LEGAL SERVICES CORPORATION

Office of
Inspector General

Semiannual Report to the Congress
April 1, 2012 – September 30, 2012

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TO THE BOARD OF DIRECTORS OF THE LEGAL SERVICES CORPORATION AND TO THE UNITED STATES CONGRESS

A MESSAGE FROM THE INSPECTOR GENERAL

I am pleased to submit this report on the activities and accomplishments of LSC's Office of Inspector General (OIG) for the period April 1, 2012 through September 30, 2012.

During this reporting period we conducted audits relating to the adequacy of internal controls, particularly with respect to grantee financial operations, and also continued our audits of grantee expenditures and accomplishments under LSC's Technology Initiative Grant program. Audits completed during the period identified a total of over $1.4 million in questioned costs.

This period also marked the beginning of the second year of our initiative to provide enhanced oversight of the independent audits required annually of LSC grantees. All firms performing grantee audits are now subject to a Quality Control Review (QCR) at least once every four years. During the period we issued 10 QCRs, 5 of which triggered a need for further review.

We opened 6 new investigations and closed 23 investigations during the reporting period. Among the investigations were criminal cases involving fraudulent activity and financial irregularities by grantee employees, and regulatory matters, including allegations of improper lobbying and solicitation of clients by grantee personnel. In a case arising from an earlier OIG investigation, a former grantee executive director, convicted for his role in the theft of nearly $160,000 in federal grant funds, was sentenced to a term of imprisonment and ordered to pay restitution. In another case, a former grantee employee was convicted and sentenced on a guilty plea to theft of over $10,000 from a grantee.

We continued to emphasize outreach and educational initiatives as part of our ongoing efforts to help prevent fraud and abuse in LSC-funded programs. In addition to maintaining an active schedule of fraud awareness briefings (including presenting a live webinar for those who were not able to attend an in-person briefing), we continued our pilot program of regulatory vulnerability assessments, working on-site with grantees to identify internal control or compliance weaknesses.

I wish to express my continuing appreciation to LSC's Board of Directors for the interest and support they have shown for the work of the OIG. I also remain deeply appreciative to the Congress for its steadfast support of this office.

Sincerely,

Jeffrey E. Schanz
Inspector General
October 31, 2012

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OFFICE OF INSPECTOR GENERAL OVERVIEW

The LSC Office of Inspector General operates under the Inspector General Act of 1978, as amended, 5 U.S.C. App. 3. The OIG has two principal missions: (1) to assist management in identifying ways to promote economy and efficiency in the activities and operations of LSC and its grantees; and (2) to prevent and detect fraud and abuse.

The OIG's primary tool for achieving these missions is objective and independent fact-finding, performed through financial and other types of audits, evaluations, and reviews and through investigations into allegations of wrongdoing. Its fact-finding activities enable the OIG to develop recommendations to LSC, Congress, and grantee management for actions that will correct problems, better safeguard the integrity of funds, improve procedures, and otherwise increase the economy, efficiency and effectiveness of LSC programs.

The OIG is also tasked with ensuring the quality of audits of LSC and its grantees, conducted by independent public accountants, and with reviewing proposed and existing regulations and legislation affecting the operations and activities of LSC and the programs it funds.

In addition, since 1996, LSC's annual appropriations have directed that grantee compliance with legal requirements be monitored through the annual grantee audits conducted by independent public accountants, under guidance developed by the OIG. Congress has also specified that the OIG has authority to conduct its own reviews of grantees.

The OIG is headed by the Inspector General, who reports to and is under the general supervision of the LSC Board of Directors. The IG has broad authority to manage the OIG, including setting OIG priorities and activities, and to hire OIG personnel and contractors.

To ensure objectivity, the IG Act grants the LSC IG independent authority to determine what audits, investigations, and other reviews are performed, to gain access to all necessary documents and information, and to report OIG findings and recommendations to LSC management, its Board of Directors, and Congress.

The IG Act also prohibits LSC from assigning to its IG any of LSC’s own "program operating responsibilities." This means that the OIG does not perform functions assigned to LSC by the Legal Services Corporation Act, 42 U.S.C. §§2996 *et seq.*, other than those transferred to the OIG under the IG Act and those otherwise assigned by Congress, for example in LSC’s annual appropriations acts.

The IG reports serious problems to the LSC Board of Directors and must also report to appropriate law enforcement authorities when, through audit, investigation, or otherwise, the IG has found that there are reasonable grounds to believe that a crime has occurred. The OIG is not an "arm" of the Congress, as is the Comptroller General, but is required by law to keep the Congress informed through semiannual reports and other means. The IG also provides periodic reports to the board and management of LSC and, when appropriate, to the boards of directors and management of LSC grantees. Some of these reports will be specific (*e.g.*, an audit of a particular grantee or an investigation of a theft or embezzlement), while others will be of broader application and may address more general or systemic issues.

To be effective, the OIG works cooperatively with the board and management of LSC, seeks their input prior to choosing topics for OIG review, and keeps them informed of OIG activities. Within their different statutory roles, the OIG and LSC management share a common commitment to improving the federal legal services program and increasing the availability of legal services to the poor.

AUDITS

During this reporting period, the OIG issued five audit reports, discussed below. The five reports identified over $1.4 million in questioned costs. In addition, the OIG issued two draft audit reports to grantee management for comment. Work in progress at the end of the reporting period included audits at four other grantees. Three of these audits were in the draft report stage; field work was in progress for the remaining grantee. Additional audits were in the planning stage.

The OIG has responsibility for overseeing the independent public accountant (IPA) audits performed annually at each grantee. During the reporting period, the OIG reviewed 112 IPA reports, with fiscal years ending from December 31, 2011 through March 31, 2012.

The OIG also issued 10 quality control review (QCR) reports this period under our QCR initiative. We are in the process of scheduling and conducting an additional 25 QCRs. The goal of this initiative is to improve the overall quality of the audits and to ensure that all audits are conducted in accordance with applicable standards and with the guidance provided by the OIG. The OIG required the IPAs for five of the audits reviewed to provide further documentation or to complete additional audit work. We will be evaluating the information provided and monitoring the IPAs' corrective actions.

During the last reporting period 15 QCRs identified deficiencies for which we required IPAs to provide additional documentation supporting the work performed or to perform additional audit work. This period, we evaluated the documentation submitted by the IPAs and determined that the documentation adequately demonstrated that the deficiencies identified in the 15 QCRs had been corrected.

All federal IG audit organizations are required by government auditing standards to undergo a peer review every three years. Each OIG audit office also conducts a peer review of another federal OIG every three years. The purpose of a peer review is to provide an opinion on whether the reviewed audit organization has a system of quality control that has been suitably designed and complied with to provide reasonable assurance that applicable professional standards are being met in all material respects. During this reporting period, the OIG audit staff conducted a peer review of the Securities and Exchange Commission OIG audit organization.

Texas RioGrande Legal Aid, Inc. – Audit of Selected Internal Controls

The OIG assessed the adequacy of selected internal controls in place at Texas RioGrande Legal Aid, Inc. (TRLA) related to specific grantee operations and oversight, including program expenditures and fiscal accountability.

The OIG found that the grantee's internal controls needed to be strengthened. While many of the controls were generally adequately designed and properly implemented as the controls related to specific grantee operations and oversight, some controls needed to be improved and formalized in writing. The grantee needed to place more emphasis on establishing, documenting, and enforcing all internal controls.

Specific findings included:

- The cost allocation system was not adequately documented. Non-personnel central office administrative and management overhead expenses were not allocated to the public defender programs, with the result that LSC funds may have been used to subsidize prohibited activities.
- The method used to allocate costs for six separate migrant grants was not based on actual work conducted in each of the six service areas.
- The grantee needed to enforce policies and procedures for credit card purchases, filing of travel vouchers, and obtaining prior approval for travel.
- Policies and procedures needed to be fully developed, documented, and implemented with respect to soliciting and awarding contracts, reimbursing employees for cell phones, and prohibiting the use of LSC funds to purchase alcoholic beverages.

The OIG made eight recommendations. Three recommendations addressed issues with the cost allocation system: the need to ensure that the system is fully documented; the need to ensure that a fair share of central office costs are allocated to the grantee's public defender programs; and the need to develop a cost allocation system for migrant grants that accurately accounts for the expenditure of LSC funds for each grant and ensures that LSC funds provided are spent for services applicable to the respective service area. Two recommendations concerned the need to enforce policies and procedures in place for credit card use and out-of-town travel. Finally, three recommendations addressed the need for written policies and procedures with respect to: contracting and consulting agreements; the use and reimbursement for cell phones and other electronic devices; and the prohibition on using LSC funds to purchase alcoholic beverages.

The OIG considered grantee management's planned actions to be responsive to six of the eight recommendations. The OIG considered the grantee's response to one recommendation as partially nonresponsive and to another recommendation as nonresponsive. Both were referred to LSC management for resolution. All eight recommendations will remain open until the respective grantee management actions are completed and appropriate written notification is provided to the OIG.

For the first recommendation, grantee management disagreed that a cost allocation for migrant grants needed to be developed to accurately account for the expenditure of LSC funds for each migrant grant and ensure that LSC funds provided are expended for services applicable to the respective service area. Grantee management stated that because of the nature and the relatively small amount of the grants it would be "…virtually impossible to guarantee that the grant in any given state in any given year will exactly match the operations and service provided in that state." However, grantee management did state that it will request LSC management approval for pooling the funding of the migrant grants.

For the second recommendation, grantee management did not cite any corrective action planned with regard to ensuring that credit card receipts are submitted. Grantee management responded to a portion of the recommendation by stating that the executive director adds adequate explanatory information on the credit card billing to support his charges, but he does not file a travel reimbursement form because he does not seek reimbursement for his travel expenses. However, the executive director would file a travel reimbursement request if he did seek such reimbursement.

The OIG disagreed with grantee management's comments for these latter two recommendations. While the grantee will request that LSC management approve the pooling of funds for the six migrant grants, the grantee's proposal does not address the finding that the grantee's allocation methodology for migrant grants was inadequate. We concluded that regardless of whether LSC management approves pooling of the funds in question, the grantee needed to implement an acceptable allocation methodology for those funds. We also reported that grantee management's proposed action did not address the need to ensure that credit card receipts are submitted by all staff, and that all employees, including the executive director, file a travel voucher as required by the grantee's policies. The grantee's employee handbook provided no exceptions for filing a voucher whether the expense is paid to the employee or to a vendor.

Inland Counties Legal Services, Inc. – Audit of Selected Internal Controls

The OIG assessed the adequacy of selected internal controls in place at Inland Counties Legal Services (ICLS), related to grantee operations and oversight, in particular those relating to program expenditures and fiscal accountability and compliance with selected LSC regulations.

We found that although some controls needed to be strengthened, internal controls reviewed at ICLS were generally adequate. Disbursements tested were, for the most part, found to be adequately supported, allowable, and properly allocated to LSC. Internal controls over compliance with the provisions of 45 C.F.R. Part 1617 were found to be adequate. We did find, however, several issues that needed management attention, as discussed more fully in the report.

The OIG found that:

- Over $1.3 million of LSC funds were used to provide stipends and other benefits during FYs 2006, 2007, 2009, and 2010, that, in our opinion, were not reasonable and necessary under the circumstances.
- The grantee's accounting manual was outdated and did not reflect many of the practices currently in place. The manual was adopted in 1992 and an updated official version has not been approved by the board.

- The grantee did not have adequate practices or written policies and procedures in place for its Loan Repayment Assistance Program (LRAP), to ensure that employees use the funds provided to pay off outstanding student loan balances.

As a result of our audit, the OIG questioned $1,367,480 charged to LSC funds because the grantee provided stipends to employees that the OIG identified as not being reasonable and necessary. The questioned costs were referred to LSC management for review.

The OIG made four recommendations. One of the recommendations was related to the stipend issue and suggested that ICLS develop and implement both short-term and long-term plans to address the staffing shortages which resulted in excess funding being available at the program. We also identified a number of potential methods that could be used to directly address the problems the grantee was facing in this regard. The second recommendation was that ICLS management should update their accounting manual by preparing written policies and procedures that document current practices in use and include all processes required by LSC's Accounting Guide. The remaining two recommendations addressed the LRAP issue. First, we recommended that the use of LRAP funds be better controlled by either (a) performing analyses of outstanding employee loan balances from year to year to determine whether employees are actually paying off their loan balances; or (b) having the program make payment directly to the lenders to ensure employee loans are being paid off. Finally, we recommended strengthening the LRAP program by (a) specifying the types of loans that are eligible; (b) establishing time limits for being in the program and a maximum amount an employee can receive; and (c) requiring a service commitment as a condition of receiving and keeping LRAP funds.

While grantee management strongly disagreed with the finding regarding year-end stipends and the related questioned costs, grantee management's actions taken or planned were responsive to all four recommendations. The four recommendations will remain open until all stated grantee management actions are completed.

In disagreeing with the finding on stipends, grantee management stated the OIG's audit "found ICLS to have adequate internal controls that are carefully followed." They also stated that "the stipend and benefits disbursements did not violate any rule or regulation." ICLS management explained that the stipends and other benefits were provided to help attract and retain an underpaid staff. They further explained that the stipends and other benefits were not given to avoid seeking a waiver under LSC's fund balance regulation, but were part of fiscal planning which had been in place for many years. The comments indicated that historically the ICLS Board of Directors has approved stipends and other benefits, and that the board was presented with all the relevant financial information and fully informed about potential amounts available at year-end for the proposed stipends.

The OIG disagreed with the grantee's comments; we did not agree that the comments provided adequate justification for the payment of stipends. We noted that we questioned the cost of the stipends based on the reasonableness and necessity of the payments, not on the basis of a lack of adequate documentation or a violation of law.

We also noted that the documentation provided by grantee management clearly indicated that the amount of money used for the stipends was tied directly to reducing the LSC fund balance carryover to under the 10 percent threshold (the point at which the grantee would be required to return the excess funds or request a waiver from LSC and obtain approval for a "spend-down" plan).

Management's comments cited many compensation figures, including averages for legal aid attorneys in California, averages for LSC funded programs in California, and averages based on years of experience. In reviewing management's response, we acknowledged there may be some merit to the discussion regarding the disparity in pay for attorneys in California. We noted, however, based on management's comments that the stipend was intended for staff retention, that the OIG questioned the structure of the stipend, and not necessarily the stipend itself.

We also observed that the stipend program was in place during a significant economic downturn within the state, as well as the country as a whole. Law firms were downsizing and many recent law school graduates were having difficulty finding employment. A well designed hiring plan would have leveraged these situations while simultaneously taking into account staff attrition. No evidence was provided by the grantee to indicate that the hiring difficulties encountered by the grantee had been mitigated by the use of this stipend program.

South Jersey Legal Services, Inc. – Audit of Selected Internal Controls

The OIG assessed the adequacy of selected internal controls in place at South Jersey Legal Services, Inc. (SJLS) related to grantee operations and oversight, in particular those relating to program expenditures, fiscal accountability, and compliance with selected LSC regulations.

The OIG found that internal controls reviewed and tested at SJLS were generally adequate, however some controls and practices needed to be formalized and documented. We reported that disbursements tested were adequately supported, allowable, and appeared to be properly allocated to LSC funds. We found that controls over the regulations reviewed were designed in a manner expected to ensure compliance with selected provisions of the LSC Act and regulations.

We reported that the grantee's current practices involving internal management reporting and budgeting, contracting, cost allocation, salary advances, and property inventory were not documented in their accounting manual, as required by the LSC Accounting Guide and GAO guidelines. We did note, however, that our tests did not disclose any deficiencies in the actual practices used by the grantee in these areas. Our test of the practices used indicated that these practices were generally in accordance with the "Fundamental Criteria" contained in the LSC Accounting Guide.

The OIG recommended that grantee management update its Accounting Procedures

Manual by incorporating current practices in use into the manual. Grantee management agreed with the recommendation. The recommendation will remain open until the OIG receives written notification that the revised accounting manual has been updated and issued.

Audits of Technology Initiative Grants

As noted in previous reports to Congress, the OIG is conducting audits of grantees receiving Technology Initiative Grants (TIGs). This initiative is a follow-on to our FY 2011 audit report on the TIG program at LSC headquarters. The audits focus on whether TIG expenditures were allowable and supported, and whether the stated purposes of the TIGs have been achieved.

As a condition of receiving a TIG, each grantee executes a grant assurance document, undertaking to comply with specified terms and conditions of the grant. TIG assurances reference LSC regulations and guidelines that describe documentation requirements for supporting costs. The accurate determination of TIG project costs is important since TIG assurances also require that funds provided in excess of project costs be returned to LSC or reprogrammed to other projects with the approval of LSC.

Because LSC does not normally maintain information on the actual expenditures charged to these grants, the OIG obtained expenditure information from grantees on completed and terminated TIGs. To determine which TIGs to review the OIG analyzed the information provided on 120 grants, valued at a total of just under $9 million, awarded to 65 separate grantees. We will conduct a field visit to the grantee for each grant selected for review. Since the TIGs selected for review have been closed, our reports are directed to LSC management rather than to the individual grantee. We do, however, provide our draft findings to grantee management and invite their comments as part of our report preparation process.

Our reports provide an opinion on the expenditures charged to the grant, refer any questioned costs to LSC management, and render a conclusion as to whether the stated purpose of the grant had been accomplished. In addition, to the extent we can identify potential improvements to the overall program or areas for strengthening grant oversight, appropriate recommendations will be made to LSC management. This reporting period the OIG issued two reports, which are described below.

Examination of Expenditures Incurred for the Performance of TIGs Awarded to Southeast Louisiana Legal Services

The OIG examined expenditures incurred for the performance of TIGs awarded to Southeast Louisiana Legal Services (SLLS). The objectives of the examination were to determine whether the expenditures for three SLLS TIGs totaling $227,315 were allowable and supported, and whether the stated purposes of the TIGs were achieved.

The OIG concluded that the stated purposes of the three TIGs appeared to have been met. However, the OIG also concluded that for two grants, $55,741 of personnel and fringe benefit expenditures were not supported by adequate documentation as required by TIG assurances.

The grantee's response indicated, among other things, that LSC management represented the TIGs as "milestone" grants and not "cost reimbursement" grants. However, we noted that TIG assurances require compliance with LSC regulations, guidelines, and directives that do provide specific written instructions about timekeeping requirements. As a result of the audit, the OIG referred $55,741 in questioned costs to LSC management.

Examination of Expenditures Incurred for the Performance of TIGs Awarded to Legal Services of Southern Missouri

The OIG examined expenditures incurred for the performance of a TIG awarded to Legal Services of Southern Missouri (LSSM). The objectives of the examination were to determine whether the expenditures for the TIG totaling $124,383 were allowable and supported, and whether the stated purpose of the TIG was achieved.

The OIG concluded that the stated purpose of the TIG appeared to have been met. However, the OIG also concluded that $3,659 of personnel expenditures were not supported by adequate documentation as required by TIG assurances.

The grantee's response indicated among other things that contemporaneous time records were kept and that the actual cost exceeded the amount charged to the TIG. We reviewed the additional supporting documentation provided with LSSM's written response but continued to consider the cost to be questioned, finding that the cost records and analysis did not meet the requisite standard. As a result of the audit, the OIG referred $3,659 in questioned costs to LSC management.

Statistical Summary

Audit Reports

Open at beginning of reporting period 5

Issued during reporting period 5

Closed during reporting period 4

Open at end of reporting period 6

Recommendations to LSC Grantees

Pending at beginning of reporting period 24

Issued during reporting period 13

Closed during reporting period 12

Pending at end of reporting period 25

Recommendations to LSC Management

Pending at beginning of reporting period 11

Issued during reporting period 0

Closed during reporting period 11

Pending at end of reporting period 0

Oversight of IPA Audits

Independent Audits of Grantees

Since 1996, LSC's annual appropriations acts have required that each person or entity receiving financial assistance from the Corporation be subject to an annual audit, to be conducted by an independent public accountant (IPA). Each grantee contracts directly with an IPA to conduct the required audit in accordance with generally accepted government auditing standards and the OIG Audit Guide for Recipients and Auditors (including the Compliance Supplement), which incorporates most requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

The OIG provides guidance to the IPAs and grantees, as well as general oversight of the IPA process. Our oversight activities include desk reviews and a recently enhanced program of quality control reviews.

Desk Reviews of IPA Reports

The OIG conducts desk reviews of all IPA reports issued to grantees. This process enables us to identify and forward to LSC management significant IPA findings that require management's attention. We also track whether recommendations have been acted upon and appropriate actions taken by the grantee. In addition, we use information from this review of 100% of IPA reports as part of our risk assessment and planning processes, identifying potential problems or concerns that may warrant follow-up via audit, investigation, or other review.

Quality Control Reviews

The OIG is in the second year of its QCR initiative. The QCR initiative is a comprehensive program under which all IPA firms performing grantee audits will be subject to at least one QCR every four years. The QCRs determine whether the IPA's financial statement audit work, compliance audit work, and the associated review of internal controls over both financial reporting and compliance were conducted in accordance with applicable standards and in compliance with the instructions issued by this office. The reviews are conducted by a CPA firm under contract to the OIG. The contractor also identifies issues that may require additional attention or any additional audit work by the IPA under review. The QCR program is proving to be a valuable tool in assessing the reliability of audits and in ensuring IPAs are fully aware of the specific requirements for auditing an LSC grantee.

Quality Control Review Results

This reporting period, the OIG issued 10 QCR reports to IPAs. The OIG issued 29 QCRs last reporting period, for a combined total of 39 QCRs for the fiscal year. Also, as of the end of this reporting period, another 11 QCRs were in process.

Of the 10 QCRs issued this reporting period, five QCRs identified deficiencies that required the IPAs to provide the OIG with additional documentation to support the conclusions reached. For four QCRs, additional documentation was not required at this time, but the IPAs needed to ensure that additional steps were taken on future audits of LSC grantees. For one QCR, no deficiencies were noted. The OIG will review all additional documentation required to be provided by the IPAs to ensure that LSC grantees receive an acceptable audit.

During the last reporting period, 15 QCRs identified deficiencies for which IPAs were required to provide the OIG additional documentation supporting the work performed or to perform additional audit work. This reporting period, we evaluated the documentation submitted by the IPAs and determined that for all 15 QCRs, the documentation provided adequately demonstrated that the deficiencies identified had been corrected.

Follow-up Process

LSC's annual appropriations acts have specifically required that LSC follow-up on significant findings identified by the IPAs and reported to the Corporation's management by the OIG. IPA audit reports are submitted to the OIG within 120 days of the close of each grantee's fiscal year. As noted above, through our desk review process the OIG reviews each report and refers appropriate findings and recommendations to LSC management for follow-up. LSC management is responsible for ensuring that grantees submit appropriate corrective action plans for all material findings, recommendations, and questioned costs identified by the IPAs and referred by the OIG to management.

After corrective action has been taken by the grantee, LSC management advises the OIG and requests that the finding be closed. The OIG reviews management's request and decides independently whether it will agree to close the finding.

Review of Grantees' Annual Audit Reports: IPA Audit Findings

In order to provide more complete information in our semiannual reports to Congress, the OIG customarily includes a summary of significant findings and the status of follow-up on significant findings reported by the IPAs as part of the grantee oversight process. The audit reports and the findings identified below reflect the work of the IPAs, not the OIG.

During the reporting period, the OIG reviewed 112 IPA audits of grantees with fiscal year ending dates from December 31, 2011 through March 31, 2012. These audit reports contained 73 findings. The OIG determined that 42 findings were not significant or that corrective action had already been completed and closed the findings. The remaining 31 findings were referred to LSC management for follow-up. The tables below present information on those findings.

Summary of Findings for Grantee Audit Reports Reported in Grantee Financial Statement Audits with Fiscal Years Ending December 31, 2011 through March 31, 2012

Total Number of Findings Referred	31
Number of Findings with Corrective Action Accepted by LSC Management	14
Number of Findings Awaiting LSC Management Review	17

Types of Findings Referred to LSC Management for Follow-up

Category	Number of Findings
Financial Transactions and Reporting	9
Missing Documentation	7
Policies and Procedures (establishment/compliance)	7
Timekeeping	5
Reporting Issues	1
Subgrant Issues	1
Physical Inventory	1
TOTAL	31

INVESTIGATIONS

The OIG opened six investigations during this reporting period. These included three criminal investigations, one compliance matter, one fraud vulnerability assessment, and one regulatory vulnerability assessment. The criminal investigations included allegations of fraudulent activity and financial irregularities. The compliance investigation included allegations of violations of LSC statutes and regulations involving matters such as lobbying and solicitation of clients.

During the reporting period the OIG closed 23 investigations. These included 10 criminal investigations, six compliance matters, two fraud vulnerability assessments, and five regulatory vulnerability assessments. The OIG also issued two Inspector General subpoenas in connection with our ongoing work.

Criminal Proceedings

Former Grantee Executive Director Sentenced for Theft of Government Funds

The former executive director of U'una'i Legal Services Corporation of American Samoa, a now-defunct LSC grantee, was sentenced to five-months imprisonment, followed by three years of supervised release, and ordered to pay $31,292 in restitution for his role in the theft of $159,763 from the grantee. The executive director, office manager, and the office manager's daughter, who also was employed at the program, previously pled guilty to fraudulently diverting federal grant funds. They admitted making and receiving unlawful payments from the grantee, including unlawful "salary advances" in excess of their approved salaries. The office manager's and daughter's sentences were reported in the prior reporting period.

Former Grantee Employee Convicted and Sentenced for Theft

A former payroll specialist at an LSC grantee was convicted on a plea of guilty to one count of theft and received a five-year suspended sentence and three years of supervised probation as a result of her scheme to defraud the grantee of $10,350. The defendant has paid full restitution to the grantee. The scheme began when the defendant identified part-time employees at the LSC grantee who did not work every pay period. For those periods when an employee did not work, the defendant entered work hours for them into the payroll system and then changed their direct deposit information to hers. Even though pay statements were generated for the part-time employees, the defendant concealed her activities by intercepting the statements when they were delivered to the office. Since the employees had not worked during those periods they thought nothing was amiss when they received no statement. To strengthen controls, the program enacted a policy requiring employee notification by e-mail whenever there is any change in their payroll deposit information.

Personnel Actions

Grantee Employee Admits to Improperly Enrolling Boyfriend for Grantee-Paid Healthcare Benefits

The OIG received an anonymous hotline complaint alleging that the director of human resources at an LSC grantee improperly included her boyfriend on her employee medical plan as a domestic partner. The complaint further alleged that the employee's boyfriend was married to another woman at the time he was covered under the medical plan and that the employee knew of the marriage. The grantee's medical plan excludes individuals from coverage as an employee's domestic partner if they are currently married to a third person. The OIG conducted an investigation and determined that over a one-year period the grantee spent $3,537 more in health insurance premiums for the boyfriend than it would have spent to cover the employee only. During an interview with the OIG, the employee admitted to knowing that her boyfriend was married. The employee signed a promissory note to reimburse the grantee the full amount owed through payroll deductions over a three-year period and disciplinary action was taken by the grantee against the employee.

Proactive and Preventive Initiatives

The OIG maintains an active fraud prevention program, engaging in a variety of outreach and educational efforts intended to help protect LSC and its grantees from fraud and abuse. We regularly conduct fraud awareness briefings, fraud vulnerability assessments, and regulatory vulnerability assessments, as described below, and provide fraud alerts and other information that we believe will help increase grantees' awareness of potential vulnerabilities.

Fraud Awareness Briefings

Fraud awareness briefings (FABs) are presented by OIG investigators and cover topics such as who commits fraud, why people commit fraud, how fraud can be prevented, how fraud can be detected, and what to do if fraud is suspected.

While individuals at LSC-funded programs may be generally aware that fraud and abuse can occur at any organization, they may not be aware of the potential for such incidents to occur "close to home," within their own programs. Moreover, program staff often may think that if there is any such wrongdoing, it must be minimal. Our briefings highlight the unfortunate truth that in recent years a number of LSC-funded programs have been victimized by frauds involving hundreds of thousands of dollars, and even in one case the diversion of over a million dollars in grant funds. The FABs describe common types of fraud, with particular focus on the various schemes that have been perpetrated against LSC grantees and the conditions that helped facilitate the losses. The briefings aim to foster a dialogue with staff and to engender suggestions for ways to help protect their own programs from fraud and abuse.

LSC grantees are invited to request a fraud awareness briefing at a time and place convenient to them. We make every effort to accommodate requests as promptly as possible. We encourage attendance by all program staff and welcome the grantee's board members, their IPAs, and other interested parties.

This reporting period the OIG conducted 20 on-site fraud awareness briefings for LSC-funded programs in Florida, Iowa, Maryland, Massachusetts, Michigan (two), New Jersey (three), New York (four), Ohio (two), Pennsylvania, and Texas (four).

Fraud Awareness Briefing via Webinar

The OIG conducted a live webinar of the fraud awareness briefing usually offered in person to LSC grantees. All LSC grantee executive directors were sent an email invitation, which encouraged them to invite their staff, board members, and outside auditors. The webinar was viewed by 121 attendees representing 55 LSC grantees, including 24 executive directors, five IPAs, and four board members.

Fraud Vulnerability Assessments

The OIG's fraud vulnerability assessments (FVAs) are conducted on-site at individual grantee's offices. They consist of a focused document review in any area considered weak or prone to abuse, as well as a review of grantee internal control policies and the degree to which those policies are observed in practice. We also brief the executive director and principal financial officer on fraud detection and prevention measures keyed to their particular program. The FVAs can help grantees identify both existing vulnerabilities and potential problem areas.

We continued our project to analyze per capita costs in program travel and office supply expenditures (areas that have often been focal points for diversion of program funds), and to conduct FVAs at programs with apparent anomalies in their spending patterns. Project findings are incorporated into the FVA program on an on-going basis.

Two FVAs were completed during the reporting period, including one that was begun during the prior period.

Regulatory Vulnerability Assessments

During the reporting period, the OIG continued the pilot program of regulatory vulnerability assessments (RVAs). RVAs are conducted on-site at individual grantee's offices. This initiative was triggered by our experience in recent years in investigating numerous financial frauds in which grantees have been victimized. We often found that the failure to comply with, or laxity with respect to, certain LSC regulations, grant assurances, provisions of the Accounting Guide, and case documentation and reporting requirements (as set forth in the Case Service Report Handbook) contributed to an environment that increased the potential for fraud. This was also, in part, the subject of an OIG fraud alert (September 30, 2011), highlighting common internal control weaknesses and pointing out that compliance with specified requirements could help prevent several recurring types of fraud. We believe that by focusing on certain key areas, in addition to identifying potential problems from a strictly regulatory compliance point of view, grantees might also benefit by applying the classic "ounce of prevention" to areas where there is the potential for broader financial vulnerabilities.

The pilot program consists of six RVAs. Five RVAs were opened during the prior reporting period and were completed this period. The field work on the final pilot RVA was conducted this period; the report will be completed in the next period, along with an evaluation of the overall pilot. RVA results are provided to LSC grantee executive directors as well as LSC management, as appropriate.

Hotline

The OIG maintains a Hotline for reporting illegal or improper activities. Information may be provided by telephone, fax, email, or mail. Upon request, a provider's identity will be kept confidential. Reports may also be made anonymously. During this reporting period, the OIG received 80 Hotline contacts (compared to 98 for the previous period). Of these matters, 17 were referred to LSC management for follow-up; 4 were opened as investigations; 3 are open pending further inquiry; and the remaining 56 were closed.

Statistical Summary

Investigative Cases

Open at the beginning of period	24
Opened during the period	6
Closed during period	23
Open at the end of period	7

Prosecutorial Activities

Guilty pleas	1
Sentencing	2

Investigative Activities

Inspector General subpoenas issued	2

OTHER OIG ACTIVITIES

Review of Proposed Legislation, Regulations, and Policy

Pursuant to the IG's statutory responsibilities, the OIG reviews and, where appropriate, comments on statutory and regulatory provisions affecting LSC and/or the OIG, as well as LSC interpretive guidance and internal policies and procedures.

The most significant regulatory matter the OIG addressed this period concerned proposed amendments to LSC's enforcement mechanisms that would lengthen maximum available suspension periods, authorize limited reductions in funding in cases of substantial noncompliance, and permit the imposition of special grant conditions during a grant term. The OIG has maintained a long-standing interest in this subject matter, having made comparable recommendations to the board of directors and LSC management at various times over the past 10 years.

LSC published its proposed amendments in a January 31, 2012, Notice of Proposed Rulemaking (NPRM). On August 7, 2012, it published primarily technical modifications of its proposal in a Further Notice of Proposed Rulemaking (FNPRM). With limited reservations, the OIG commented favorably on both the NPRM and FNPRM and recommended adoption of the proposed amendments. The OIG believes the regulatory changes contemplated by the NPRM will increase LSC's flexibility as a grant administrator and go a long way toward remedying shortcomings in LSC's existing enforcement mechanisms.

The OIG also provided the Operations and Regulations Committee of the LSC Board of Directors with a memorandum detailing our concerns regarding a proposal to issue interpretive guidance that would alter the application of LSC's subgrant rule, 45 C.F.R. Part 1627. LSC had previously maintained that certain third-party payments made with Technology Initiative Grant (TIG) funds were not subgrants because the recipients of those payments were not providing legal services. The OIG's memorandum included a comprehensive analysis of the text of the regulation, the regulatory history, and LSC's governing statutes, and concluded that Part 1627 was intended to apply to a wide range of the grants LSC is authorized to make and to reach third-party payments made from LSC grant funds to carry out the purposes of those grants. Building on a recommendation made in an earlier OIG audit report, the memorandum explained that should LSC desire to oversee the third-party payments in question as contracts rather than subgrants, and thereby to exempt such payments from treatment as subgrants under the TIG program, it would be inappropriate to proceed simply via interpretive guidance; because the action would require substantial changes to the existing rule, we concluded, the text of Part 1627 should be amended through the normal regulatory process.

Litigation

On November 14, 2011, the United States District Court for the District of Columbia issued an order granting the OIG's petition for enforcement of a subpoena it had issued to California Rural Legal Assistance (CRLA). The court held that the OIG's subpoena was issued for a lawful purpose and that the information sought was reasonably relevant to the OIG's investigative purpose. The court also concluded that OIG's proposed review protocol could allow for adequate privilege review of the electronic data sought by the subpoena without overburdening CRLA. Subject to a protective order, the court enforced the subpoena as narrowed by agreement of the parties in the course of litigation and as requested by the OIG.

On December 13, 2011, CLRA appealed the district court's order granting enforcement of the OIG's subpoena. On January 12, 2012, the OIG filed a cross-appeal. Briefing of the case will be complete on January 9, 2013.

Advisory Memoranda

During the reporting period, the OIG issued an advisory memorandum to management entitled, *Workplace Safety and Security Follow-up*. This advisory followed-up on a 2006 OIG advisory memorandum entitled, *Workplace Safety and Security Concerns.* The OIG conducted a review of the issues identified in the previous advisory and issued six further recommendations for management to consider. To date, LSC has fully implemented four of the six recommendations. Management has advised they have taken steps to facilitate implementation of the remaining two recommendations, which require building management's action.

Board of Directors' Strategic Plan

During the reporting period, the OIG provided comments in response to the LSC Board of Directors' solicitation of comments on its draft Strategic Plan for 2012-2016. We provided detailed discussion of a number of areas which we believed the board might consider in further developing and implementing the plan. Among these were: the initiation of performance reporting on an annual cycle, with results linked to the Strategic Plan, in a manner similar to that used by federal agencies under the Government Performance and Results Act; the development of a formal program for identifying and benchmarking to best practices among grant-making organizations in the federal and non-profit spheres; possible creation of an executive level IT department and chief information officer position, as well as more institutionalized, in-depth focus on information technology issues at the board level; the development and use of improved performance data with respect to both LSC and grantee programs and operations; identification of opportunities for improved coordination and possible partnering with federal entities serving many of the same populations and needs as LSC; and increased attention in the plan to the areas of compliance, resource management, and human capital management.

Freedom of Information Act

The OIG is committed to complying fully with the requirements of the Freedom of Information Act (FOIA). During this reporting period, the OIG received six FOIA requests; all were responded to within the requisite timeframes.

Professional Activities and Assistance

The OIG participates in and otherwise supports various activities and efforts of the Council of the Inspectors General on Integrity and Efficiency (CIGIE), as well other inter-agency and professional groups. The Inspector General serves as a member of the CIGIE Audit Committee, which focuses on government auditing standards and cross-cutting audit issues. Senior OIG officials are active participants in IG community peer groups in the areas of audits, investigations, inspections and evaluations, communications, and legal counsel. The groups provide forums for collaboration and are responsible for such initiatives as developing and issuing professional standards, establishing protocols for and coordinating peer reviews, providing training programs, and promulgating best practices. The OIG also routinely responds to requests for information or assistance from other IG offices.

APPENDIX – PEER REVIEWS

The following information is provided pursuant to the requirements of Section 989C of Public Law 111-203 (July 21, 2010), the Dodd-Frank Wall Street Reform and Consumer Protection Act, amending the Inspector General Act of 1978 (the IG Act), 5 U.S.C. App 3. The references are to the newly added provisions of Section 5(a) of the IG Act.

(14)(B) – The last peer review of the OIG was conducted by the Office of Inspector General for the Corporation for Public Broadcasting, and was completed on September 30, 2011.

(15) – There are no outstanding recommendations from any peer review of the OIG conducted by another Office of Inspector General that have not been fully implemented.

(16) – The last peer review performed by the OIG was of the Office of Inspector General for the U.S. Securities and Exchange Commission, and was completed on August 23, 2012. There are no outstanding recommendations for the last peer review or any previous peer review that remain outstanding or have not been fully implemented.

TABLE I

Audit Reports and Quality Control Reviews Issued for the Period Ending September 30, 2012

Audit Reports

Report Title	Date Issued	Questioned Costs	Funds Put to Better Use	Unsupported Costs[1]
Report on Selected Internal Controls – Texas RioGrande Legal Aid	06/12/12	$0	$0	$0
Examination of Expenditures Incurred for the Performance of Technology Initiative Grants Awarded to Southeast Louisiana Legal Services	07/10/12	$55,741	$0	$55,741
Examination of Expenditures Incurred for the Performance of Technology Initiative Grants Awarded to Legal Services of Southern Missouri	07/20/12	$3,659	$0	$3,659
Report on Selected Internal Controls – South Jersey Legal Services	08/03/12	$0	$0	$0
Report on Selected Internal Controls – Inland Counties Legal Services	08/06/12	$1,367,480	$0	$0

[1] Unsupported costs are a subset of questioned costs and included in the question cost amount.

Quality Control Reviews

	IPA	Recipient	Date Issued
1	GBQ Partners, LLC	Ohio State Legal Services	08/23/12
2	George Johnson & Co.	Legal Aid & Defenders Assoc.	08/23/12
3	Ahern Adcock Devlin LLP	Inland Counties Legal Services	09/20/12
4	David B. Green, CPA	Colorado Legal Services	09/26/12
5	Brown Armstrong	Greater Bakersfield Legal Assistance	09/26/12
6	Yeo & Yeo, PC	Legal Services of Eastern Michigan	09/27/12
7	Yeo & Yeo, PC	Legal Services of South Central Michigan	09/27/12
8	Klatzkin & Company	Ocean-Monmouth Legal Services	09/28/12
9	Blue & Co.	Indiana Legal Services	09/28/12
10	Plante and Moran, PLLC	Legal Aid of Western Michigan	09/28/12

TABLE II

Audit Reports Issued with Questioned Costs for the Period Ending September 30, 2012

	Number of Reports	Questioned Costs	Unsupported Costs[1]
A. For which no management decision has been made by the commencement of the reporting period	2	$99,651	$82,300
B. Reports issued during the reporting period	3	$1,426,880	$59,400
Subtotals (A + B)	5	$1,526,531	$141,700
C. For which a management decision was made during the reporting period:	0	$0	$0
(i) dollar value of recommendations that were agreed to by management	0	$0	$0
(ii) dollar value of recommendations that were not agreed to by management	0	$0	$0
D. For which no management decision had been made by the end of the reporting period	5	$1,526,531	$141,700
Reports for which no management decision had been made within six months of issuance	2	$99,651	$82,300

[1] Unsupported costs are a subset of questioned costs and are included in the question cost amount.

TABLE III

Audit Reports Issued with Funds to Be Put to Better Use for the Period Ending September 30, 2012

	Number of Reports	Dollar Value
A. For which no management decision has been made by the commencement of the reporting period	0	$0
B. Reports issued during the reporting period	0	$0
Subtotals (A + B)	0	$0
C. For which a management decision was made during the reporting period:	0	$0
(i) dollar value of recommendations that were agreed to by management	0	$0
(ii) dollar value of recommendations that were not agreed to by management	0	$0
D. For which no management decision had been made by the end of the reporting period	0	$0
Reports for which no management decision had been made within six months of issuance	0	$0

TABLE IV

Audit Reports Issued Before this Reporting Period for Which No Management Decision on Questioned Costs Was Made by the End of the Reporting Period

Report Title	Date Issued	Questioned Costs	Comments
Examination of Expenditures Incurred for the Performance of TIG Grants Awarded to Center for Arkansas Legal Services	02/27/12	$82,300	LSC is initiating a questioned cost proceeding.
Report on Selected Internal Controls – North Mississippi Rural Legal Services	03/30/12	$17,351	LSC has requested a legal opinion on the questioned cost and is awaiting the final opinion.

Audit Reports Issued Before this Reporting Period with Open Recommendations as of the End of the Reporting Period

Report Title	Date Issued	Comments
Report on Selected Internal Controls: Appalachian Research and Defense Fund of Kentucky	08/22/11	Corrective action still in process of being implemented.
Report on Selected Internal Controls: Legal Services of Northern Virginia, Inc.	09/30/11	LSC management is working with the grantee to resolve all open recommendations.
Report on Selected Internal Controls – North Mississippi Rural Legal Services	03/30/12	According to a status report received from the grantee's executive director, all corrective actions should be completed by December 31, 2012.

TABLE V

Index to Reporting Requirements of the Inspector General Act

IG Act Reference*	Reporting Requirement	Page
Section 4(a)(2)	Review of legislation and regulations.	19
Section 5(a)(1)	Significant problems, abuses, and deficiencies.	5-7
Section 5(a)(2)	Recommendations with respect to significant problems, abuses, and deficiencies.	5-7
Section 5(a)(3)	Prior significant recommendations on which corrective action has not been completed.	27
Section 5(a)(4)	Matters referred to prosecutive authorities.	None
Section 5(a)(5)	Summary of instances where information was refused.	None
Section 5(a)(6)	List of audit reports by subject matter, showing dollar value of questioned costs (including a separate category for the dollar value of unsupported costs) and funds to be put to better use.	23-24
Section 5(a)(7)	Summary of each particularly significant report.	5-7
Section 5(a)(8)	Statistical table showing number of audit reports and dollar value of questioned costs.	25
Section 5(a)(9)	Statistical table showing number of reports and dollar value of recommendations that funds be put to better use.	26
Section 5(a)(10)	Summary of each audit issued before this reporting period for which no management decision was made by the end of the reporting period.	27
Section 5(a)(11)	Significant revised management decisions.	None
Section 5(a)(12)	Significant management decisions with which the Inspector General disagrees.	None
Section 5(a)(14)-(16)	Peer reviews.	22

*Refers to sections in the Inspector General Act of 1978, as amended.

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