

**LEGAL SERVICES  
CORPORATION**

Office of  
Inspector General



Semiannual Report to the Congress  
April 1, 2007– September 30, 2007

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

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

### **A MESSAGE FROM THE ACTING INSPECTOR GENERAL**

This Semiannual Report sets forth the significant activities and accomplishments of the Office of Inspector General (OIG) for the period April 1, 2007 through September 30, 2007. It reflects our overall efforts to improve the effectiveness and efficiency of the Legal Services Corporation (LSC), and to protect the operations of LSC and its grant recipients from fraud and abuse. It also details our continuing efforts to oversee the system of routine monitoring of compliance with the restrictions on the use of LSC funds by grantees.

This reporting period finds the OIG going through a change of leadership. Kirt West left his position as the Inspector General (IG) in August to accept a position in the private sector. The LSC Board of Directors is moving quickly to select a permanent replacement. We look forward to welcoming the next Inspector General soon.

Among our significant activities during this reporting period, we issued our report on the Office of Program Performance as part of our continuing broad review of LSC's oversight of grantees. We are nearing completion of our work on the Office of Information Management, the final major LSC component to be reviewed in this effort. We also transmitted the Fiscal Year 2006 Financial Statement Audit to the Board of Directors. In addition, the OIG issued eight Audit Service Review (ASR) reports. We opened 28 new investigations and closed 15 investigations. A joint OIG audit and investigation team is continuing its work on a significant financial fraud case at one of LSC's grantees.

The OIG continues its involvement in two important litigation matters. First, the OIG, in conjunction with the U. S. Department of Justice, is pursuing a subpoena enforcement action in support of its ongoing investigation of California Rural Legal Assistance, Inc. Second, the OIG is assisting the Office of Legal Affairs and outside counsel in the defense of a lawsuit challenging LSC's program integrity regulation.

The Government Accountability Office (GAO) issued its report on corporate governance and accountability in August 2007. The draft report on GAO's work on grants management at LSC is due out shortly. The OIG will, in accordance with the IG Act, avoid duplicating the work of GAO.

April 1, 2007 – September 30, 2007

I wish to express my appreciation to the Board of Directors, LSC management, and to the Congress, for their support and cooperation during this period of transition. I will continue to work to ensure that the OIG is fulfilling its mission to help improve the effectiveness and efficiency of the Corporation, and to prevent and detect fraud, waste, and abuse.

Sincerely,

A handwritten signature in cursive script that reads "Ronald D. Merryman".

Ronald D. Merryman  
Acting Inspector General  
September 30, 2007

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## OFFICE OF INSPECTOR GENERAL OVERVIEW

The LSC Office of Inspector General operates under the Inspector General Act of 1978, 5 U.S.C. App. 3. In 1988, Congress amended the IG Act and required LSC and about 30 other, mostly smaller, federally funded entities to establish independent Offices of Inspector General.

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. Thus, the OIG assists management in fostering effective operations, in identifying and overcoming obstacles to good program management, and in preventing future problems. The OIG must also identify and report on current problems.

The OIG's primary tool for achieving these missions is objective and independent fact-finding, performed through financial, performance and other types of audits, evaluations and reviews, as well as through investigations into allegations of wrongdoing. Its fact-finding activities enable the OIG to develop recommendations to LSC, Congress and grantee management for actions or changes that will correct problems, better safeguard the integrity of funds, improve procedures, or 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 that are 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 the 1996 Congress, LSC's annual appropriation has directed that an additional tool for monitoring grantee compliance with legal requirements is to be 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 grantee compliance.

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, consultants and experts.

To ensure the objectivity of the IG, the IG Act grants the LSC IG the independence to determine what reviews are performed; to gain access to all documents needed for OIG reviews; to publish findings and recommendations based on OIG reviews; and to report OIG findings and recommendations to the LSC 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.

§2996-2996I, other than those transferred to the OIG under the IG Act, and those otherwise assigned by Congress, for example in the FY 1996 Appropriations Act.

The IG must report 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 occasionally 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), while others will be of more general interest to management.

To be effective, the OIG works cooperatively with the Board and management, 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 concluded its review of the Office of Program Performance, part of its ongoing overall review of LSC's grantee oversight program. The OIG also transmitted the Corporation's FY 2006 Financial Statement Audit to the Board of Directors. The office continued its focus on conducting Audit Service Reviews (described below) and identifying risk factors that may require a review of selected aspects of a grantee's operations. As a member of a joint LSC OIG audit and investigative team, OIG auditors identified several fraud risk factors for one grantee. A financial fraud investigation is currently underway. Because of serious internal control and other management issues, LSC has terminated funding for this grantee.

### Interim Report on the Office of Program Performance

During this period, the OIG issued the final audit report on the Office of Program Performance (OPP). This audit found that the programs managed by OPP generally did not duplicate the efforts of other LSC offices providing oversight to grantees. The OIG detected a system error in the scoring of grant applications that was corrected during the course of the audit. The system error did not impact LSC decisions resulting from the scoring of the applications. The OIG found that OPP could leverage its limited resources and facilitate more frequent oversight coverage of grantees by restructuring the scope of some on-site grantee program reviews. Management had taken action to address these findings during the audit so no recommendations were necessary. The OIG also found that the grantee evaluation process could be improved by developing more comprehensive measures of productivity and implementing new procedures to track significant recommendations. LSC management accepted and is implementing these recommendations.

### Fiscal Year 2006 Corporate Audit

The Fiscal Year 2006 Financial Statement Audit was issued this reporting period. The report disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards. The report noted that there were no matters involving the internal control over financial reporting and its operation that were considered to be material weaknesses. The audit firm issued a Management Letter advising the Board of three matters where internal control and operating efficiency could be strengthened. These areas pertained to data security, the accounting and reporting of fixed assets, and documenting certain control procedures.

## Audit Service Reviews

The OIG is responsible for the oversight of the Independent Public Accountants (IPAs) who are selected by the grantees to perform their annual financial and compliance audits. To fulfill this responsibility, the OIG conducts Audit Service Reviews (ASRs), which are reviews of the audit documentation of selected IPAs to ensure that they adequately tested the grantee's compliance with LSC regulations. During this period, the OIG issued eight ASR reports. We have requested additional information from some IPAs prior to finalizing nine additional ASR reports.

## Review of Grantees' Annual Audit Reports

LSC grantees are responsible for submitting annual financial statement and compliance audits to the OIG. Each grantee contracts with an IPA to conduct this audit in accordance with Government Auditing Standards, OMB Circular A-123, and the LSC OIG Audit Guide for Recipients and Auditors.

During the reporting period, the OIG reviewed 115 IPA audits of grantees with fiscal years ending December 31, 2006. Of the 115 audit reports reviewed, 80 contained no findings and 35 contained a total of 81 findings. Of the 81 findings, 22 either had corrective action already implemented or the OIG determined that the finding was not significant. The remaining 59 findings were referred to LSC's Office of Compliance and Enforcement for follow-up action.

## **Work In Progress**

### Grantee Financial Fraud

Because of significant internal control issues contained in the annual audit report, a grantee filed a complaint with LSC claiming that the IPA's work did not meet standards and that the findings were incorrect. LSC management referred the complaint to the OIG. The OIG reviewed the issues raised about the IPA's work in the complaint and visited the IPA and grantee. The team reviewed appropriate documentation and interviewed the IPAs involved, the leadership of the program, and the program's chairman of the board. LSC management has taken corrective action against the grantee because of the control issues identified in the IPA reports and because of other serious program management concerns.

While addressing the control issues in the complaint, a joint OIG audit and investigative team found significant fraud indicators. After coordinating with the Department of Justice which also provides a grant to the program, members of the joint OIG team traveled to American Samoa in August of 2007. The team was able to confirm that the internal control issues identified in the audit reports for the most part still existed. In addition, the team identified many questionable payments to several staff members. Currently, these payments are being reviewed by the OIG,

other federal agencies, and local authorities. LSC management has terminated funding for the program.

#### Audit of the Office of Information Management (OIM)

The work is nearing completion and a draft report on allocating funds will be issued shortly. A second draft report should be completed in the coming reporting period and will cover other areas of OIM management related to oversight functions.

#### Audit of Puerto Rico Legal Services, Inc.

The OIG initiated a limited scope audit of Puerto Rico Legal Services. The objective of a limited scope audit is to assess the adequacy of controls in place as they relate to specific grantee operations and oversight, including program expenditures, administrative case management and related issues. As part of this audit the OIG is reviewing selected internal controls throughout the grantee's organization and conducting applicable testing. Related office policies and procedures are also being reviewed, as well as any other relevant documents. Our focus is on the central administrative office and the administrative oversight functions located in specific branch offices. The OIG is awaiting documentation requested from the grantee before completing this review.

#### Review of OIG's Internal Controls

The OIG has initiated a review of its own system of internal controls to ensure that controls are in place and working properly. When completed, the report will be published and posted to the OIG's web page.

Audit Reports

Open at beginning of reporting period	1
Issued during Reporting Period	2
Closed during Reporting Period	3
Open at end of reporting period	0

Recommendations to LSC Grantees

Pending at beginning of reporting period	0
Issued during reporting period	0
Closed during reporting period	0
Pending at end of reporting period	0

Recommendations to LSC Management

Pending at beginning of reporting period	7
Issued during reporting period	2
Closed during reporting period	9
Pending at end of reporting period	0

## INVESTIGATIONS

The OIG opened 28 investigations during the reporting period. These included 18 compliance matters (including one survey on privacy information), 7 criminal investigations, 2 financial risk assessments and 1 administrative investigation. The compliance investigations included allegations involving matters such as prohibited political activity, financial eligibility, attorneys' fees, and solicitation. The seven criminal investigations included embezzlements and thefts of property from LSC programs. During the reporting period, the OIG closed 15 investigations. These included four compliance matters, eight criminal investigations, two financial risk assessments, and one administrative case.

Significant investigative activities noted for this period include the identification of three grantee employees in an alleged embezzlement scheme to steal grant funds. This case is being pursued by local prosecutors. In addition, a fraud advisory alert was issued to all LSC program executive directors in an effort to reduce the loss of funds to LSC grantees due to employee embezzlement and theft of funds by preventing and detecting losses dealing with the fraudulent purchase of office supplies.

The OIG issued and served one Inspector General Subpoena in connection with an ongoing investigation related to the embezzlement of filing fees collected from grantee clients.

### OIG Investigation of Potential False Statements to Congress

An OIG investigation of a management official disclosed no evidence that the official actually knew that two submissions to Congress were inaccurate and incomplete at the time they were transmitted. The investigation did establish that the two submissions to Congress contained statements and representations that were false or misleading and omitted certain facts. The investigation found that LSC did not sufficiently review information in its possession to ensure accurate statements to Congress. The investigation is closed.

### Compliance Investigations Initiative

OIG investigations has for the past several years focused on investigating allegations of fraud that could result in criminal prosecutions. Those investigations were and still are being conducted by staff with extensive criminal investigative experience. To complement our criminal investigative efforts, the OIG increased its activities conducting compliance investigations. The OIG recently hired two experienced attorneys to serve as investigative counsels. The investigative counsels are responsible for conducting investigations to determine whether there are violations of the LSC Act, including restrictions imposed by LSC's appropriations, and or violations of LSC regulations. In their first reporting period,

our investigative counsels opened 18 cases (including the survey on privacy information), and closed 4 cases. Issues addressed included matters such as requests for attorneys' fees, solicitation of clients, litigating class action lawsuits, engaging in political activities, and part-time employees' conducting restricted activities. The OIG intends to work with and coordinate compliance investigation activities with LSC counterparts, including the Office of Compliance and Enforcement and the Office of Program Performance, in order to avoid duplication of effort and ensure adequate coverage of compliance issues.

#### IG Fraud Alert Issued

In August 2007, the Acting Inspector General issued a special fraud alert letter to all Executive Directors in LSC's grantee community, reporting on recent OIG investigations involving grantee employees. The alert described two long-running embezzlement schemes in which trusted employees used their office's credit cards to purchase office equipment and supplies in order to sell them for cash or convert them to personal use. The alert also contained specific recommendations for improving internal control and other preventive measures, that grantees can take to help prevent such occurrences and to protect scarce funds from theft or embezzlement.

#### Personal and Private Information Survey

In light of recent events, such as the loss of claims data by federal agencies and the unintentional disclosure of personally identifiable information, such as social security numbers and credit card accounts, the OIG determined that it would be beneficial to LSC management to obtain information regarding the collection, maintenance and security of personal and private information at LSC. The OIG Office of Investigations developed, conducted, and is finalizing a survey of LSC offices to identify personal and private information (PPI) maintained in LSC paper and electronic records, and to determine what steps have been taken to ensure that PPI records are being properly collected, maintained, used and disclosed. The OIG evaluated the adequacy of LSC policies and processes, and will recommend additional controls to safeguard against inappropriate or unauthorized access to, use of, or disclosure of personal and private information.

#### Hotline

The OIG maintains a Hotline for reporting illegal or improper activities by LSC grantees or corporate staff. For this reporting period, the OIG received 13 Hotline contacts. Two of these matters were referred to LSC's Office of Compliance and Enforcement for follow-up; the remaining matters were closed.

**INVESTIGATIVE CASES**

Open at beginning of reporting period	8
Opened during reporting period	28
Closed during reporting period	15
Open at end of reporting period	21

**PROSECUTORIAL ACTIVITIES**

Referred for prosecution	0
Accepted for prosecution	0
Declined for prosecution	0

**INVESTIGATIVE ACTIVITIES**

Inspector General subpoenas issued	1
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## LEGAL REVIEWS

### Review of Proposed Legislation, Regulations and Policy

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

During the reporting period, the OIG reviewed proposed legislation of significance to Inspectors General, including S.680, a bill that would enhance the independence of Inspectors General.

Also during the reporting period, the OIG commented to the LSC Board of Directors regarding its possible initiation of a rulemaking providing additional tools to induce grantee compliance, historically termed lesser sanctions. This rulemaking had been among those recommended to the Board by the OIG during the last reporting period.

### Subpoena Enforcement Activities

As previously reported, in March 2007 the U.S. Department of Justice filed on behalf of the United States and the OIG for summary enforcement of an OIG subpoena issued in connection with the OIG's ongoing investigation into the activities of LSC grantee California Rural Legal Assistance (CRLA).

Last year, the OIG issued an interim report on the activities of CRLA, finding substantial evidence that CRLA had violated federal law by soliciting clients, working a fee-generating case, requesting attorneys' fees, and associating CRLA with political activities. The report cited a number of additional serious concerns. The OIG could not complete its investigation due to CRLA's refusal and/or failure to provide the OIG certain requested information required to be produced by federal law and explicit in LSC grant requirements. The OIG issued the subject subpoena in furtherance of its investigation.

### Assisting in Litigation Against LSC

During this reporting period, the OIG worked closely and cooperatively with attorneys from the LSC Office of Legal Affairs and LSC outside counsel who are defending LSC against a legal action brought by an LSC grantee and others challenging the LSC program integrity regulation, 45 CFR Part 1610. LSC management and the OIG were involved in the discovery aspect of the litigation during the reporting period, working cooperatively on giving depositions and responding to a motion to compel production of documents.

**AUDIT REPORTS ISSUED**  
for the Period Ending September 30, 2007

<u>Title</u>	<u>Date Issued</u>
Interim Report on Management Oversight of Grantees – Office of Program Performance	April 5, 2007
FY 2006 LSC Corporate Audit (Conducted by an independent public accounting firm)	June 6, 2007

**AUDIT SERVICE REVIEWS ISSUED**  
for the Period Ending September 30, 2007

<b>Recipient</b>	<b>IPA</b>	<b>Date Issued</b>
Legal Aid of North Carolina	Romeo, Wiggins & Co.	04/10/07
Georgia Legal Services	PJD Group	05/22/07
South Carolina Legal Services	Dixon Hughes PLLC	06/14/07
Blue Ridge Legal Services	Barcalow & Hart	06/14/07
Atlanta Legal Aid Society	Donner, Weiser & Assoc.	09/17/07
Legal Advice & Referral Ctr	Melanson, Heath & Co.	09/17/07
LAF of Metro Chicago	Clifton Gunderson	09/25/07
Lone Star Legal Aid	Mir, Fox & Rodriguez	09/25/07

**TABLE I**  
**Audit Reports Issued with Questioned Costs**  
**for the Period Ending September 30, 2007**

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

## TABLE II

### Audit Reports Issued with Funds to Be Put to Better Use for the Period Ending September 30, 2007

	NUMBER OF REPORTS	DOLLAR VALUE
A. For which no management decision has been made by the commencement of the reporting period.	1	\$5,437,160
B. Reports issued during the reporting period	0	0
Subtotals (A + B)	1	\$5,437,160
LESS:		
C. For which a management decision was made during the reporting period:	1	\$5,437,160
(i) dollar value of recommendations that were agreed to by management	1	\$5,437,160**
(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

**\*\*NOTE:** We closed all open recommendations pertaining to the Audit of LSC's Space Needs. Management has completed specific actions to address the recommendations including benchmarking space needs with other organizations and a bottoms-up review of staffing needs. As indicated in management's comments to the audit report, some excess space has been sublet. In addition, attempts have been made to sublet additional excess space. However, management's analysis of the cost to lease additional space, the projected revenue, and the need for additional space in the near future as LSC's staffing increases indicated it would not be economically feasible to lease additional space at this time.

Because of the above reasons, no additional savings were realized as a result of implementing the recommendations. The OIG considers all recommendations from the Audit of LSC's Space Needs closed.

**TABLE III**  
**Index to Reporting Requirements**  
**of the Inspector General**

IG ACT REFERENCE*	REPORTING REQUIREMENT	PAGE
Section 4(a)(2)	Review of legislation and regulations	11
Section 5(a)(1)	Significant problems, abuses, and deficiencies	None
Section 5(a)(2)	Recommendations with respect to significant problems, abuses, and deficiencies	None
Section 5(a)(3)	Prior significant recommendations on which corrective action has not been completed	None
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	None
Section 5(a)(7)	Summary of each particularly significant report	None
Section 5(a)(8)	Statistical table showing number of audit reports and dollar value of questioned costs	15
Section 5(a)(9)	Statistical table showing number of reports and dollar value of recommendations that funds be put to better use	16
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	None
Section 5(a)(11)	Significant revised management decisions	None
Section 5(a)(12)	Significant management decisions with which the Inspector General disagrees	None

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

## **INSPECTOR GENERAL HOTLINE**

**To report suspected fraud, waste or abuse:**

**Call:** 1 800 678 8868 or  
1 202 295 1670

**Or write:** PO Box 3699  
Washington DC 20027

**You can request that your identity be protected.**

**LSC employees are protected from reprisals by the Corporation.**