

**LEGAL SERVICES
CORPORATION**

Office of
Inspector General



Semiannual Report to the Congress
April 1, 2008 – September 30, 2008

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 April 1 through September 30, 2008.

This report is the first for which I have had the privilege of serving as Inspector General throughout the entire covered period. I have been impressed with the talent and dedication of the OIG staff, and am gratified at the contributions we have been able to make in helping to promote economy and efficiency and to protect against fraud and abuse in the Corporation's operations.

A major focus of our efforts during the period was the priority audits we had initiated to review internal controls at selected grantees. These audits, undertaken at management's request, address issues identified in a recent Government Accountability Office (GAO) report regarding LSC's controls over grant management and oversight. We completed audits at five of the eight grantees referred to us by management. In each of the completed audits, grantee management agreed with our recommendations and took corrective action. The remaining audits will be completed during the next reporting period.

As part of our oversight role with respect to the grantee audit process, during the period the OIG issued three audit service review (ASR) reports. We also conducted field work for one new and one follow-up ASR.

The OIG opened 23 new investigations, and closed 22 investigations during the reporting period. We also completed a comprehensive financial risk assessment project, conducted fraud vulnerability assessments at two grantee locations, and issued a fraud alert to all executive directors to highlight issues and vulnerabilities identified in the investigation of a fraudulent scheme in which both grantee and client funds were stolen by a grantee employee.

This period we initiated a new practice for the OIG, the issuance of Management Information Memoranda (MIMs). We will issue a MIM when we identify an issue in the course of ongoing OIG work that we believe should be brought promptly to management's attention, so that they may consider taking immediate corrective action. During the period we issued MIMs on matters including unallowable dues payments, inaccurate grantee data reporting, a deficiency in the Corporation's automated accounting system, and delinquent travel expense reports. Management was responsive to each of these MIMs.

I would like to express my appreciation to the Board of Directors, LSC management, and to the Congress, for the support and cooperation I have received. I will reiterate the sentiment I expressed shortly after I embarked upon my tenure as LSC's Inspector General: I can think of no better role than one devoted to the dual goals of helping to improve the economy and efficiency of programs serving the legal needs of the poor and of protecting taxpayer dollars from fraud and abuse.

I look forward to continuing to work with all in the LSC community in seeking to improve and protect LSC's programs.

Sincerely,

Jeffrey E. Schanz
Inspector General
October 31, 2008

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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 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, 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 appropriation has 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, consultants, and experts.

To ensure objectivity, the IG Act grants the LSC IG independent authority 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 *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 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 issued final reports on selected internal controls for five of the eight grantees referred to us by LSC management. The remaining three audit reports will be issued next reporting period. Work at these grantees was a primary focus of the OIG's audit efforts this period. These audits are the result of a high priority request and were undertaken in support of the Board's and management's desire to quickly address the issues identified in a report by the Government Accountability Office on LSC's grant management and oversight.

Also during this reporting period, the OIG issued three Audit Service Reviews (ASRs), and conducted field work for one new and one follow-up ASR. In addition, audit staff assisted in one fraud investigation, which is still on-going.

In order to keep the Board of Directors, LSC management, the Congress, and the public fully informed, the OIG is including summary information of its review of the fiscal year 2007 independent public accountant audits required by law of each recipient receiving financial assistance from the Corporation.

Audits Of Selected Internal Controls At Grantees

On November 20, 2007, the President of LSC referred to the OIG instances of internal control weaknesses at eight grantees that were identified in the GAO Draft Report entitled, "Legal Services Corporation - Improved Internal Controls Needed in Grants Management and Oversight," or identified in a November 13, 2007 meeting between GAO and LSC staff. The final GAO report (GAO-08-37) was published on December 28, 2007.

The OIG agreed to review the internal control issues identified in the GAO report to determine whether the conditions cited in the GAO report were corrected and whether controls were put in place to detect similar situations and to prevent them from recurring. In addition, we evaluated other selected financial and administrative areas relating to the GAO findings and tested the related controls.

We began our review during the last reporting period. This period we conducted the remaining field work – visits to all eight grantees have now been completed – and issued five final audit reports. The remaining three reports will be issued during the next reporting period. The OIG will issue an overview report to management summarizing the findings for all eight audits and identifying any policy issues that need to be addressed.

One issue cited in the GAO report was that GAO identified no authority to use LSC grant funds for interest-free or other loans to grantee employees. While we also did not find a specific authority to allow such loans, neither did we find any specific authority to prohibit such loans. Since the GAO report, LSC management issued an advisory memorandum to all Executive Directors as a general reminder of the importance of proper fiscal management. Among the items specifically addressed was the issue of salary advances. The memorandum noted that grantees were not prohibited from providing salary advances to employees, but stressed the importance of having written policies and procedures governing such advances and the need for timely repayments. The memorandum also highlighted issues concerning documentation of expenditures; unallowable costs (in particular, lobbying fees, penalties, and alcohol); and derivative income. (Advisory from the President, Legal Services Corporation to all LSC Executive Directors regarding "Fiscal Management and Use of LSC Funds," March 20, 2008.)

The following sections summarize the five audit reports issued during this reporting period.

Neighborhood Legal Services Program of the District of Columbia

Neighborhood Legal Services Program of the District of Columbia management had taken appropriate actions to address issues raised by GAO dealing with the lack of supporting documentation for payments. Our tests disclosed that disbursements were adequately supported and allowable, and allocations to LSC funds were proper. Also, internal controls over the client intake process; employee benefits and reimbursements; disbursements; and internal management reporting/budgeting were operating in a manner expected to ensure compliance with the LSC Act and regulations.

However, we did note that the grantee's internal controls could be strengthened by documenting adjustments to accounting records; controlling significant dollar value purchases; and reviewing and approving the Executive Director's travel vouchers. We also noted that a written policy on salary advances was necessary. Grantee management agreed with our recommendations and has taken corrective actions.

Philadelphia Legal Assistance Center

Grantee management had taken action to correct issues identified by GAO and implemented internal controls to prevent and detect such issues in the future. Grantee management had drafted a written policy on salary advances and an authorization process requiring employees to sign a statement acknowledging the amount advanced and the monthly repayment amount. Subsequent to our on-site fieldwork, the grantee's Director of Finance provided us with the current policy in place on salary advances. In addition to signed agreements, the policy

now includes a provision requiring repayments by payroll deduction. Based on our review, all of the salary advances outstanding as of December 31, 2007, were supported by signed agreements.

Our review also disclosed that disbursements tested were adequately supported, allowable and properly allocated to LSC. Also, internal controls over the client intake process; employee benefits and reimbursements; disbursements; and internal management reporting/budgeting were operating in a manner expected to ensure compliance with the LSC Act and LSC regulations.

However, we did note that the grantee's internal controls could be strengthened by revising and updating the grantee's accounting manual to incorporate current accounting and fiscal practices; treating adjustments to accounting records as journal entries and having the entries reviewed or approved by a separate grantee employee; and by having an authorized individual review and approve bank account reconciliations. Grantee management agreed with our recommendations and has taken corrective actions.

Wyoming Legal Services, Inc.

Our review disclosed that Wyoming Legal Services, Inc. management had taken action to address issues raised by GAO. GAO identified two instances of internal control weaknesses at the grantee dealing with insufficient documentation and late fees.

As noted in the GAO report, the grantee had a change in management in August 2006, and the current Executive Director was unable to locate many of the records and invoices related to payments made under the previous Executive Director. In addition, the main office of the grantee had moved from Lander, Wyoming to Casper, Wyoming. Since the visit by GAO, the grantee was able to locate the missing documentation. Based on our review, we were able to determine that approved purchase orders and invoices were now maintained in the grantee's Casper office supporting the grantee's disbursements for the period January 1, 2005 through July 31, 2006 (the time period reviewed by GAO). In addition, our review of a sample of disbursements made in 2007 and 2008 found they were sufficiently documented.

Late fees were incurred by the grantee because of a breakdown in controls under the previous Executive Director's administration and because invoices were not routed to the recently relocated main office by vendors and staff. While we did note that the grantee incurred additional late fees after the GAO visit, the grantee has implemented steps to preclude the incurrence of late fees in the future. Notwithstanding the improved internal control, we consider the late fees of \$961 to be questioned costs and these were referred to LSC management for their review and action.

Our review of disbursements disclosed that payments were supported with adequate documentation. However, two payments totaling \$ 3,725 charged to LSC funds for membership dues to the National Legal Aid & Defender Association for the years 2007 and 2008 were not allowable under LSC regulations. We consider the dues payment of \$3,725 to be questioned costs and have referred the matter to LSC management. As a result of this finding, the OIG issued an advisory memorandum to LSC management suggesting that future visits to other grantees by LSC oversight staff determine if this is a systemic problem that management needs to address LSC-wide.

While we did find that internal controls reviewed were operating in a manner expected to ensure compliance with the LSC Act and regulations, we noted that the grantee's internal controls could be strengthened by preparing internal management reports on a monthly basis with sufficient detail to provide oversight and internal control over financial operations; periodically reviewing and updating as needed the percentages used to allocate costs to the various funding sources; conducting periodic physical inventories of fixed assets; and developing and using a strategic plan that formalizes processes for assessing risk and performing periodic internal control evaluations. Grantee management agreed with our recommendations and has taken corrective action.

Laurel Legal Services, Inc. (PA)

The OIG found that grantee management had taken appropriate actions to address an issue raised by GAO dealing with the lack of supporting documentation for contract payments. The grantee entered into an LSC approved subgrant with an organization to make pro bono referrals for qualified clients and to assist the grantee in establishing and operating a reduced fee panel for qualified clients. The subgrantee was to submit monthly detailed written statistical information concerning cases handled. At the time of GAO's review, grantee management indicated that it had only obtained verbal information from the subgrantee on a monthly basis and the required written statistical information on cases annually. Grantee management determined it would require the subgrantee to submit the information on a monthly basis, in accordance with the terms of the subgrant. Our review of detailed reports for the first two months of 2008 confirmed that the grantee is now obtaining the required written information from the subgrantee on a monthly basis.

Disbursements tested were adequately supported, allowable, and properly allocated to LSC. Also, internal controls over the client intake process; employee benefits and reimbursements; disbursements; and internal management reporting/budgeting were operating in a manner expected to ensure compliance with the LSC Act and regulations.

However, we did note three areas where internal controls could be strengthened. First, the grantee should complete a client intake manual. Second, procedures

should be established to control sensitive assets valued under the \$5,000 capitalization threshold. Third, client trust accounts should be reconciled on a monthly basis. Grantee management agreed with our recommendations and has taken corrective actions.

Legal Assistance Foundation of Metropolitan Chicago

Legal Assistance Foundation of Metropolitan Chicago had taken appropriate action to address the issue raised by GAO dealing with insufficient supporting documentation. Grantee disbursements tested were adequately supported, allowable, and properly allocated to LSC with minor exceptions. We noted in several instances that supporting documentation was not contained in the respective vendor file, but the grantee was able to locate the documentation upon request.

In addition, we noted derivative income had been improperly recorded as unrestricted funds. During 2006, the grantee received over \$900,000 in an attorneys' fee award relating to a case in which the grantee had been involved prior to 1996. The receipt of such an award for work undertaken in cases prior to 1996 is not prohibited and therefore was not a violation of LSC regulations. However, we found that the fees received from the award were allocated to the unrestricted funds account rather than allocated to LSC funds as required by regulation. The grantee noted, however, that although the award was not treated pursuant to LSC regulations when received, a dollar amount at least equal in size was ultimately allocated to the LSC funds account for both 2006 and 2007. Because the derivative income was not recorded in accordance with LSC regulations, the OIG referred this matter to LSC management for follow-up and corrective action.

In addition, we found that internal controls over the general client intake process; employee benefits and reimbursements; disbursements; and internal management reporting/budgeting were operating in a manner expected to ensure compliance with the LSC Act and regulations.

However, we identified areas where internal controls could be strengthened. Duties in the accounts payable function should be periodically rotated and a formal written policy governing consultant contracting should be prepared. Grantee management agreed with our recommendations and has taken corrective actions.

Audit Reports

Open at beginning of reporting period	0
Issued during reporting period	5
Closed during reporting period	3
Open at end of reporting period	2

Recommendations to LSC Grantees

Pending at beginning of reporting period	0
Issued during reporting period	16
Closed during reporting period	14
Pending at end of reporting period	2

Recommendations to LSC Management

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

Independent Audits Of Grantees

Since 1996, LSC's annual appropriations acts have required that each person or entity receiving financial assistance from the Legal Services Corporation be subject to an annual audit, to be conducted by an independent public accountant (IPA) in accordance with generally accepted government auditing standards and guidance established by the Office of the Inspector General. 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 and Compliance Supplement, which incorporates some requirements of OMB Circular A-133.

While these audits are not performed by the OIG, the OIG does provide guidance to the IPAs and oversees the IPA process. The OIG reviews all audit reports prepared by the IPAs each year, and performs on-site quality reviews of selected IPAs' documentation.

The OIG also works with management through an audit follow-up process to ensure that adequate action is taken to address all significant findings identified in IPA reports and referred to LSC management. LSC's annual appropriations acts specifically require that LSC follow up on significant findings identified by the IPAs and reported to the Corporation's management by the OIG.

In order to provide more complete information in our Semiannual Reports to Congress, included in this report is 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 in this section and the related schedules reflect the work of the IPAs, not the OIG.

Follow-up Process

Recipient audit reports are submitted to the OIG within 120 days of the close of the recipient's fiscal year end. The OIG reviews the report and any related findings and recommendations. Based on this review, the OIG refers appropriate findings to LSC management for follow-up.

If not included as part of the audit report, LSC management ensures that the recipient submit a corrective action plan for all material findings, recommendations, and questioned costs identified by the IPA and referred to management.

After appropriate corrective action has been taken by the recipient, 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. If LSC management and the OIG cannot agree on closing a finding, the matter is entered into a resolution process for final determination.

Review of Grantees' Annual Audit Reports: IPA Audit Findings

During the reporting period, the OIG reviewed 113 IPA audits of grantees with a fiscal year end of December 31, 2007. These audit reports contained 94 findings. The OIG determined that 18 findings were not significant and closed the findings. Of the remaining findings, 73 were referred to LSC management and three findings were assigned for review within the OIG. Of the 73 findings referred to LSC management, 11 were identified by the OIG as matters of possibly significant concern or interest to LSC management. By highlighting

these findings, management is informed of the issue even though follow-up action with the recipient may not be required.

The tables below present information on the 113 recipient audit reports received this period (recipients with fiscal years ending December 31, 2007).

Summary of Findings Reported in Recipient Financial Statement Audits

Total Number of Findings Referred.....	73
Number of Findings with Corrective Action Accepted by LSC Management.....	36
Number of Findings Awaiting LSC Management Review.....	37

Types of Findings Referred to LSC Management for Follow-up

<u>Category</u>	<u>Number of Findings</u>
Missing documentation	21
Weaknesses in Financial Transactions and Reporting.....	15
OIG Alerts	11
Other	8
Policies and Procedures	6
Timekeeping.....	5
Reporting Issues	4
Physical Asset Inventory	3
Total	73

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 three ASR reports.

INVESTIGATIONS

The OIG opened 23 investigations during this reporting period (compared to 18 the previous reporting period). These included 11 compliance matters, nine criminal investigations, two fraud vulnerability assessments, and one financial risk assessment project. The compliance investigations included allegations of violations of LSC statutes and regulations involving matters such as improperly seeking attorneys' fees and representing ineligible clients. The criminal investigations included allegations of financial fraud and thefts of property from LSC programs. During the reporting period the OIG also closed 22 investigations (compared to 19 the previous period). These included 13 compliance matters, seven criminal investigations, one fraud vulnerability assessment, and one financial risk assessment project. The OIG also issued two Inspector General subpoenas in connection with two ongoing investigations.

Fraud Alert Issued to Executive Directors

During this reporting period, the OIG issued a fraud alert to all grantee Executive Directors to highlight issues related to an investigation where a grantee employee embezzled grant funds and stole monies from clients. This employee bypassed the grantee's regular intake process and, without the grantee's knowledge, provided services to clients needing assistance in obtaining immigration documents from the government. The clients thought they were getting assistance from the grantee in the normal course of business as all the activities were conducted at the grantee's office. The employee would instruct the clients to pay the required government document fees in cash, or by money orders with the payee section left blank, and the employee would then keep the funds. To continue the process of getting the immigration documents for the client, the employee would request a check for the fees under an existing grantee case number, or request a fee waiver from the government. No one at the grantee ever questioned the check requests as all checks issued under this scheme were made payable to the government. This scheme was detected by the grantee when a client contacted the grantee to question the status of the application and the grantee could not find an open case for the client.

The OIG will continue to issue periodic alerts advising Executive Directors about fraudulent schemes and activities in an effort to prevent them from occurring and to help detect them if they do, unfortunately, occur.

Financial Risk and Fraud Vulnerability Assessments

During this reporting period the OIG completed a comprehensive financial risk assessment project that identified program risks for 2008. This project was initiated to identify and proactively address grantee financial risk. It included a survey of all LSC grantees. Based on financial statement reviews, other reviews, hotline complaints, and referrals from LSC and other sources, grantee programs are selected for field visits to conduct individual fraud vulnerability assessments ("FVAs").

This period the OIG conducted two fraud vulnerability assessments. The FVAs consist of a fraud awareness briefing to the Executive Director and Chief Financial Officer; a focused document review in areas identified as weak or prone to abuse; and a review of grantee internal control policies versus practices. These reviews help surface both existing and potential problem areas; improve managers' awareness of their fiscal responsibilities; and serve as a deterrent by making staff aware that funds are subject to review.

Past OIG investigations at grantee sites have involved funds stolen from petty cash, and fraudulent activity involving travel and mileage expenses, credit card accounts, payroll/salary advances, and grantee vendor accounts. Reviews of internal controls for the programs affected by these incidents were found adequate for the size of the operations, yet a breakdown of these controls facilitated the opportunities for embezzlements. In most cases, the employee was a trusted employee and internal control processes were ignored. The OIG found the leading indicators for embezzlement of funds were greed/lifestyle, gambling, revenge, and medical costs. By bringing these factors to the attention of grantee managers, the OIG hopes to assist them in detecting early warnings of potential fraud.

The OIG will report the results on the two FVAs conducted during this period in our next report.

Hotline

The OIG maintains a Hotline for reporting illegal or improper activities by LSC grantees or Corporation staff. For this reporting period, the OIG received 27 Hotline contacts (compared to 29 the previous reporting period). Of these matters, three were referred to LSC's Office of Government Relations and Public Affairs; two were referred to LSC's Office of Compliance and Enforcement for follow-up; six were opened as investigations within the OIG; and the remaining matters were closed.

During this reporting period, the OIG also made several improvements to its Hotline process. The toll-free Hotline number (800-678-8868) now directs callers seeking information about getting legal help to LSC's main telephone number (202-295-1500). Because LSC does not maintain a toll-free call-in number, the OIG had received many requests on its toll-free Hotline number from people looking to find an LSC program in their area. The change will help reduce OIG time spent on such calls and direct callers to a central LSC number so they can obtain this important information. The Hotline also added two additional ways to be contacted: by e-mail and by fax. The new e-mail address is hotline@oig.lsc.gov and the new fax number is 202-337-7155. The OIG will continue working to improve Hotline operations to make contacting us easier and to encourage the reporting of potential fraud, waste, and abuse in LSC programs and operations.

INVESTIGATIVE CASES

Open at beginning of reporting period	20
Opened during reporting period	23
Closed during reporting period	22
Open at end of reporting period	21

PROSECUTORIAL ACTIVITIES

Referred for prosecution	0
Accepted for prosecution	0
Declined for prosecution	0
Indictments	0
Convictions	0

INVESTIGATIVE ACTIVITIES

Inspector General subpoenas issued	2
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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.

This period the OIG reviewed and, where appropriate, provided comments on 10 legislative, regulatory, and policy matters. The more significant items are discussed below.

The OIG reviewed a number of legislative proposals to amend the Inspector General Act of 1978, and coordinated with counsel for the Legislative Committee of the President's Council on Integrity and Efficiency in their continuing work in connection with the long-standing initiatives to amend the IG Act. (These efforts recently came to fruition with the passage of H.R. 928, signed into law on October 14, 2008, just after the close of the current reporting period, as the Inspector General Reform Act of 2008.)

Each year, LSC reviews and revises the standard grant assurances each LSC recipient must agree to as a condition of receiving an LSC grant. During the reporting period, the OIG provided recommended revisions to the grant assurances for the 2009 grant year, with particular emphasis on those assurances affecting the OIG. Management accepted the OIG's recommendations clarifying the requirement that grantees report criminal activity to the OIG as well as the terminology for referral of significant audit findings for resolution.

As reported in our last Semiannual Report, the LSC Board of Directors is considering rulemaking options to provide additional tools to induce grantee compliance, termed lesser or alternative sanctions. This rulemaking is among those previously recommended to the Board by the OIG. During the current reporting period, the OIG continued to monitor consideration of lesser or alternative sanctions by the Board and LSC management. In addition, the OIG participated as an observer and commenter in a rulemaking workshop held by management to solicit opinions from grantees and other interested parties regarding available rulemaking options.

The OIG also reviewed, commented on, and offered revisions to LSC's updated Freedom of Information Act regulations. Under the revised regulations, the OIG will be authorized to receive and act upon Freedom of Information Act requests

directly, without LSC's Office of Legal Affairs being required to receive such requests initially and then refer them to the OIG.

Litigation Activities

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.

Accordingly, in March 2007, the U.S. Department of Justice filed a petition in the United States District Court for the District of Columbia to enforce the OIG's subpoena. Following resolution of a number of procedural issues and submission of briefs later in 2007, on August 26, 2008, the district court heard arguments on the petition. At the request of the district court, the parties subsequently agreed to attempt to resolve their differences through mediation. That process is currently underway.

Other Activities

During this reporting period, the OIG responded to two Freedom of Information Act (FOIA) requests. The OIG legal staff also worked in conjunction with LSC's Office of Legal Affairs to ensure that LSC and the OIG are in compliance with FOIA electronic reading room requirements. OIG counsel provided 11 written legal opinions during the period.

OTHER OIG ACTIVITIES

Management Information Memoranda

This period the OIG initiated a practice of issuing Management Information Memoranda (MIMs). These are designed to bring promptly to management's attention issues that may be uncovered in the course of ongoing OIG work, so that management may consider taking immediate corrective action.

Management Information Memorandum – Dues Payments

As part of the Inspector General's responsibility to keep management informed, a MIM was sent to LSC management to alert them of a situation that was discovered as a result of an audit at a grantee. The grantee had paid for staff membership dues in a nonprofit organization, which were an unallowable cost under the LSC Act and regulations. The purpose of the MIM was to suggest that management have members of its oversight teams look at this issue when visiting other grantees to determine if the problem is systemic and needs to be addressed LSC-wide. Management reported it would raise the issue with Executive Directors at an upcoming conference to emphasize that LSC funds may not be used for such purposes.

Management Information Memorandum – Grantee Data Reporting

A MIM was issued to alert management to apparent data reporting errors involving LSC's Grantee Profile and Grantee Reports (GREPS). The OIG reported data problems with grantees' reporting of staff attorneys' part-time vs. full-time status, as a function of hours worked. Management responded positively to the MIM. The issues identified by the OIG were corrected; management reported the problems were not widespread.

Management Information Memorandum – Automated Accounting Records, Improvement Needed

A MIM was issued to bring to management's attention a deficiency in the Corporation's automated accounting system. In the course of collecting information requested by Congress, the OIG found that the automated system did not contain information needed to correlate travel expenditures to the purpose of a trip. The OIG recommended changes to the system which would improve accountability of funds and provide management with better cost and planning information. Management responded positively and reported it would implement the recommended changes.

Management Information Memorandum – Delinquent Travel Expense Reports

A MIM was issued to alert management to a number of fiscal control issues arising from an inventory of delinquent travel expense reports. The OIG noted that the outstanding reports created expense tracking and other accounting problems. LSC management had initiated some corrective actions; the MIM outlined additional steps for management to consider to help address the problem. Management responded positively to these suggestions.

Congressional Request

On June 30, 2008, the OIG responded to a request from the Ranking Members of the Senate Committees on Finance and Health, Education, Labor, and Pensions, for information regarding LSC's implementation of actions recommended in two recent GAO reports, "Legal Services Corporation – Governance and Accountability Practices Need to be Modernized and Strengthened" (August 2007), and "Legal Services Corporation – Improved Internal Controls Needed in Grants Management and Oversight" (December 2007).

Pursuant to the Senators' request, the OIG specifically reported on: (1) its assessment of the status of LSC's efforts to address the deficiencies identified in the August 2007 report, both as to GAO's recommendations for action by the Board of Directors and by LSC management; (2) questions regarding the amount and purpose of travel by LSC officials; (3) questions regarding the purpose, attendance, costs, and funding source for the January 2008 LSC-sponsored reception on Capitol Hill; (4) questions regarding the purpose and costs of LSC's May 2008 Executive Directors' Conference, as well as certain information regarding past LSC conferences; and (5) information regarding LSC's on-site reviews of grantees during 2008, from January 1st to date of the report.

Ad Hoc Committee

The Board of Directors formed an Ad Hoc Committee to consider and address issues raised in two recent GAO reports, "Legal Services Corporation – Governance and Accountability Practices Need to Be Modernized and Strengthened" (August 2007), and "Legal Services Corporation –Improved Internal Controls Needed in Grants Management and Oversight" (December 2007).

The OIG participated as part of a working group assisting the Ad Hoc Committee in its efforts.

The OIG provided detailed informational briefings to Committee members and senior management concerning the “integrated internal control framework,” as defined by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.¹ The COSO “integrated internal control framework” is among the most widely employed in the United States, used by virtually every audit organization, including GAO, when looking at an organization’s system of internal control. An understanding of this framework was deemed critical to a full understanding of the concerns and context underlying the GAO reports and of how best to address the issues raised in the reports.

Audit Committee

On March 24, 2008, just prior to the start of this reporting period, LSC’s Board of Directors established an Audit Committee and adopted its charter. The Chairman thereafter appointed three directors to serve as its initial members. The formation of such a committee was one of the specific recommendations made by GAO in its report on LSC’s governance and accountability practices. The Committee constitutes a key element in strengthening LSC’s corporate governance regime, and serves as a needed mechanism to address and resolve audit questions and other important issues.

The OIG played a significant advisory role in helping the Board develop a charter for the Audit Committee. In addition to providing comments on the various draft charters, the OIG provided a broad range of information for the Board to consider, which included audit committee charters from government organizations, and commentary and recommendations on the roles and responsibilities of audit committees from a variety of sources, including the American Institute of Certified Public Accountants. The Audit Committee’s charter takes specific cognizance of the statutory authority and role of the Inspector General. The Audit Committee and the OIG complement each other in their respective oversight roles.

Professional Assistance

The OIG responded to a request by the Project on Government Oversight (POGO) to participate in a survey as part of its long-term study of the IG system and how to improve it. We responded to survey questions dealing with issues

¹COSO is comprised of five major U.S. professional financial associations: the American Accounting Association, the American Institute of Certified Public Accountants, Financial Executives International, the Institute of Internal Auditors, and the Institute of Management Accountants (formerly the National Association of Accountants). COSO was formed in 1985 to sponsor the National Commission on Fraudulent Financial Reporting, popularly known as the Treadway Commission, an independent private-sector initiative which studied the factors that can lead to fraudulent financial reporting. It also developed recommendations for public companies and their independent auditors, for the SEC and other regulators, and for educational institutions.

such as IG budgeting and contracting authority, independent IG legal counsel, and cooperation and coordination with agency management. POGO had previously sent a survey to all OIGs, which led to its February 28, 2008 report entitled, "Inspectors General: Many Lack Essential Tools for Independence."

Other surveys or studies the OIG participated in this period included: a GAO survey on the governance practices of designated federal entities; a Postal Service OIG survey of how IGs handle financial statement audits at their respective agencies; and a Federal Audit Executive Council survey on human capital issues affecting the federal audit community.

Statement of Professional Standards

The OIG developed and issued a formal Statement of Professional Standards for OIG employees. The statement articulates the principles and rules of conduct governing OIG employees in carrying out their duties, and reflects the OIG's commitment to ensuring the continued independence, integrity, and reliability of its work. The statement includes detailed provisions with respect to: professionalism; integrity; objectivity; freedom from impairments; confidentiality; reporting responsibilities; compliance; and other matters. The statement is supplemental to the recently adopted Code of Ethics and Conduct, applicable to all LSC personnel.

**AUDIT REPORTS ISSUED
for the Period Ending September 30, 2008**

Report Title	Date Issued	Questioned Costs	Funds Put to Better Use	Unsupported Costs
Reports on Selected Internal Controls:				
Neighborhood Legal Services Program of DC	07/31/08	\$0	\$0	\$0
Laurel Legal Services	08/07/08	\$0	\$0	\$0
Wyoming Legal Services	08/08/08	\$4,686	\$0	\$0
Philadelphia Legal Assistance Center	08/14/08	\$0	\$0	\$0
Legal Assistance Foundation of Metropolitan Chicago	09/30/08	\$0	\$0	\$0

**AUDIT SERVICE REVIEWS ISSUED
for the Period Ending September 30, 2008**

Recipient	IPA	Date Issued
Neighborhood LSP of DC	Walker & Co.	05/06/08
Central Minnesota LS	Harrington, Langer & Assoc.	08/13/08
Iowa Legal Services	Denman Co.	09/11/08

TABLE I

**Audit Reports Issued with Questioned Costs
for the Period Ending September 30, 2008**

	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	1	\$4,686 ²	\$0
Subtotals (A + B)	0	\$0	\$0
LESS:			
C. For which a management decision was made during the reporting period:	1	\$4,686	\$0
(i) dollar value of recommendations that were agreed to by management	1	\$4,686	\$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

² On August 8, 2008 the OIG referred to LSC management questioned costs found in the audit report on Selected Internal Controls – Wyoming Legal Services, Inc. The OIG’s review covered the period 2007-2008. The \$4,686 in questioned costs represents \$3,725 in membership dues and \$961 in late fees. LSC management, by memo dated September 15, 2008, advised that the questioned costs of \$6,801.93 had been recouped from the grantee. LSC management conducted its own review of the recipient’s payment of late fees and impermissible dues for the longer period of 2006-2008. LSC collected the higher amount of \$6,801.93. This issue of questioned costs is resolved.

TABLE II

**Audit Reports Issued with Funds to Be Put to Better Use
for the Period Ending September 30, 2008**

	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
LESS:		
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 III
Index to Reporting Requirements
of the Inspector General

IG ACT REFERENCE*	REPORTING REQUIREMENT	PAGE
Section 4(a)(2)	Review of legislation and regulations	15
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	21
Section 5(a)(7)	Summary of each particularly significant report	4-7
Section 5(a)(8)	Statistical table showing number of audit reports and dollar value of questioned costs	22
Section 5(a)(9)	Statistical table showing number of reports and dollar value of recommendations that funds be put to better use	23
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.



President
Helaine M. Barnett

Board of Directors
Frank B. Strickland
Atlanta, GA
Chairman

Lillian R. BeVier
Charlottesville, VA
Vice Chairman

Jonann C. Chiles
Little Rock, AR

Thomas A. Fuentes
Lake Forest, CA

Herbert S. Garten
Baltimore, MD

David Hall
Boston, MA

Michael D. McKay
Seattle, WA

Thomas R. Meites
Chicago, IL

Bernice Phillips-Jackson
Buffalo, NY

Sarah M. Singleton
Santa Fe, NM

November 25, 2008

The Honorable Edward M. Kennedy, Chairman
Committee on Health, Education, Labor and Pensions
United States Senate
644 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Kennedy:

I am pleased to provide you with a copy of the Semiannual Reports to the Congress of the United States from the Legal Services Corporation (LSC) Board of Directors and Office of Inspector General, for the period April 1, 2008 to October 31, 2008. The Board of Directors' report includes a summary of LSC's major activities during the reporting period.

Sincerely,

Frank B. Strickland
Chairman

Attachment



November 25, 2008

President
Helaine M. Barnett

Board of Directors
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Atlanta, GA
Chairman

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Buffalo, NY

Sarah M. Singleton
Santa Fe, NM

The Honorable Edward M. Kennedy, Chairman
Committee on Health, Education, Labor and Pensions
United States Senate
644 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Kennedy:

The Office of the Inspector General (OIG) of the Legal Services Corporation (LSC) has completed its Semiannual Report for the period April 1, 2008 through September 30, 2008. I am transmitting the Report to Congress as required by law, along with this Management Response containing additional information. The Board concurs with the presentation of statistics in Tables I, II, and III of the report.

Congress entrusts 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 137 programs with 923 offices serving every congressional district in the nation.

LSC is governed by a bipartisan, 11-member Board of Directors appointed by the President of the United States with the advice and consent of the Senate. The Board appoints LSC's President, who serves as the chief executive officer. The Inspector General Act of 1988 established the OIG within LSC. The Inspector General is appointed by the Board and operates under its general supervision.

Our nation promises equal access to justice for all, not just for those who can afford to pay for it. That ideal may never be fully realized, but America can do better—we must if we are to fulfill our nation's promise of equal justice for all.

As we forward this semi-annual report to Congress, our challenges in fulfilling our mission are very large. Nearly 51 million people—including 19.7 million women and 17.6 million children—are eligible for LSC-funded services, according to the recently released 2007 Census data. That represents an increase of 1.18 million people from 2006.

This new poverty snapshot does not reflect this year's economic downturn, suggesting that even more people are eligible for LSC-funded services than have shown up thus far in official counts. There can be no doubt that low-income Americans will be most severely impacted by the downturn. Prices for gasoline, food and utilities are rising; unemployment is up, and foreclosures continue to unsettle communities. Economic erosion affects the poor disproportionately, resulting in increased loss of housing, loss of jobs, and reductions in access to healthcare. Legal aid helps clients who have nowhere else to turn.

Helping fuel the uncertain economy is the rise in foreclosures flowing from the subprime mortgage crisis. An increasing number of low-income Americans are in danger of losing their homes. They may be victims of predatory lenders, especially if they are minorities or elderly. They may be in financial distress because they lost a job, have become disabled, or lost a spouse who contributed to their household income. Often, low-income individuals and families who rent face imminent eviction because they are the last to know that their landlord is in foreclosure.

Many of our programs report a rise in requests for help from low-income Americans facing foreclosure actions. Foreclosure laws vary by state, and our local programs are well-suited to help low-income homeowners, especially with foreclosures that can be traced to predatory lending schemes. With legal assistance, they can renegotiate the terms of their loans or assert truth-in-lending protections in court.

Sadly, the economic downturn and mortgage foreclosure crisis are not the only reasons we expect to see an increased demand for legal services. Natural disasters, such as Hurricanes Ike and Gustav, have devastated parts of Texas, Louisiana and Arkansas and increased the number of people without jobs, income and health care, while putting more poor people at risk of consumer fraud. Wildfires have prompted emergency declarations in California and Texas, and snowstorms led Ohio and Wisconsin to declare emergencies. Five Midwestern states suffered their worst flooding in a century this summer.

Faced with this challenging environment, the Board, LSC management, and the OIG have worked together during this reporting period to continue to improve LSC's economy and efficiency, to modernize Board governance, to clarify the roles and responsibilities for grantee oversight, and to reiterate the importance of compliance with the law and regulations governing our grantees.

LSC provided a May 20, 2008 update and an August 28, 2008 final report to the Government Accountability Office (GAO) documenting the substantial completion of all of the recommendations of two recent reports, *Legal Services Corporation, Governance and Accountability Practices Need to Be Modernized and Strengthened, August 2007*, and *Legal Services Corporation, Improved Internal Controls Needed in Grants Management and Oversight, December 2007*.

Specifically, the newly established Audit Committee of the Board conducted its first three meetings on April 26, 2008, August 1, 2008, and October 31, 2008, and discussed the process used by LSC's Inspector General to select and retain the Corporation's external auditor, examined how the work of the OIG will complement the work of the Audit Committee, heard comments from LSC's Independent Public Accountant regarding the Audit Committee's mission, reviewed and acted on a new protocol for the acceptance and use of private contributions to LSC, and reviewed management's plan for a risk assessment program.

In addition, training sessions were conducted for all officers, employees, and Board members of the Corporation on the Code of Ethics and Conduct that was adopted by the Board in March. At the August meeting of the Board, the charters for the final two committees, the Governance and Performance Review Committee and the Operations and Regulations Committee were adopted.

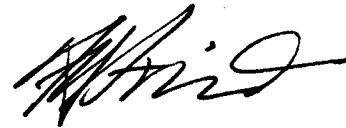
LSC hosted an LSC Executive Directors Conference, in Washington, DC, in June, which was attended by 136 of the 137 LSC-funded programs, all but four of which were represented by the Executive Director. The conference provided a timely opportunity to make a very direct presentation about compliance, the important role that it plays in quality legal services programs, and the individual and collective responsibility all programs have to do their very best to maintain close attention to applicable laws and regulations in all of their work. LSC spoke about the GAO findings and the expectations for heightened compliance awareness in all programs.

The Board and LSC management continue to appreciate the work of the OIG and, in particular, the efforts of Jeffrey E. Schanz, Inspector General of LSC, to improve communication and cooperation during this reporting period. In particular, the introduction of Management Information Memoranda (MIM) has provided timely information to management and provided the opportunity to take appropriate action where necessary.

We fully recognize that it is our ongoing responsibility to ensure that our programs deliver high quality civil legal assistance to eligible clients in the most effective and efficient means possible, in conformity with the mandates of Congress. The annual audit plans of the OIG, the newly-formed Audit Committee of the Board, the independent audit of the finances of the Corporation, the independent public accountant audits of the 137 LSC-funded programs, and the coordinated on-site program visits by the Office of Compliance Enforcement and Office of Program Performance, will combine to verify the effectiveness of the changes. LSC will engage in an ongoing assessment of our oversight processes and will continue to share this information with the appropriate committees of Congress. In addition, we will keep the Congress apprised of our progress on the implementation of our risk assessment program and any other areas that our oversight and appropriations committees would deem appropriate.

If you have any questions or desire any 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 "F. Strickland", written in a cursive style.

Frank B. Strickland
Chairman
Board of Directors