – Priorities in Use of Resources. Testing should include the consideration of “matters,” as well as non-priority or emergency cases as well as the review of certifications completed by intake personnel.
3. *Cost Allocation* – Obtain, review, and test recipients’ processes for allocating costs and income and thoroughly document the results.
4. *Private Attorney Involvement* – Obtain the recipient’s private attorney involvement plan and review their processes to ensure compliance with the plan; and document the results.
5. *Staff Interviews* – Ensure that all Compliance Supplement parts are considered and evaluated when performing staff interviews. The results of these interviews should be adequately documented in the IPA’s workpapers.

We appreciate your close attention to these recommendations. Our ultimate aim is to help ensure that annual audits are rigorously designed and conducted to promote accountability, transparency, and integrity in the expenditure of federal funds. If you have any questions regarding this Advisory, please contact me by phone at 202-295-1582 or by email rcaruso@oig.lsc.gov. Thank you for your attention to these matters.