

## **Assessment of Compliance with Restrictions and the Compliance Oversight System as of September 30, 1999**

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October 29, 1999

The purpose of this report is to provide an assessment of grantee compliance with restrictions on the services provided by grantees, and an assessment of the effectiveness of the oversight system itself.

### **Background**

The Congress imposed a new compliance oversight system in the Legal Services Corporation appropriations statute for fiscal year 1996. LSC management had made monitoring visits to grantees on a periodic basis until 1994, when monitoring was suspended as a program of peer reviews was being designed to replace it.

The new compliance oversight system is based on the annual financial audits of grantees conducted by independent public accounting firms, or "IPAs". The statute required that these audits also check grantee compliance with the restrictions and prohibitions on the legal services provided by grantees, in accordance with guidance established by the Office of Inspector General, or "OIG." The law also required that the OIG refer IPA findings for follow up and track the progress of corrective actions by grantees and LSC management.

### **Implementing Actions**

The LSC OIG published a new Audit Guide in Fall 1996, which included a Compliance Supplement that provided guidance to the IPAs conducting the audits. The Compliance Supplement covers 24 regulations, provides a summary of each regulation and suggests audit procedures for the IPAs to follow in testing grantee compliance with the regulations. The Compliance Supplement has been updated twice, primarily as a result of changes to LSC laws and regulations.

The OIG also developed the Audit Information Management System (AIMS) in anticipation of the substantial administrative workload associated with the new compliance oversight system. The receipt and review of the several hundred grantee audit reports due each year, the resultant reporting of findings to LSC management, and the subsequent tracking of corrective actions, would have completely consumed the OIG audit staff resources without AIMS.

### **Compliance Verification**

The OIG uses a three-prong strategy to verify compliance with the congressionally-imposed prohibitions and restrictions. As required by law, the grantees hire independent public accountants to check compliance as part of the annual financial audits, and the OIG reviews these reports to determine if they meet our audit requirements. The OIG refers significant IPA findings to LSC management for follow up to ensure that the grantees correct the reported problems. The OIG conducts Audit Service Reviews which are quality controls checks of the IPAs' work. The OIG will conduct a series of program integrity audits that will test grantees' compliance with the prohibition on providing support with LSC funds to organizations that engage in restricted or prohibited activities.

## Grantee Audit Results

The independent public accountants have submitted 752 audit reports since the inception of the new system. These audit reports cover all grantees with fiscal year ends between December 31, 1996 and May 30, 1999. The Office of Inspector General has published summary reports covering various segments of this time period. [[AU97-002](#), [AU98-002](#), [AU98-003](#), and [AU99-016](#)]. The IPA reports contained a total of 162 significant findings, which were referred to LSC management for corrective action.

The independent public accountants have reported only three findings of practice restrictions thus far. All of these were in the initial period. In one, a class action case was not divested until 13 days after the statutory deadline for implementation; in another, a motion to withdraw from representation of a group of aliens was opposed by the state and pending at the time of the audit. A third finding reported that a grantee employee had used an organizational computer on one occasion during the employee's campaign for state office.

[Figure 1](#) depicts the nature of the remaining 159 findings. There were 48 findings of internal control weaknesses, 45 findings of missing and/or unsigned documents, 35 findings of various procedural problems, 19 findings relating to timekeeping procedures, and 12 findings concerning LSC fund balance or case management reporting.

Of these findings, the 45 reporting missing documentation are of greatest concern, because missing documentation has the potential to conceal noncompliance.

**Figure 1**

<b>SUMMARY OF SIGNIFICANT FINDINGS IN GRANTEE AUDIT REPORTS REFERRED TO LSC MANAGEMENT</b>					
<b>Type of Finding</b>	<b>216 Grantee Audits with FY-end 12/31/96</b>	<b>266 Grantee Audits for Calendar Year 1997</b>	<b>263 Grantee Audits for Calendar Year 1998</b>	<b>7 Grantee Audits with FY-end 1/1/99 - 5/31/99</b>	<b>TOTAL</b>
Noncompliance with prohibitions and/or restrictions	3				3
Internal Control Problems	16	9	23		48
Procedures lacking or not followed					
Reconciliation of client trust accounts					
Processing financial data					
Weaknesses over cash receipts/disbursements					
Segregation of duties					

Missing and/or Unsigned Documents (I.e., client statement of facts, citizenship attestation, retainer agreements)	24	10	10	1	45
<b>Timekeeping Procedures and/or Systems Problems</b>	11	3	5		19
<b>Case Management Reporting</b>		2	3		5
<b>LSC fund balance was greater than 10 percent of LSC support requiring a waiver from LSC</b>	5	1	1		7
<b>Other Procedural/Regulatory Problems</b>	12	5	17	1	35
Qualified Opinion in Audit Report					
FDIC insurance limits exceeded					
Implementing procedures for regulations lacking					
PAI shortfall					
Questioned Cost					
Uncorrected Prior Year Finding					
<b>TOTAL NUMBER OF FINDINGS</b>	<b>71</b>	<b>30</b>	<b>59</b>	<b>2</b>	<b>162</b>

### Effectiveness of Grantee Audits

The above findings provide reasonable assurance of system compliance only if the audits conducted by the independent public accountants are effective. To obtain information on audit effectiveness, the OIG began performing Audit Service Reviews, or ASRs, in fiscal year 1998. ASRs are on-site reviews of the independent auditors' work papers to verify that effective compliance checks were made, all material findings were reported, and the audit reports provided reasonable assurance that the grantees complied with the prohibitions and restrictions.

Ten ASRs were performed in fiscal year 1998 and early fiscal year 1999. Four of the 10 grantee audits were inadequate and the OIG required the IPAs to do additional work to correct the deficiencies. Two audits were found inadequate because the IPAs were not given full access to case file information; one was given only redacted information. In one audit the IPA did not adequately test compliance due to a sampling deficiency, and in another audit the IPA did not adequately verify the extent of the grantee's involvement in a restricted case.

The OIG performed 60 ASRs in fiscal year 1999. Each ASR examined the independent accountant's work on the 14 regulations noted as requiring special compliance reporting in the OIG Compliance Supplement. These 14 regulations cover all of the restrictions imposed and/or amended by the fiscal year 1996 appropriations statute.

The ASRs determined that 49 of the 60 audits adequately reviewed all 14 regulations. Three audits were deficient primarily due to a systemic flaw in the case samples. Two audits conducted by the same auditor were not performed in accordance with auditing standards

and therefore the adequacy of the audit tests could not be determined. Another auditor did not adequately test a grantee's compliance with the regulation prohibiting collection of attorney fees and, therefore failed to detect a violation of the regulation. The remaining five audits involved isolated deficiencies in one to three regulations.

Of the 60 audits reviewed, the regulation with the lowest level of adequate checking was timekeeping, where 88 percent of the audits proved effective. The remaining 13 regulations were adequately checked in between 90 percent and 97 percent of the audits. [Figure 2](#) depicts the degree to which each of the 14 regulations was adequately checked by the IPA.

The 1999 ASRs showed that the IPA's review of grantees' compliance with LSC prohibitions and restrictions is working although some improvements are needed. The IPA reviews provide a reasonable level of assurance that the grantees are complying with the LSC prohibitions and restrictions. There were no indications that widespread violations of practice restrictions have occurred

**Figure 2**

<b>LSC OIG SUMMARY OF REGULATIONS ADEQUATELY TESTED FY 1999 AUDIT SERVICE REVIEWS</b>						
<b>ITEM</b>	<b>REGULATION</b>	<b>DESCRIPTION</b>	<b>AUDITS TESTING ADEQUATE</b>	<b>%</b>	<b>AUDITS TESTING INADEQUATE</b>	<b>%</b>
1	1627	Subgrants	58	97%	2	3%
2	1638	Solicitation	58	97%	2	3%
3	1610	Use of Non-LSC Funds	58	97%	2	3%
4	1642	Attorneys' Fees	57	95%	3	5%
5	1612	Lobbying & Certain Other Activities	57	95%	3	5%
6	1617	Class Actions	55	92%	5	8%
7	1626	Alien Representation	55	92%	5	8%
8	1632	Redistricting	55	92%	5	8%
9	1633	Eviction Proceedings	55	92%	5	8%
10	1636	Client Identity & Statement of Facts	55	92%	5	8%
11	1637	Prisoner Litigation	55	92%	5	8%
12	1639	Welfare Reform	55	92%	5	8%
13	1620	Priorities	54	90%	6	10%
14	1635	Timekeeping	53	88%	7	12%

The 1999 ASRs also identified some areas where OIG guidance could be improved to ensure adequate sample size for testing purposes and to account for the interrelationship of some regulations. The OIG will make those improvements, and will perform Audit Service Reviews

on a continuing basis as a routine check of the oversight system. The OIG will continue to evaluate the compliance oversight system as part of our continuing risk assessment.

### **Program Integrity**

The audits of the independent public accountants have not reported noncompliance with practice restrictions, and the ASRs confirmed that the compliance checks for the 14 regulations were adequate for 88 percent to 97 percent of the audits. However, it would be possible for a grant recipient to evade practice restrictions by diverting LSC funds or other resources to entities that engage in restricted activities. LSC regulation 45 C.F.R Section 1610.8 requires grantees to maintain separation from such organizations.

The Office of Inspector General had planned to conduct a series of audits of program integrity in fiscal year 2000. However, because problems with Case Statistical Reports continue to be detected, additional work in that area in fiscal year 2000 is required. As a consequence, the OIG will be unable to conduct the program integrity audit series until fiscal year 2001, except for one program integrity audit in fiscal year 2000 to refine its procedures for the following year.

### **Summary**

The independent public accountants have reported only three findings of noncompliance with practice restrictions in the approximately three years since the 1996 appropriation established the new compliance oversight system. Two of the three findings were transition-related problems.

Sixty Audit Service Reviews of the 1997/1998 audits conducted by the independent public accountants determined that the grantee audits adequately checked the governing regulations 88 percent to 97 percent of the time.

Last, program integrity audits are needed to ensure that grantees have complied with LSC regulatory requirements for separation from organizations that engage in restricted activities. The LSC OIG plans to perform those audits in fiscal year 2001.