



May 17, 2011

The Honorable Tom Harkin  
Chairman  
Committee on Health, Education, Labor and Pensions  
United States Senate  
644 Dirksen Senate Office Building  
Washington, D.C. 20510

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James J. Sandman

**Board of Directors**

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Dear Chairman Harkin:

The Office of Inspector General (OIG) of the Legal Services Corporation (LSC) has completed its Semiannual Report to the Congress for the period October 1, 2010 to March 31, 2011. I am transmitting the Report to the Congress as required by law, along with this additional information provided by the LSC Board of Directors.

Congress has entrusted LSC with a dual mission: to promote equal access to justice and to provide high-quality civil legal assistance to low-income Americans. In fulfillment of that mission, LSC funds 136 nonprofit programs with 919 offices serving every state in the nation, the District of Columbia and the U.S. territories.

Since October of last year, the new LSC Board of Directors has been working together and has several successes to bring to your attention. First of all, after a nation-wide search, we hired a new President of the Corporation, James J. Sandman, who assumed his position on January 31. We placed managerial competence at the top of our search criteria and in Jim Sandman we found the leader who met all of our expectations. A long-time managing partner of Arnold & Porter and former president of the District of Columbia Bar, Jim most recently served as the General Counsel for the District of Columbia Public Schools under Michelle Rhee. We are fortunate to have him as our new CEO.

Secondly, we are pleased to report that all of the 2007 recommendations of the Government Accountability Office (GAO) regarding governance, oversight, and internal controls at LSC have been implemented and have been reviewed and accepted by GAO as completed. The Board will be working with the management of LSC to ensure ongoing adherence to all associated policies and procedures.

The recommendations from the most recent GAO report, issued in June 2010 regarding the Corporation's internal controls over grant awards and grant program effectiveness, are nearing completion. LSC has submitted documentation of completion on 13 of the 17 recommendations. The remaining recommendations are being taken up as part of the Board's recently commenced strategic planning effort. We look forward to working with the GAO to complete all the recommendations to their satisfaction in the near future. We assure you that our Board will continue to oversee the implementation of recommendations contained in the report.

Finally, shortly after we took office, this Board saw the need to determine whether LSC has the structure, procedures, and measurements in place to ensure the best fiscal oversight of our grantees. We created a Special Task Force on Fiscal Oversight to study how fiscal oversight of grantees is currently performed by the Corporation and to report findings and make recommendations to the Board. Victor B. Maddox, the Chairman of our Audit Committee, and Robert J. Grey, Jr., the Chairman of our Finance Committee, are co-chairing the effort, and Father Pius Pietrzyk, of the Board, and Robert E. Henley, Jr., a non-director member of the Finance Committee, are also members.

The majority membership of the Task Force is comprised of persons from outside the Corporation and the Board. It includes three senior executives of Fortune 500 corporations, six leaders of national foundations, two experienced accounting executives, and two former inspectors general. It is an impressive group of individuals and is working hard to have a draft report and recommendations completed by July.

The LSC Board of Directors concurs with the presentation of statistics in Tables I, III, and IV of the Inspector General's Semi-Annual Report. The Board concurs with the presentation of statistics in Table II of the Report, with the exception of the \$866,673 questioned cost figure, which is described as an amount for which no management decision was made by the end of the reporting period. Although the subject audit report (with questioned costs) was issued during the period, a questioned costs referral was not made to LSC management until after the close of the reporting period (as noted in the footnote to Table II). LSC management received the referral on April 29, 2011. LSC management has begun its review of the background on these questioned costs, but in light of the recency of the referral, it is not yet in a position to make a decision on acceptance of those questioned costs.

Pursuant to 5 U.S.C. App.3 § 5(b)(2)(C)(i), the Corporation reports that at the beginning of this reporting period no funds identified in OIG audits as disallowed have been either collected by LSC or not charged to LSC funds.

Regarding audits that have been open since the last reporting period, progress is as follows:

- The Report of an Audit of Capital Area Legal Services Corporation (CALSC) of Baton Rouge, LA. On April 12, 2011, CALSC provided LSC's Office of Compliance and Enforcement (OCE) with a written response to each of the 21 recommendations of LSC's Office of Inspector General. OCE is committed to devoting the time and resources to review the CALSC's current status and progress towards becoming compliant with LSC regulations and requirements. CALSC is currently on month-to-month funding, and its service area is under competition. A final decision on the competition of the service area is expected in June 2011. In addition, LSC issued a questioned cost decision against the program for disallowed costs of \$700,000. The program appealed that determination and the LSC President, after reviewing the matter, issued a final decision on March 23, 2011 and modified the disallowed costs to \$487,000.
- The Report on Selected Internal Controls: Legal Aid and Defender Association, Inc.(LADA) The remaining open recommendation is the program's accounting manual, including its travel expense policies and forms. On April 26, 2011, a conference call was held between OCE and LADA to further clarify what needs to be done in order to satisfy the OIG recommendation. LADA sent a revised travel policy on April 27, which LSC is currently reviewing. LSC management will work with LADA and the OIG for an early resolution of this last open item.
- The Report on Selected Internal Controls: California Indian Legal Services (CILS). The new accounting manual completed by CILS and transmitted to the OIG completes management's required documentation. CILS was notified by the OIG in a letter dated April 28, 2011 that the manual was accepted and the audit is closed.
- The Report on Selected Internal Controls: Legal Services New York City. In a memo dated April 27, 2011, the OIG closed out the audit of Legal Services of NYC based on the program's submission of a written description of its new cost allocation methodology and a certification that the program has begun applying this new method. The methodology complies with OMB Circular A-122, Cost Principles for Non-Profit Organizations.

I want to take this opportunity to thank you and the Congress for your ongoing support of LSC. We take our responsibilities very seriously as stewards of both the principle of equal justice and of the funds appropriated to help ensure that principle is preserved in our nation.

If you have any questions or desire further information, please contact John Constance, Director, Government Relations and Public Affairs, at 202-295-1611.

Sincerely,

A handwritten signature in black ink, appearing to read "John G. Levi". The signature is fluid and cursive, with a large initial "J" and "L".

John G. Levi  
Chairman

Enclosure

cc: Jeffrey E. Schanz, LSC Inspector General

# LEGAL SERVICES CORPORATION



Office of  
Inspector General



Semiannual Report to the Congress  
October 1, 2010 – March 31, 2011

[www.oig.lsc.gov](http://www.oig.lsc.gov)

**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 October 1, 2010 through March 31, 2011.

During this reporting period we completed a major audit of LSC's multi-million dollar Technology Initiative Grant (TIG) program. While recognizing the TIG program's achievements, the audit found that the various deficiencies identified constituted a material weakness in the program's internal control system. In response to our recommendations, LSC management took prompt action to suspend the 2010 grants under the program, pending the development of additional internal controls. Management was subsequently able to report that sufficient progress had been made in implementing the OIG's recommendations and improving controls to permit the resumption of TIG awards by late November 2010.

In addition to our other audit work, we initiated a program to provide improved oversight of the independent audits required annually of LSC grantees. A program of quality control reviews will provide broader coverage in the individual reviews and will ensure that all firms performing grantee audits are subject to review on a four-year cycle.

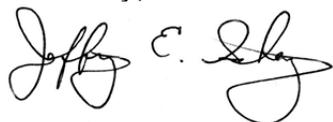
The OIG opened 11 new investigations and closed 15 investigations during the reporting period. A multi-count indictment was obtained charging two individuals in a significant case following an OIG investigation. The former office manager/grants administrator of an LSC grantee and another employee were charged in connection with their activities over several years resulting in the theft of over \$150,000 in federal grant funds. In other cases, former grantee officials were sentenced to imprisonment for their roles in major frauds and thefts from their programs.

We are continuing our outreach and educational initiatives – including fraud awareness briefings, vulnerability assessments, and on-site work with individual grantees – as part of our ongoing efforts to help prevent fraud and abuse in LSC-funded programs.

I would like to add a personal note to recognize Victor Fortuno for his exemplary service as LSC's interim president, and to extend a warm welcome to Jim Sandman, who was appointed as LSC's new president on January 31<sup>st</sup> of this year. I look forward to working closely with him in helping LSC to effectively carry out its mission.

Finally, I wish to express my appreciation to LSC's Board of Directors for the interest and support they have shown for the work of the OIG. I am also 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 fluid and cursive, with the first name "Jeffrey" being the most prominent part.

Jeffrey E. Schanz  
Inspector General  
April 29, 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

In this reporting period, the OIG issued two audit reports, discussed below. The OIG also provided oversight for the LSC Fiscal Year (FY) 2010 financial statement audit and transmitted the final audit report to the LSC Board of Directors. Work in progress at the end of the reporting period included audits at eight grantees. Four of these audits are in the draft report stage. Field work is in progress for the remaining four.

The OIG has responsibility for overseeing the independent public accountant (IPA) audits performed annually at each grantee. The OIG reviewed 22 IPA reports, with fiscal years ending from June 30, 2010 to September 30, 2010, received during the reporting period. This period, the OIG also 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 contracted out to ensure that all IPAs will receive a QCR within the four-year cycle. To implement the new approach, the OIG issued a Request for Proposal to select a contractor to conduct QCRs of IPAs' audits of grantees. On an exception basis, a more targeted, in-depth QCR will be conducted when serious questions arise about the quality of work of a specific IPA. This period the OIG contracted with an accounting firm to conduct two such targeted QCRs.

### **Technology Initiative Grant Program**

At the request of the then Ranking Member of the Senate Committee on Finance, the OIG conducted an audit of LSC's Technology Initiative Grant (TIG) program. The Senator indicated his office had received a number of concerns regarding the TIG program and requested an audit of the mechanisms used to monitor and evaluate the program.

The objectives of the audit were to determine whether the TIG program had appropriate internal controls in place, whether controls were being properly followed, and whether the TIG program was in compliance with applicable laws, regulations, and LSC policies. The OIG reviewed the internal control system used to provide both program and financial oversight. This included control activities with respect to awarding grants, monitoring grant performance, terminating grants, and complying with applicable laws and regulations, as well as with respect to LSC's application of the legal framework governing the TIG program itself.

We found that, taken as a whole, the control deficiencies identified in the audit constituted a material weakness in the TIG program's internal control system. In the OIG's opinion, LSC management did not have adequate assurance that

funds spent on TIG projects met stated goals, met planned timelines, or adhered to established budgets.

We reported that while the TIG program has consistently been credited with achieving its end goal of increasing access to legal representation, the processes for awarding and administering grants needed improvement. Appropriate internal control activities were not in place to provide adequate program or financial oversight. In some instances, LSC regulations were not followed; procedures and processes were not in place to ensure compliance with all LSC laws and regulations.

We found that LSC inconsistently interpreted and applied the statutory framework authorizing TIG grants, and that the process for making TIG awards did not adequately provide for competition among vendors performing major TIG functions. Policies and procedures governing the award and administration of TIG grants were not adequately documented and lacked necessary internal controls, which had a negative impact on the selection of TIG grant recipients, the monitoring of grantees' performance and expenditures, and the termination of TIG grants in a timely manner. Finally, in some cases, LSC did not require compliance with LSC regulations dealing with sub-grants and did not sufficiently monitor TIG recipients' compliance with LSC regulations.

The OIG made one overall recommendation and 35 specific recommendations to address the issues identified and to strengthen internal controls over the TIG program. Overall, the OIG recommended that LSC consider suspending the award of TIG grants until an adequate internal control system was designed and implemented.

The OIG made 35 other recommendations to strengthen the internal controls over TIG program operations. These included recommendations to LSC management in the following three areas:

Legal Interpretation Issues (6 recommendations). These included recommendations intended to:

- Ensure that LSC consistently interprets and applies the statutory framework authorizing TIG grants; and
- Ensure that vendors who receive a significant portion of TIG funding are selected based on competitive processes that ensure best value.

Award and Administration Issues (22 recommendations). These included recommendations to ensure that specific policies and procedures that govern the management and administration of the TIG program are fully documented and establish adequate internal controls and processes to be followed. Areas of emphasis included:

- Documenting award decisions;
- Monitoring performance reporting;
- Terminating non-performing grants;
- Monitoring TIG grantee expenditures;
- Evaluating TIG grantee sustainability plans; and
- Addressing conflicts of interest.

Regulatory Compliance Issues (7 recommendations). These included recommendations to:

- Identify TIG grants subject to LSC’s sub-grant regulations and, for these grants, ensure that sub-grant rules are followed; and
- Develop processes to detect and prevent violations of restrictions by transferees and to monitor program integrity issues on TIG projects.

In response to the report, the LSC President indicated that he had “suspended awarding all 2010 TIGs pending rigorous further review ... [except to] consider awarding some critical TIGs in which failure to do so would result in shutting down technology projects that provide crucial support to vital ongoing activities.” The President further indicated the remaining TIG awards would resume “only when I am confident that sufficient progress has been made in improving internal controls and that doing so will not unreasonably put LSC funds at risk.”

Subsequently, the LSC President reported that as of November 2010 the changes made to the program enabled LSC management to feel “confident that the TIG Program was being administered in a sufficiently secure, efficient, and effective manner ... [therefore] [m]anagement felt comfortable approving most of the 2010 TIG awards on November 23, 2010.” Based on LSC management’s representations and our review of the information provided, the OIG agreed to close the overall recommendation as to the suspension of TIG awards.

Since the report was issued, LSC management has taken necessary actions to close 12 of the total of 36 recommendations. The OIG will continue to monitor and evaluate actions taken by LSC management on the remaining 24 open recommendations.

## **Colorado Legal Services – Audit of Selected Controls**

The OIG assessed the adequacy of selected internal controls in place related to the grantee's operations and oversight. We found that, in general, the internal controls reviewed were adequate. Grantee disbursements tested were adequately supported. Internal controls over reimbursements and internal management reporting and budgeting were adequate and followed. In addition, internal controls over compliance with specific LSC regulations reviewed were adequate.

However, we reported that controls needed to be strengthened or formalized in four specific areas. The audit found that the grantee did not have an accurately documented cost allocation process in place to adequately ensure proper distribution of indirect costs and non-labor related direct costs among grants. Although adequate written policies and procedures existed concerning Client Trust Fund accounting, the grantee did not follow the policies and procedures contained in its current Accounting Manual. Also, the grantee did not maintain a master inventory list for use in reconciling physical property inventory. Lastly, the grantee did not have written procedures documenting the arrangements with employees governing the reimbursement for business use of employee-owned personal digital assistants (PDAs), including cell phones.

The OIG made five recommendations to address these issues:

- Implement a cost allocation methodology that properly allocates all costs;
- Fully document the cost allocation methodology in the grantee's Accounting Manual;
- Ensure, through training and supervisory oversight, that grantee staff follows the Client Trust Fund accounting policies and procedures contained in its Accounting Manual;
- Create a master inventory list that contains the fixed assets owned by the grantee and reconcile the list with the accounting records; and
- Implement written procedures in the Accounting Manual documenting arrangements with employees for reimbursement for the business use of employee-owned PDAs, and require that only business use be reimbursable with program funds.

Grantee management has provided the OIG with documentation supporting that action was taken to implement all recommendations in the report. The OIG

evaluated the grantee's corrective actions and now considers all recommendations as closed.

### **FY 2010 Corporate Audit**

The FY 2010 LSC financial statement audit report was issued this reporting period and transmitted to LSC's Board of Directors. The Corporation's financial statement audit is conducted by an independent public accounting firm (IPA) under contract to and subject to general oversight by the OIG. The OIG reviewed the work of the IPA and found it in compliance with generally accepted government auditing standards.

The *Independent Auditor's Report* stated that LSC's financial statements present fairly, in all material respects, the financial position of LSC as of September 30, 2009, and the results of its operations and changes in its fund balance for the year then ended. The auditor's *Report of Deficiencies in Internal Control Over Financial Reporting and Other Matters* did identify some control deficiencies, however these did not constitute significant deficiencies or material weaknesses.

## **Statistical Summary**

### **Audit Reports**

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### **Recommendations to LSC Grantees**

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### **Recommendations to LSC Management**

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Issued during reporting period.....	36
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## **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.

While these audits are not performed by the OIG, the OIG does provide guidance to the IPAs and grantees, and oversees the IPA process. The OIG's oversight of the IPAs consists primarily of two activities: (1) desk reviews, and (2) the recently initiated quality control reviews. The purpose of both reviews is to identify significant IPA findings requiring follow-up by LSC management, determine whether the IPA's work meets applicable professional standards, and ensure that the work is conducted in accordance with the instructions issued by this office.

### **Desk Review of IPA Reports**

The OIG conducts a desk review of all IPA reports issued to grantees. This process enables the OIG to identify and forward to LSC management significant findings that require management's attention. The OIG then tracks which recommendations have been acted upon and what actions have been taken by the grantee. In addition, the OIG uses information from its review of IPA reports as part of its risk assessment and planning process for audits, investigations, and other reviews.

### **Quality Control Reviews**

#### ***Request for Proposals for Quality Control Reviews***

The OIG issued a Request for Proposals this reporting period to select an accounting firm to conduct QCRs of the IPA audit work associated with the grantees' required annual audits. This is the first step in implementing the OIG's new program to review every IPA during a four-year cycle.

These 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 this office. The selected contractor will also identify any issues that may require additional

attention or any additional audit work by the IPA under review. After each QCR is completed and submitted to OIG by the contractor, the OIG will issue a report to the IPA on the results of the review. In addition, the contractor will provide an annual summary report, on the basis of all the QCRs it performs, identifying any significant or recurring issues. The OIG will use the results of the QCRs to improve or add to its guidance to the grantees and IPAs.

### Contract for Targeted Quality Control Reviews

The OIG entered into a contract with an accounting firm to perform in-depth QCRs of two different IPAs. The regular annual audits conducted by the subject IPAs did not detect significant issues that had gone on for many years. The targeted QCRs will focus in particular on the undetected issues in determining whether the audits were conducted in accordance with professional standards and the OIG's guidance, and whether the OIG might be able to issue additional guidance or information to help detect significant frauds or internal control weaknesses.

### 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. The OIG reviews each report and refers appropriate findings and recommendations to LSC management for follow-up. LSC management ensures that grantees submit 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 ordinarily 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. These audit reports and findings reflect the work of the IPAs, not the OIG.

During the reporting period, the OIG reviewed 22 IPA audits of grantees with fiscal year ending dates from June 30, 2010 through September 30, 2010. These audit reports contained four findings. This period the OIG determined that all four findings were not significant or that corrective action had already been

completed and closed the findings. No findings in the grantee audit reports for fiscal years ending from June 30, 2010 through September 30, 2010 were referred to LSC management for follow-up.

## **INVESTIGATIONS**

The OIG opened 11 investigations during this reporting period. These included five criminal investigations, two compliance matters, and four fraud vulnerability assessments. The criminal investigations included allegations of embezzlement, falsification of records, and theft of cash and property from LSC programs. The compliance investigations included allegations of violations of LSC statutes and regulations involving matters such as retaliation and the outside practice of law.

During the reporting period the OIG closed 15 investigations. These included ten criminal investigations, three compliance matters, and two fraud vulnerability assessments. The OIG also issued eight Inspector General subpoenas in connection with our ongoing investigations.

### **Criminal Proceedings**

#### **Indictment**

##### **Former Grantee Employees Indicted for Theft of \$150,000**

A 20-count federal indictment was returned charging the former office manager/grants administrator of a past LSC grantee and her daughter, also a former grantee employee, with conspiracy; mail and wire fraud; theft of federal funds; and falsification of records. The two were charged for fraudulently converting to their own use and benefit over \$150,000 in federal grant funds. Trial for this case has been set for November of this year. The former acting executive director of the grantee was also named in the indictment as an unindicted co-conspirator. He was previously convicted on a plea of guilty to theft of federal grant funds for his part in the scheme and is currently awaiting sentencing. Investigation of this case was handled jointly by the OIG, the Department of Justice OIG, and the FBI.

#### **Sentencing**

During the reporting period three individuals were sentenced to terms of imprisonment in cases arising out of OIG investigations.

##### **Former Chief of Finance and Accomplice Sentenced for Theft of Over \$1 Million**

The former chief of finance of a grantee and his outside accomplice were sentenced in federal court as a result of their scheme to defraud an LSC grantee. The two had, among other things, created a sham office supply company which they used to submit false and inflated invoices to the grantee, ultimately

defrauding the program of approximately \$1.2 million. In the previous reporting period, both subjects were convicted on pleas of guilty to theft from a program receiving federal funds. The former chief of finance was sentenced to 30 months imprisonment; his accomplice was sentenced to 15 months imprisonment. Both were ordered to make full restitution of the moneys stolen from the program. In addition, both were to be placed on three years of supervised probation upon release from prison.

### **Former Bookkeeper Sentenced for Theft of Grant Funds**

The former bookkeeper of an LSC grantee was sentenced in federal court to 22 months imprisonment as a result of her scheme to defraud the program of over \$188,000. The subject had been convicted on a plea of guilty to a charge of theft from a program receiving federal funds. The former employee had defrauded the program by writing program checks to herself and recording the transactions as payments to existing program vendors; making unauthorized bank withdrawals using the grantee's ATM card; making unauthorized electronic funds transfers to pay personal bills; and making improper charges to the grantee's credit card. The grantee reported that full restitution has been made for the embezzled funds.

### **Personnel Actions**

The following personnel actions were taken by grantees as a result of or in connection with investigations and/or audits undertaken by the OIG.

#### **Removal of Executive Director**

During the reporting period, a program executive director was removed from his employment by the grantee's board of directors following an OIG investigation reporting on multiple questionable practices and apparent violations of LSC regulations, and an OIG audit of the grantee's financial practices, resulting in questioned costs of over \$300,000.

#### **Removal of Executive Director**

During the reporting period, a program executive director was removed from her employment by the grantee's board of directors, citing financial mismanagement and multiple concerns regarding misconduct and violations of policy on her part. The board of directors' action was taken following investigation by an outside counsel and the initiation of an investigation by the OIG. The OIG also initiated an audit of the grantee's financial controls during the period.

#### **Removal of Office Manager**

The office manager/assistant bookkeeper at an LSC grantee was removed from employment by grantee management due to the mishandling of client funds and

the comingling of petty cash and personal funds. Following OIG investigation, the former office manager agreed to make full restitution to the program.

## **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 a fraud awareness briefing for an LSC-funded program in Tennessee. Briefings are scheduled in the coming months for programs in California, Ohio, 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 and potential problem areas.

This period the OIG initiated a 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 is integrating project findings with the FVA program.

Two FVAs were completed during the reporting period.

### **Fraud Alert**

The OIG issued a “Fraud Alert” memorandum to all executive directors on the subject of “Employee Theft of Cash.” The alert was prompted by recurring reports of loss or theft of cash from grantees’ offices. We found that even when the amounts involved have been relatively small, these incidents have been particularly troubling for program managers. In addition to the direct loss of client funds, such incidents can bring into question the trustworthiness of the (often multiple) employees responsible for handling cash and create difficult personnel issues for managers and staff alike. The alert identified common factors that may have contributed to the losses or thefts and provided suggestions as to preventive measures for managers to consider.

### **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 56 Hotline contacts. Of these matters, 13 were referred to LSC management for follow-up; 11 were opened as investigations; 5 are open pending further inquiry; and the remaining 27 were closed after review and, where possible, response to the Hotline complaint.

The OIG has worked both to improve Hotline operations and to increase awareness of the Hotline throughout LSC and the grantee community. This period the OIG produced a Spanish language version of its Hotline poster and distributed it to grantees across the country to post in their offices.

## **Statistical Summary**

### **Investigative Cases**

Open at the beginning of period.....	25
Opened during the period .....	11
Closed during period.....	15
Open at the end of period .....	21

### **Prosecutorial Activities**

Referred this period .....	1
Accepted for prosecution .....	1
Declined for prosecution .....	0
Indictments/Informations.....	2
Sentenced.....	3

### **Investigative Activities**

Inspector General subpoenas issued .....	8
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## **OTHER OIG ACTIVITIES**

### **Litigation**

As noted in previous Semiannual Reports, in 2006 the OIG issued an interim report on the activities of California Rural Legal Assistance (CRLA), finding substantial evidence that CRLA had violated federal law and regulations governing LSC grantees. The OIG could not complete its investigation due to CRLA's refusal and/or failure to respond to an OIG subpoena seeking information relevant to the investigation.

In March 2007, the U.S. Department of Justice filed a subpoena enforcement petition in the United States District Court for the District of Columbia. In August 2008, following resolution of a number of procedural issues, the Court heard arguments on the petition. At the request of the Court, the parties subsequently agreed to attempt to resolve their differences through mediation. Although mediation proved unsuccessful, in April 2009 the LSC OIG submitted to the Court additional briefing regarding a proposal it had developed to resolve all outstanding issues in the enforcement proceeding.

As of this date, the subpoena enforcement action remains pending as the parties await the Court's ruling on all outstanding issues in the case.

### **Freedom of Information Act**

The OIG is committed to complying fully with the requirements of the Freedom of Information Act (FOIA). All FOIA requests received by the OIG this period were responded to within the requisite timeframes.

### **Professional 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 IG groups. Additionally, the OIG routinely responds to requests for information or assistance from other OIGs.

## 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 the Special Inspector General for Iraq Reconstruction on January 28, 2009. (We note that a peer review of the OIG is scheduled to take place during the next reporting period.)

(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 the OIG was of the Office of Inspector General for the National Railroad Passenger Corporation (Amtrak), and was completed on September 30, 2009. We have been advised by that office that our recommendation that they implement a system that accurately tracks required continuing professional education (CPE) credits has been partially implemented. They advised that CPE information is being recorded and reviewed to ensure CPE requirements are being met, and that an automated system is being developed for use during this fiscal year. They reported no other recommendations as outstanding or not fully implemented.

# TABLE I

## Audit Reports Issued for the Period Ending March 31, 2011

<u>Report Title</u>	<u>Date Issued</u>	<u>Questioned Costs</u>	<u>Funds Put to Better Use</u>	<u>Unsupported Costs</u>
Audit of LSC's Technology Initiative Grant Program	12/08/10	\$886,673	\$0	\$0
LSC's FY 2010 Financial Statement Audit	01/27/11	\$0	\$0	\$0
Report on Selected Internal Controls: Colorado Legal Services	02/18/11	\$0	\$0	\$0

## TABLE II

### Audit Reports Issued with Questioned Costs for the Period Ending March 31, 2011

	NUMBER OF REPORTS	QUESTIONED COSTS	UNSUPPORTED COSTS
A. For which no management decision has been made by the commencement of the reporting period.	1	\$318,768	\$0
B. Reports issued during the reporting period	1	\$886,673	\$0
Subtotals (A + B)	2	\$1,205,441	\$0
C. For which a management decision was made during the reporting period:	1	\$318,768	\$0
(i) dollar value of recommendations that were agreed to by management	1	\$133,860	\$0
(ii) dollar value of recommendations that were not agreed to by management	1	\$174,908	\$0
D. For which no management decision had been made by the end of the reporting period	1	\$886,673 <sup>1</sup>	\$0
Reports for which no management decision had been made within six months of issuance	0	0	\$0

<sup>1</sup>The OIG referred these questioned costs to LSC management for action after the close of the reporting period.

### TABLE III

## Audit Reports Issued with Funds to Be Put to Better Use for the Period Ending March 31, 2011

	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 Was Made By The End Of The Reporting Period

<u>Report Title</u>	<u>Date Issued</u>	<u>Questioned Costs</u>	
Report on Selected Internal Controls: Legal Aid and Defender Association, Inc.	02/05/09	\$273,054	One recommendation remains open. Questioned cost proceedings were completed by LSC and reported in a previous Semiannual Report.
Report on Selected Internal Controls: Legal Services New York City	12/11/08	\$0	One recommendation remains open while awaiting confirmation that new allocation system has been implemented.
Report on Selected Internal Controls: Capital Area Legal Services Corporation	09/27/10	\$318,768	Final management decision on questioned costs issued on March 23, 2011. All 21 recommendations contained in the report are still open.

## 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	None
Section 5(a)(1)	Significant problems, abuses, and deficiencies.	3-5; 12-13
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.	22
Section 5(a)(4)	Matters referred to prosecutive authorities.	12-13; 16
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.	19
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.	20
Section 5(a)(9)	Statistical table showing number of reports and dollar value of recommendations that funds be put to better use.	21
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.	22
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.	18

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



**OFFICE OF INSPECTOR GENERAL  
HOTLINE**

**IF YOU SUSPECT –**

**FRAUD** INVOLVING LSC GRANTS OR OTHER FUNDS  
**WASTE** OF MONEY OR RESOURCES  
**ABUSE** BY LSC EMPLOYEES OR GRANTEEES  
**VIOLATIONS** OF LAWS OR LSC REGULATIONS

**PLEASE CALL OR WRITE TO US AT –**

<b>PHONE</b>	<b>800-678-8868 OR 202-295-1670</b>
<b>FAX</b>	<b>202-337-7155</b>
<b>E-MAIL</b>	<b><u><a href="mailto:HOTLINE@OIG.LSC.GOV">HOTLINE@OIG.LSC.GOV</a></u></b>
<b>MAIL</b>	<b>P.O. BOX 3699 WASHINGTON, DC 20027-0199</b>

**UPON REQUEST YOUR IDENTITY WILL BE KEPT CONFIDENTIAL.  
REPORTS MAY BE MADE ANONYMOUSLY**