

# LEGAL SERVICES CORPORATION



Office of  
Inspector General



Semiannual Report to the Congress  
April 1, 2011 – September 30, 2011

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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, 2011 through September 30, 2011.

During this reporting period we completed five audits at LSC-funded programs. Our primary focus was on the adequacy of internal controls, especially as they related to financial operations. We continue to regard this type of review as a high priority, and had four additional such audits underway at the close of the period.

At one program we found an array of deficiencies in controls and accounting processes so serious overall as to constitute a material weakness in the program's internal control system. We reported that the control weaknesses raised questions about both the reliability of the information we received and the integrity of the accounting system. We concluded that there could not be adequate assurance that LSC funds were spent in accordance with the terms and conditions of the grant and, accordingly, we questioned more than \$250,000 in costs charged by the program to LSC funds.

This period we also fully implemented our initiative to provide improved oversight of the independent audits required annually of LSC grantees. Quality control reviews will be conducted on a four-year cycle of all firms performing grantee audits, along with targeted reviews when fraudulent activities, internal control deficiencies, or other problems indicate a need for special review. This period 16 routine reviews were completed or underway, and 8 targeted reviews were completed.

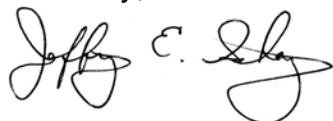
We opened 13 new investigations and closed 16 investigations during the reporting period. Among the investigations were cases involving fraudulent expense claims and theft of client funds by grantee employees.

We have received considerable positive feedback on our fraud awareness briefings. We expanded our schedule of these presentations, and are continuing to pursue other outreach and educational initiatives with grantees as part of our ongoing

efforts to help prevent fraud and abuse in LSC-funded programs.

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,

A handwritten signature in black ink, appearing to read "Jeffrey E. Schanz". The signature is written in a cursive style with a large initial "J" and a long horizontal stroke at the end.

Jeffrey E. Schanz  
Inspector General  
October 31, 2011

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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 to 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. Work in progress at the end of the reporting period included audits at five grantees. Two of these audits were in the draft report stage; field work was in progress for the remaining three. Additional audits were in the planning stage.

The OIG has responsibility for overseeing the independent public accountant (IPA) audits performed annually at each grantee. The OIG reviewed 115 IPA reports, with fiscal years ending from December 31, 2010 to March 31, 2011, received during the reporting period.

As detailed below, the OIG recently initiated a new, expanded approach to its oversight of the IPA process. The new approach will result in a quality control review (QCR) being conducted at each IPA over a four-year cycle, starting with the FY 2010 reports. The QCRs will include coverage of both the IPAs' financial and compliance audit work, providing a broader review than had been possible under the previous approach. These reviews will primarily be conducted by CPA firms under contract to the OIG, enabling the OIG to leverage its resources and thereby provide for review of a larger number of IPAs. A contract was awarded and an initial series of 16 QCRs were completed or in progress during the period.

In addition, special targeted QCRs will be conducted when circumstances warrant, e.g., when significant issues arise or fraudulent activity is discovered at a grantee, or when questions otherwise arise about the quality of a specific IPA's work. These targeted reviews are also conducted by an accounting firm under contract to the OIG. Eight such reviews were completed this period.

The OIG also has responsibility to contract for and oversee LSC's annual financial statement audit. During this reporting period we initiated the competitive bid process and selected a new audit firm to conduct the annual audit.

### **Appalachian Research and Defense Fund of Kentucky – Audit of Selected Controls**

This audit resulted from allegations received by the Office of Inspector General about activities at Appalachian Research and Defense Fund of Kentucky (AppalReD). Because of the seriousness of the allegations, the OIG promptly initiated an audit focusing on the adequacy of selected internal controls in place at AppalReD, particularly with respect to grantee financial operations and oversight, including grantee expenditures and fiscal accountability.

We found that, taken as a whole, the control deficiencies identified in the report constituted a material weakness in the grantee's internal control system. As a result, we reported, the grantee may have impairments to the effectiveness and efficiency of operations, misstatements in financial and performance information, and there may be violations of laws and regulations that are not being prevented,

detected, or corrected by management or staff in a timely manner in the normal course of business.

We reported that, in our opinion, grantee's management did not have adequate assurance that LSC funds spent on the delivery of legal services and related support services had been expended in accordance with LSC grant terms and conditions.

Among other things, our report identified 17 distinct areas of deficiency where the grantee needed to improve internal controls and accounting processes. We reported that the internal control weaknesses led us to question the reliability of the information we received and raised questions about the integrity of the amounts generated from the accounting system and presented to us during the period under review. Six people had unrestricted access to multiple incompatible aspects of the grantee's accounting system. Approximately 77 percent of all the disbursements tested were either unsupported or inadequately supported. Also, an invoice for the approximately \$64,000 cost of new teleconferencing equipment had not been recorded in the accounting system, reportedly because the grantee did not have the funds available to pay the invoice. We noted that lack of funds is not a valid reason for not recording legitimate purchases in the accounting records. The OIG could not determine whether this was the only such invoice not recorded or if there were other unrecorded invoices.

As a result of the deficiencies cited in the report, the OIG questioned \$257,057 in costs charged to LSC funds. We concluded that the conditions we found likely occurred because the grantee had not established or enforced an adequate system of internal controls, and the staff did not have the knowledge, skills, and abilities necessary to properly operate the existing controls and accounting system.

The OIG made one overall recommendation. The OIG expects that by implementing necessary corrective actions in response to the overall recommendation, all issues contained in the report will be addressed. The OIG recommended that the grantee's Board of Directors obtain the services of a skilled individual(s), not associated with the grantee, to review the internal control design, accounting process and accounting department organizational structure, and implement changes, in accordance with LSC requirements, to ensure that the grantee's resources are properly controlled, accounted for, and safeguarded. The individual(s) should assess the personnel needs of the accounting department and provide any necessary training to the employees in that department or recruit qualified individuals to perform such duties.

Grantee management's comments were responsive to the overall recommendation. We noted our concern that while the recommendation was directed to the Board of Directors, the grantee's response was provided by the Interim Executive Director, and there was no direct indication of the Board's agreement with the comments.

The recommendation will remain open until management has completed all necessary actions and the OIG has evaluated those actions.

### **California Indian Legal Services Inc. – Follow-up Report on Selected Internal Controls**

This audit followed up on corrective actions taken by California Indian Legal Services, Inc. (CILS) to correct significant issues identified in the OIG's *Report on Selected Internal Controls, California Indian Legal Services (AU09-03)*, March 2009. Specifically, our review was to determine whether the grantee's cost allocation system was adequately designed, fully documented, and implemented as designed. In addition, we determined whether attorney incentive payments resulting from CILS' fee for service program were properly allocated.

The OIG found that the allocation system as explained and demonstrated by CILS management provides a reasonable basis for allocating indirect costs to LSC funds. However, the new accounting manual provided a general description of the system and was not detailed enough to provide an understanding of how the system actually operated.

With regard to allocating attorney incentive payments, for payments made in 2009, CILS management instituted a policy to allocate these payments to the fee for service program only. However, the 2008 attorney incentive payments, totaling over \$60,000, were recorded in a shared overhead account, \$27,600 of which we found was improperly allocated to LSC funds. The OIG questioned the portion of the attorney incentive payments improperly charged to LSC funds in 2008 and referred that amount as a questioned cost to LSC management.

The OIG noted that the grantee had a practice of charging expenses to its LSC grant account in amounts totaling more than the grant it actually received from LSC. The grantee would then cover the resulting shortfalls between its LSC grant and the amounts charged to it by transferring money from its other funding source accounts to its LSC account. The grantee transferred over \$190,000 in this manner to its LSC grant account during fiscal years 2008 and 2009.

A review of LSC's accounting guidance and discussions with LSC officials indicated that transferring monies at year's end from non-LSC funds to cover deficits in LSC funds was considered an accepted practice, and was LSC's preferred way to handle such deficits. (This practice eliminates the need for the recipient to obtain prior written approval from LSC, as would be required by LSC regulations if they were to use current year LSC grant funds to liquidate a deficit in their LSC fund account from a preceding period.)

However, even though the practice was sanctioned by LSC, we believed it raised a number of concerns. Essentially, at year's end a lump sum was simply added to the grantee's LSC account net asset figure to "zero out" any negative balance (deficit). The transfer was reported only on a supplemental schedule; at the time of the audit, the amount was not entered into the accounting records as an

adjustment; there was no clear indication of the funding source(s) from which the transfer was made; and the amount transferred was not distributed to any specific expense accounts (e.g., salaries, employee benefits, rent, office supplies, etc.). We concluded that this did not constitute “adequate and contemporaneous document[ation] in business records,” as required for expenses to be allowable under LSC regulations (45 CFR Part 1630). We commented that while the practice might simplify handling deficits in LSC fund balances, it may also have the unintended consequence of encouraging or perpetuating poor accounting methods for those receiving LSC funds. The OIG will forward the issue to LSC management for review.

The audit included one recommendation for grantee management, that they document the allocation system in sufficient detail to capture all key steps and processes, and incorporate steps to review grants annually for any changes that would impact cost allocation amounts. Grantee management took corrective action and provided the OIG detailed documentation of its cost allocation system. The OIG considers the recommendation closed. Since management had already implemented corrective action pertaining to attorney incentive payments, no recommendation was necessary. The OIG referred the questioned cost of \$27,600 in attorney incentive payments charged to LSC funds to LSC management for action.

### **MidPenn Legal Services, Inc. – Audit of Selected Internal Controls**

The OIG assessed the adequacy of selected internal controls in place at MidPenn Legal Services, Inc. related to grantee operations and oversight.

We found that, in general, the internal controls reviewed were adequate. Grantee disbursements tested were adequately supported, allowable, and properly allocated to LSC funds. The grantee’s current practices involving internal management reporting and budgeting were generally in accordance with the “Fundamental Criteria” contained in LSC’s Accounting Guide. Internal controls over reimbursements and employee benefits were adequate. Policies over employee benefits practices were in writing and followed. Controls over regulations were designed in a manner expected to ensure compliance with the LSC Act and selected LSC regulations.

However, we reported that controls need to be strengthened or formalized to correct the following weaknesses in four specific areas: (1) The audit found that the grantee’s fiscal and information technology departments maintained separate inventory records, that the listings were not reconciled with each other, and that neither one contained all the relevant information as recommended by LSC’s Fundamental Criteria. Moreover, the grantee did not maintain comprehensive property records for fixed assets purchased or received through donation. (2) A portion of the grantee’s office space in Gettysburg, PA, had been subleased to Regional Housing Legal Services (RHLS), a nonprofit law firm, since July 2007. However, the grantee recorded the income from the rent and the RHLS’s share of utilities as reductions of the grantee’s rent expense and the utilities accounts.

Thus, the grantee had not reported the receipts from RHLS as derivative income in the audited financial statements. As of April 30, 2010, the unreported derivative income was estimated at \$4,125 for the previous 34 months. (3) The grantee did not have in place an entity-wide disaster recovery plan. (4) Grantee invoices and other supporting documentation that were approved for payment were not marked paid or otherwise cancelled.

The OIG made four recommendations to address these issues:

- A subsidiary property record should be prepared for all fixed assets purchased or received through donation. The record should contain all information required by LSC's Fundamental Criteria.
- Income derived from rental or subleased office space should be properly recorded.
- The Board of Directors should be presented with a finalized entity-wide disaster recovery plan for approval. Once approved, the Executive Director should implement the plan.
- The grantee should implement procedures for properly annotating documentation supporting disbursements as paid or otherwise cancelled to avoid duplicate payments.

The OIG considered the actions taken or planned by grantee management to be responsive to all four recommendations. Action was completed on all but one recommendation at the time our report was issued. Subsequent to the report, grantee management provided detailed information on actions taken on the remaining recommendation and the OIG closed the recommendation.

### **Legal Services of Northern Virginia, Inc. – Audit of Selected Internal Controls**

The OIG conducted an audit to assess the adequacy of selected internal controls in place at Legal Services of Northern Virginia (LSNV) related to the grantee operations and oversight. We found that, in general, the internal controls reviewed were adequate. Grantee disbursements tested were adequately supported, allowable, and appeared to be properly allocated to LSC funds. The grantee's current practices involving internal management reporting and budgeting were generally in accordance with the Fundamental Criteria contained in the Accounting Guide. Internal controls over reimbursements and employee benefits were adequate. Policies over employee benefits practices were in writing and adhered to, except for salary advances.

However, we reported that controls needed to be strengthened in three specific areas. First, we found that the grantee's current accounting manual did not contain written policies and procedures governing credit card usage; monitoring of subgrant funds; cost allocation methodology; salary advances; travels and per diem reimbursement limits; internal management reporting and budgeting; and

cell phones and electronic devices. Second, we found that the grantee did not properly manage fixed assets. Subsidiary records of capitalized equipment and property that were purchased or donated did not include details required by the grantee's accounting manual and LSC's Accounting Guide. The grantee did not affix any unique characteristics or markings on its capitalized assets, which would have made locating and identifying the fixed assets easier. Since its merger with Potomac Legal Aid Services, Inc. (PLAS) in January 2010, the grantee has not conducted a physical count of all capitalized equipment and property. Lastly, we found that the grantee was not monitoring its subgrants as required by subgrant agreements and in accordance with LSC regulations.

The OIG made six recommendations to address these issues:

- incorporate in LSNV's accounting manual all essential policies and processes as required by the LSC Accounting Guide;
- improve the management of fixed assets by including in the subsidiary records the details required by the grantee's accounting manual and the LSC Accounting Guide;
- document the processes to be used to ensure that subsidiary records are accurately updated;
- attach inventory tags or labels to fixed assets;
- conduct a physical inventory; and
- put in place written policies and procedures to ensure that subgrants are properly monitored.

The OIG considered grantee management's comments on actions taken or planned to be partially responsive to five of the six recommendations and non-responsive to one recommendation. All six recommendations have been forwarded to LSC management for resolution and will remain open until resolved.

### **Legal Aid of North Carolina – Audit of Selected Controls**

The OIG assessed the adequacy of selected internal controls in place at Legal Aid of North Carolina, Inc. related to specific grantee operations and oversight. We found that, for the most part, internal controls tested were adequate. However, several controls needed to be developed or strengthened, including those over purchasing and those regarding compliance with LSC's regulation on lobbying and legislative activity. Other control procedures, such as cost allocation and contracting, appeared reasonable but were not documented. Disbursements tested were for the most part adequately supported, allowable, and appeared to be properly allocated to LSC.

We reported that the following areas needed improvement:

- The grantee's purchasing and contracting procedures needed to be strengthened. Purchasing and receiving duties were not adequately separated. The grantee did not use a three-way matching system that would require the purchase order, invoice, and receiving report be completed or compared and on file before a payment was made. Policies and procedures for awarding consulting and service contracts were not documented. Supporting documentation was not kept with respect to the grantee's solicitation of multiple vendors, and receipt and analyses of bids or cost estimates.
- Unnecessary or unallowable expenses totaling \$7,506 were charged to LSC funds. These included expenditures for the purchase of flowers, a holiday party, meals (where there was not a description of an underlying business purpose), and finance charges. The OIG questioned the costs associated with those expenses.
- Internal controls over financial operations needed to be improved. Specific steps needed include strengthening controls over credit cards, providing financial reports with variance data to the grantee's Board of Directors, documenting position descriptions, and developing and documenting policies for managing grantee vehicles.
- Policies and procedures needed to be formulated, formalized, or revised in several areas, including: the awarding of contracts; allocating costs; reimbursing for personal mobile communication plans; identifying participants attending and the purposes of business meetings where meals are provided; handling source documents after scanning; and ensuring that differences do not exist between written policy and actual practice.
- The grantee did not adequately control and document its compliance with LSC's restrictions on legislative activity (45 CFR Part 1612), and used LSC funds for the activity in violation of the regulation. (This matter was highlighted and reviewed with grantee and, as described below, was promptly addressed.)

The grantee had initiated corrective action for two of the issues noted above. Specifically, the Executive Director issued instructions to all grantee staff that should ensure that any involvement in legislative activities complies with LSC regulations and is properly reported. The Executive Director had the finance staff prepare an adjusting journal entry to reverse improper charges to LSC funds related to the legislative activities. Also, the grantee's staff prepared a revised vehicle usage log to better ensure accurate reporting of mileage, and placed the gas credit card in a more secure area.

The audit report included 14 OIG recommendations. Four of the recommendations related to improving internal controls, including: segregating ordering and receiving duties; instituting a purchase order system; including variance information with monthly financial data provided to the Board of Directors and the Finance committee; and conducting year-end reviews to ensure that only allowable items are charged to LSC funds. Seven recommendations addressed the need to formalize and document policies and procedures pertaining to such areas as contracting; cost benefit analyses; prohibiting the use of LSC funds for non-business functions and purposes; operating and managing grantee vehicles and gas credit cards; electronic filing of source documents; compliance with LSC's restrictions on legislative activity; and ensuring that documented policies and procedures and those in actual use are in agreement. Two recommendations pertained to ensuring that documentation supporting major purchases was maintained and that documentation supporting credit card charges was provided to the finance office prior to paying the credit card bill. One recommendation addressed the need to document position descriptions.

Grantee management's actions taken or planned were responsive to 13 of the 14 final recommendations. The grantee disagreed with the remaining recommendation (to conduct year-end reviews to ensure that only allowable items are charged to LSC funds) and the OIG referred it and the \$7,506 in questioned costs to LSC management for resolution. Action was completed on two recommendations and they were closed. Twelve of the 14 recommendations will remain open until all stated grantee management actions are completed, the disagreement with the one recommendation is resolved, and appropriate written notification is provided to the OIG.

### **Audits of Technology Initiative Grants**

As a follow-on to our recent review of the Technology Initiative Grant (TIG) program at LSC headquarters, the OIG has begun audits of grantees receiving TIGs. The audits will focus on whether TIG expenditures were allowable and supported, and whether the stated purposes of the TIG have been achieved.

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. The OIG analyzed the information provided on 120 grants, valued at a total of just under \$9 million, awarded to 65 separate grantees, to determine which to review. For those grants selected for review, the OIG will visit the grantee to review supporting documentation. The first on-site visit occurred during the last week of September 2011. The OIG will evaluate the results of each visit to streamline the process and to identify any systemic issues that need to be forwarded to LSC management for review. The reviews and the reports will be handled under government auditing standards for attestation engagements.

## **FY 2011 Corporate Audit**

During this reporting period, the OIG issued a Request For Proposals for LSC's FY 2011 financial statement audit. The OIG received seven bids. WhithumSmith+Brown, PC was the successful bidder. Though not the incumbent, the firm had conducted the annual corporate audit for LSC in the past, and thus has knowledge of LSC systems and processes. An entrance conference was scheduled for October. The OIG will monitor the audit to ensure the quality and completeness of the project.

## **Statistical Summary**

### **Audit Reports**

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Pending at end of reporting period .....	19

### **Recommendations to LSC Management**

Pending at beginning of reporting period .....	24
Issued during reporting period.....	0
Closed during reporting period.....	0
Pending at end of reporting period .....	24 <sup>1</sup>

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<sup>1</sup>On September 30, 2011, LSC management provided actions taken on 10 open recommendations from the Technology Initiative Grant report and requested that the recommendations be closed. The OIG was evaluating this request as of the end of the reporting period.

## **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 have been 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 recently launched an initiative to provide more systematic and broader-based reviews of the IPA audits. A dual program of both routine and targeted quality control reviews (QCRs) is designed to provide greater assurance as to the quality of the IPAs work overall, and to identify or respond to potential problems or concerns that may arise with respect to particular grantees or IPAs. Both types will be conducted by an independent certified public accounting firm, operating under contract to the OIG.

#### **'Routine' QCRs**

We have implemented a comprehensive program under which all IPA firms performing grantee audits will be subject to at least one 'routine' QCR every four years. This reporting period the OIG contracted with an accounting firm to conduct QCRs of the grantee audits of 36 specified IPAs over the course of the initial contract year, with options for contract extensions providing for a minimum of 35 QCRs annually for up to three subsequent years.

The QCRs will 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 the OIG. (The nature and scope of the QCRs themselves are defined in the contract, and essentially accord with the *Guide for Quality Control Reviews of OMB Circular A-133 Audits*, issued by the federal Council of Inspectors General for Integrity and Efficiency (CIGIE).) The contractor will also identify any issues that may require additional attention or additional audit work by the IPA.

After each QCR is completed and submitted to the OIG by the contractor, the OIG will issue a report to the IPA on the results of the review. Depending upon the findings in the QCR, the OIG may require the IPA to do additional work or make improvements for any future audits it conducts of LSC grantees. In addition, the contractor will provide an annual summary report, based on all the QCR work it performs, identifying any significant or recurring issues. The OIG will use this report and the results of the QCRs to improve or add to its guidance to grantees and IPAs.

As of the close of this reporting period, 16 QCRs had been completed or were in progress. Of those 16, 13 reports were submitted to the OIG. Seven of the 13 reports were finalized by the OIG and provided to the IPA.

#### 'Targeted' Quality Control Reviews

We also contracted with an accounting firm to perform targeted QCRs of selected IPAs, in cases where particular problems or concerns have arisen. For example, we found that the regular annual audits conducted by two IPAs had not detected significant issues and irregularities that had gone on at their subject grantees for many years. The targeted QCRs will focus especially on the undetected issues in determining whether the audits were conducted in accordance with professional standards and the OIG's guidance. They will also help determine whether the OIG might be able to issue additional guidance or information to help grantees and auditors detect significant frauds or internal control weaknesses in the future.

This period, eight targeted QCRs were conducted, covering four annual audits at each of two different IPAs. While overall the contractor concluded that the audits appeared to have been adequate, the reports did include recommendations for improving future audits. The OIG instructed the subject IPAs to implement the recommendations before engaging in future LSC grantee audits. The contractor also provided us with information to consider for possible improvements to the IPA system.

## **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 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 115 IPA audits of grantees with fiscal year ending dates from December 31, 2010 through March 31, 2011. These audit reports contained 87 findings. The OIG determined that 28 findings were not significant or that corrective action had already been completed and closed the findings. The remaining 59 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, 2010 through March 31, 2011**

Total Number of Findings Referred.....	59
Number of Findings with Corrective Action Accepted by LSC Management .....	15
Number of Findings Awaiting LSC Management Review.....	44

**Types of Findings Referred to LSC Management for Follow-up**

<b><u>Category</u></b>	<b><u>Number of Findings</u></b>
Financial Transactions and Reporting.....	20
Missing Documentation.....	8
Policies and Procedures (establishment/compliance).....	6
Reporting Issues .....	5
Fund Balance.....	5
Data Security .....	4
Subgrant Issues.....	4
Timekeeping .....	3
Client Trust Funds.....	2
Physical Inventory.....	1
Qualified Opinion .....	1
 TOTAL .....	 59

## **INVESTIGATIONS**

The OIG opened 13 investigations during this reporting period. These included 3 criminal investigations, 6 compliance matters, and 4 fraud vulnerability assessments. The criminal investigations included allegations of fraudulent activity and financial irregularities. The compliance investigations included allegations of violations of LSC statutes and regulations involving matters such as the outside practice of law and improper recording of work hours.

During the reporting period the OIG closed 16 investigations. These included 7 criminal investigations, 5 compliance matters, and 4 fraud vulnerability assessments. The OIG also issued five 5 Inspector General subpoenas in connection with our ongoing investigations.

### **Long-Time Employee of Grantee Made Fraudulent Travel Claims**

A grantee reported that one of their paralegals, who had been with the grantee for over 30 years, appeared to have submitted false time entries and fraudulent travel reimbursement claims. When questioned by the grantee, the employee could not provide support for the travel claims and was removed from employment. The OIG conducted an investigation and loss analysis and determined that the employee had made over \$4,000 in fraudulent travel claims. Upon being interviewed by the OIG, the individual admitted that most of the claimed trips were not taken and agreed to repay the grantee. Full restitution has been made.

### **Former Paralegal Stole Client Filing Fees**

A grantee dismissed a paralegal from employment for assisting an incarcerated person with a divorce. (LSC regulations generally prohibit grantees from representing prisoners in civil litigation.) After dismissing the employee, the grantee received telephone calls from a number of clients who complained that they had given money to the former employee for filing fees but had not heard anything on the status of their cases. The grantee determined that the filing fees had not been paid to the court and agreed to pay the fees. The OIG investigated and determined that the former employee stole \$900 from the grantee's clients, all of which was "covered" by the grantee. Following OIG investigation, the employee agreed to make full reimbursement to the grantee. Reimbursement payments were begun and to date total \$600.

## **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 and fraud vulnerability assessments, as described below, and provide fraud alerts and other information which 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 most 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 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 eight fraud awareness briefings for LSC-funded programs in California, Kentucky (two), New Mexico, Ohio (two), Utah, and Wisconsin.

### **Fraud Vulnerability Assessments**

The OIG's fraud vulnerability assessments (FVAs) are conducted on-site at individual grantee's offices and consist of a focused document review in any areas considered weak or prone to abuse, a review of grantee internal control policies and the degree to which those policies are observed in practice, and briefings for the executive director and principal financial officers 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. Project findings are incorporated into the FVA program on an on-going basis.

Four FVAs were completed during the reporting period, including three that were begun during the prior period.

### **Fraud Alert**

During the reporting period, a Fraud Alert was issued to inform grantees of several investigations that uncovered repeated instances of timekeeping and travel fraud – time and attendance submissions where work was not performed and travel reimbursement claims where travel was not taken. The advisory bulletin also explained how compliance with specified LSC regulations and other requirements could help prevent and detect such types of fraud.

### **Hotline**

The OIG maintains a Hotline for reporting illegal or improper activities by LSC grantees or Corporation staff. 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 62 Hotline contacts (compared to 56 for the previous period). Of these matters, 12 were referred to LSC management for follow-up; 7 were opened as investigations; 7 are open pending further inquiry; and the remaining 36 were closed.

## **Statistical Summary**

### **Investigative Cases**

Open at the beginning of period.....	21
Opened during the period .....	13
Closed during period.....	16
Open at the end of period .....	18

### **Prosecutorial Activities**

There were no new prosecutorial activities during this reporting period.

### **Investigative Activities**

Inspector General subpoenas issued .....	5
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## **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 legislative and regulatory provisions affecting LSC and/or the OIG, as well as LSC interpretive guidance and internal policies and procedures.

### **Litigation**

As noted in previous reports, we have a subpoena enforcement action pending in U.S. District Court for the District of Columbia. This matter has been briefed and argued and, at the request of the Court, was the subject of mediation efforts, which proved unsuccessful. It remains pending decision by the District Court.

### **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 five FOIA requests; all were responded to within the requisite timeframes.

### **Congressional Requests**

In response to a request from the Chairman, House Appropriations Subcommittee on Commerce, Justice, Science, and Related Agencies, the OIG provided a letter report and analysis regarding possible violation by an LSC grantee of restrictions on political activity.

The grantee had produced a pamphlet entitled, "Know Your Rights As An H2A Worker." (The H2A visa/certification program permits foreign nationals to enter the U.S. to perform temporary or seasonal agricultural labor.) In part, the pamphlet contrasted the Bush and Obama Administrations' actions with respect to pay for H2A workers, and characterized the former as aligned with those wanting lower wages for H2A workers and the latter as aligned with those wanting higher H2A wages. The pamphlet also included a cartoon depicting former President Bush as burying H2A wages.

The OIG concluded that the publication and distribution of the pamphlet constituted political activity which would be subject to Section 1007(a)(6)(A) of the LSC Act. Under that provision, such activity would be prohibited if either LSC funds or non-LSC *private* funds were used, but would be permissible if non-LSC *public* funds (including funds from Interest on Lawyers Trust Account [IOLTA] programs) or tribal funds were used and if that use was in accord with the specific purposes for which the funds were provided. The OIG recommended

that LSC management determine the source of funds used to ascertain whether a violation occurred. Subsequently, the grantee acknowledged having used LSC funds to publish the pamphlets, and returned the money to LSC.

### **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, 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 Corporation for Public Broadcasting, Office of Inspector General. A system review report with a rating of “Pass” was issued 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) – No peer reviews were conducted by the OIG of another Office of Inspector General during the reporting period. The last peer review conducted by this office was of the National Railroad Passenger Corporation (Amtrak), Office of Inspector General’s Audits organization. The report was dated September 30, 2009. We have been advised by that office that a system has been developed and is fully operational that accurately tracks required continuing professional education (CPE) credits. There are no recommendations outstanding or not fully implemented.

## TABLE I

### Audit Reports Issued for the Period Ending September 30, 2011

<u>Report Title</u>	<u>Date Issued</u>	<u>Questioned Costs</u>	<u>Funds Put to Better Use</u>	<u>Unsupported Costs</u>
Report on Selected Internal Controls: California Indian Legal Services	08/04/11	\$27,600	\$0	\$0
Report on Selected Internal Controls: MidPenn Legal Services	08/11/11	\$0	\$0	\$0
Report on Selected Internal Controls: Appalachian Research and Defense Fund of Kentucky	08/22/11	\$257,057	\$0	\$0
Report on Selected Internal Controls: Legal Services of Northern Virginia, Inc.	09/30/11	\$0	\$0	\$0
Report on Selected Internal Controls: Legal Aid of North Carolina, Inc.	09/30/11	\$7,506	\$0	\$0

### Quality Control Reviews Issued for the Period Ending September 30, 2011

<u>Recipient</u>	<u>IPA</u>	<u>Date Issued</u>
Capital Area Legal Services Corp. Fiscal years 2005 through 2008	Broussard, Poche, Lewis & Breaux, LLP	08/2/11
Legal Services of Northwest Jersey, Inc.	Wiss & Company, LLP	08/29/11
Central Jersey Legal Services	Wiss & Company, LLP	08/29/11
Utah Legal Services	Burnham & Schumm, PC	08/30/11
Virginia Legal Aid Society, Inc.	Coley, Eubank & Company	08/30/11
Legal Aid Bureau, Inc. (Maryland) Fiscal years 2003 through 2006	Mitchell & Titus, LLP	09/08/11
Legal Services Alabama	Carr, Riggs & Ingram, LLC	09/30/11
Southern Minnesota Regional Legal Services	LarsonAllen, LLP	09/30/11
Montana Legal Services Association	Anderson ZurMuehlen & Co., PC	09/30/11

## TABLE II

### Audit Reports Issued with Questioned Costs for the Period Ending September 30, 2011

	<u>Number of Reports</u>	<u>Questioned Costs</u>	<u>Unsupported Costs</u>
A. For which no management decision has been made by the commencement of the reporting period.	1	\$886,673	\$0
B. Reports issued during the reporting period	5	\$292,163	\$0
Subtotals (A + B)	6	\$1,178,836	\$0
C. For which a management decision was made during the reporting period:	1	\$886,673	\$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	1	\$886,673 <sup>1</sup>	\$0
D. For which no management decision had been made by the end of the reporting period	3	\$292,163	\$0
Reports for which no management decision had been made within six months of issuance	0	0	\$0

<sup>1</sup> LSC management cited three main reasons for not agreeing to disallow the costs associated with the OIG's questioned costs: (1) a policy on conflict of interest, applicable to the grantees, was not in place at the time the grants being questioned were awarded; (2) no evidence was available indicating that the costs associated with the grants were not adequately documented; and (3) there was no evidence to suggest that the costs incurred were unreasonable or not prudent under the circumstances. LSC management also indicated LSC staff and possibly senior managers knew of the apparent or potential conflicts but took no action to question or challenge the relationships.

### TABLE III

#### Audit Reports Issued with Funds to Be Put to Better Use for the Period Ending September 30, 2011

	<u>Number of Reports</u>	<u>Dollar Value</u>
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 Was Made by the End of the Reporting Period

<u>Report Title</u>	<u>Date Issued</u>	<u>Questioned Costs</u>	
Audit of LSC's Technology Initiative Grant Program	12/08/10	\$886,673	Management submitted a request to close 10 recommendations on September 30, 2011. The information provided is under review.

# TABLE V

## Index to Reporting Requirements of the Inspector General Act

<u>IG Act Reference*</u>	<u>Reporting Requirement</u>	<u>Page</u>
Section 4(a)(2)	Review of legislation and regulations	None
Section 5(a)(1)	Significant problems, abuses, and deficiencies.	3-5
Section 5(a)(2)	Recommendations with respect to significant problems, abuses, and deficiencies.	3-5
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.	24
Section 5(a)(7)	Summary of each particularly significant report.	3-5
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.	23

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



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