



September 17, 2009

Anna Marie Johnson
Executive Director
Nevada Legal Services, Inc.
530 South 6th Street
Las Vegas, NV 89101

President
Helaine M. Barnett

Board of Directors
Frank B. Strickland
Atlanta, GA
Chairman

Jonah 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. Meltes
Chicago, IL

Laurie Mikva
Evanston, IL

Bernice Phillips-Jackson
Buffalo, NY

Sarah M. Singleton
Santa Fe, NM

RE: Follow-up Review – Recipient No. 829050

Dear Ms. Johnson:

During the period of May 18- 22, 2009, LSC conducted a coordinated review of Nevada Legal Services, Inc. (NLS) by both the Office of Compliance and Enforcement (OCE) and the Office of Program Performance (OPP). This letter provides feedback regarding the areas covered by the OCE portion of that review. As a matter of background, in May 2008, the NLS grant from LSC was terminated, and NLS was placed on month-to-month funding. NLS agreed to a set of detailed Special Grant Conditions (SGC) and further agreed to provide monthly reports to LSC, as directed by LSC. The OCE assessment was a Follow-Up Review (FUR) to specifically assess the program's actions taken pursuant to the SGC and to determine whether the actions taken by NLS were fully compliant, and also whether the actions taken were sufficient to ensure improved compliance and financial systems in multiple areas. This letter discusses the 2008 SGC in particular and incorporates where necessary items from the two sets of SGCs issued in 2009 prior to the May 2009 visit.

NLS complied with SGC-1 regarding the proper allocation of LSC derivative funds. As of the May 2009 visit, this past liability is not yet fully funded. NLS intends to direct the proceeds of fundraising activities to repay the LSC account, and to then spend these LSC monies in full compliance with LSC requirements.

SGC-1 required NLS to credit the LSC account with non-LSC funds in the amount of \$280,746, an amount representing a penalty paid to NLS by the prospective buyer of NLS' building for failure to purchase the building, including earned interest. SGC-1A required NLS to assess what funds are available to repay the LSC account for these amounts.

As required, NLS properly credited the LSC fund with the amount above. To date, NLS has also had insufficient funds to repay these amounts. This is reasonable, as NLS also inherited from prior management other financial liabilities, such as repayment to VARN (discussed, *infra*) of funds belonging to that organization that were misspent. However, the credited amount does raise ongoing concerns with NLS exceeding its annual fund balance allowed limits, and as such NLS is planning certain fundraising activities that will raise unrestricted private donations that can then be used to repay the LSC account. NLS is also aware that as these funds are repaid to the LSC account it is important to then spend the funds on items and activities that are fully LSC-compliant. Also, spending down this past liability is necessary so that NLS does not continue to have an excessive fund balance. Using the standards of 45 CFR Part 1628, and according to 45 CFR § 1628.3(a), (b) and (c). NLS may maintain up to 10% of their LSC support and may retain a fund balance up to a maximum of 25% of their LSC support, with specific LSC approval, in special circumstances. Using the 2008 program audit, the amount of funding that exceeded 10% was \$75,894. Due to the program's efforts in addressing SGC and other corrective action, LSC is not recovering this excess fund balance at this time. LSC is allowing NLS to carry forward its excess fund balance with the understanding the excess fund balance will need to be promptly reduced through fundraising and appropriate LSC expenditures. NLS should take immediate corrective action to reduce this pending excess fund balance so as to remove this pending issue and avoid possible LSC recovery of such amounts in the future.¹

There was a critical observation from the May 2009 review, that was not directly related to any Nevada SGC, but that is related to the proper accounting of the program's annual fund balance. It appears that the NLS auditor has been incorrectly adding the increasing value of the NLS building (bought with LSC funding) to the calculation of the annual fund balance. The value of property, although an asset, is not to be considered part of the fund balance calculation, as this would overstate the actual funds available to the program. NLS should instruct its auditor to cease including the building equity in the fund balance calculation and to report it separately.

The board has complied with multiple SGCs that required targeted board action. Further, current board oversight systems are generally strong. However, additional attention to NLS fiscal reporting and oversight is still necessary.

Interviews with staff and board members, and review of program operations conducted during the May 2009 review, as well as review of extensive documents including board minutes, and numerous SGC Monthly report submissions by NLS in 2008 and 2009, indicate that the NLS board has taken the required actions to satisfy specific board-related special grant conditions. A wider assessment of board activities since the SGC process began evidenced that the NLS board has dedicated substantial time and attention to completely overhauling its role with regard to

¹ NLS is currently on a special six-month grant that ends December 31, 2009. Should NLS receive a regular annualized grant beginning January 1, 2010, LSC will again revisit any remaining excess fund balance that exists at the end of 2009 and make a new decision as to whether an additional waiver will occur, or whether LSC will recover the amounts over 10%.

NLS. There was one pending board conflicts issue at the time of the May 2009 review that was fully resolved immediately following the review, as discussed below.

Improved board governance was a necessary and global pre-condition to the implementation of the various special grant conditions. From January 2008 through to May 2009, the NLS board took numerous effective actions to increase its expertise, oversight and involvement with critical program governance issues. These actions included a number of less active board members choosing to leave the board, and the addition of several new board members who brought new expertise to the board.

Primary among the significant changes to the NLS board was a new board chair appointed in early 2008. Under the leadership of the new chair, the board took extensive steps to study, adopt, implement, and perfect various new oversight and accountability standards for both the board and program's work. Monthly financial reporting is required and reviewed by board members, and detailed budgets are drafted and perfected so as to ensure that NLS spending is fully understood by, and disclosed to, the board of directors. Several board members devoted extensive time to improving various areas of board operations, such as redrafting the operating bylaws. Above all, the new Board Chair dedicated a large amount of time and effort to improving the board's operations, program oversight and compliance, and program service delivery. The Board Chair is commended for his extensive and detailed commitment to NLS and its board, and to the improvement of the program.

A key new board member is both an attorney and CPA. This individual was immediately appointed to serve as chair of the board's fiscal committee. This board member was interviewed at length during the May 2009 review, and board minutes and financial oversight documents were reviewed. This review evidenced that this board member has brought critical financial expertise to the NLS board, and that he works hard to ensure that the NLS board is correctly discharging its critical financial oversight functions. As discussed in the financial management section of this letter, some additional improvements in program fiscal practices are warranted. However, the board's role in ensuring continued positive change is not in question.

LSC's 2008 SGC-2 required that the NLS board receive training regarding the LSC Statute, Appropriations Act, Regulations and other guiding requirements including the restrictions on the use of LSC and non LSC funds applicable to LSC funded recipients such as NLS and those affirmative board actions that are required annually or periodically by the regulations. To address SGC-2, appropriate board training was conducted in 2008,² and board education continues as needed.³

² Board training materials evidenced that necessary oversight and accountability issues were discussed. The program utilized a highly experienced, knowledgeable trainer. The 2008 board training was held over three days, with one day being devoted to assessing program priorities. Two days were devoted to oversight and compliance-related issues and processes. Further, the board has adopted an annual calendar that will assist in the future to ensure timely board action for various regulatory and programmatic review items. In particular there are now

The May 2009 review tested the new knowledge and systems of the board, and reviewed the results of the new board awareness through assessment of its deliberations, committee structures and activities, oversight of program finances, participation in priority setting, and other key tasks. This review indicated that the NLS board is currently operating at a generally high level of appropriate oversight, and that the numerous previously identified issues confronting board governance have been effectively addressed. Further, board minutes evidence that specific requirements for an LSC-funded program board have been met, including a board-directed and adopted program priorities process, final program priorities, and private attorney involvement planning.

The one exception to the above is that the NLS fiscal reporting process, whereby fully accurate reporting is provided to the NLS board in a clear, effective and timely manner is not yet at a level in which LSC can comfortably conclude that the NLS board is being provided all information necessary to discharge its fiduciary responsibilities. Specific observations and problems are noted in this letter, *infra*. As a matter of background, the highest level of disclosure, clarity and oversight is necessary for NLS at this time due to its recent history. Under prior management, confusing or poor quality financial reporting was a significant factor causing the NLS board to be unaware of several significant financial errors or ongoing errant practices. This ultimately resulted in several highly significant financial problems for which the board was unclear and unable to provide timely corrective oversight. These problems included: routine deficit spending that ultimately resulted in a deficit of around \$300,000, misspent LSC and non-LSC funds, substantially inaccurate PAI related financial information, and numerous questionable costs. The questionable costs amounts alone could have crippled NLS due to the sheer volume and amounts of the costs involved.

It is recommended that the NLS board formulate a revised conflicts policy. Further, board members should each complete a written statement of potential conflicts as required by the board policy.

The recently departed vice-chair of the NLS board was an attorney who represents the Nevada Rural Legal Housing Authority which covers many areas of Nevada but mostly affects the program's service area in Carson City. Carson City and Reno NLS attorneys had recently begun to represent clients before this same housing authority and in opposition to the NLS vice-chair. As such, the vice-chair's presence on the board of directors raised serious questions with 45 CFR

regularly scheduled annual reviews of the PAI plan and priorities as required, and there is ongoing board assessment of the program's budget and spending practices.

³ To ensure that the gains obtained continue steadily in the future, it is recommended that the NLS board formalize a training program for new board members, that includes for the next several years, education about the problems confronted prior to 2008, and the corrective action taken in 2008 forward, so as to ensure that the board has continued awareness of critical recent program history.

§ 1607.3 compliance⁴, and raised appearance concerns under 45 CFR § 1607.4(b).⁵ To the program's and board's credit, this conflict situation was disclosed on the first day of the May 2009 visit, along with a clearly expressed intent that the situation be resolved properly under LSC and Nevada rules. Very soon after the visit, the vice-chair decided to resign from the board, thus removing any questions or concerns surrounding this situation.

At LSC's request, in 2008 NLS adopted a written conflict of interest resolution which requires each board member to execute a conflict of interest statement in writing. In light of the above recent conflicts situation involving a board member, LSC recommends that NLS update the board's conflict of interest resolution to include the concepts and language of 45 CFR §§ 1607.3 and 1607.4(b). After this new resolution is adopted, board members should promptly execute an appropriate individual written statement agreeing to the policy and disclosing any potential conflicts.⁶

Most of the 2008 SGCs that required board action on fiscal policy and procedures have been effectively addressed.⁷ However, oversight of the NLS fiscal unit to ensure that policies and practices are followed requires additional attention.

One set of 13 different 2008 SGCs (3-A through 3-M) required multiple and diverse board oversight and action to ensure that past financial issues were resolved. A core part of this set of SGC was to ensure the adoption of better processes and internal controls for the future, and to ensure the proper discharge of the board's fiduciary responsibilities. Program policies, procedures and actual practices were reviewed, and various financial documents, reports and testing were conducted. Each of these SGC is discussed below.

SGC-3A required the NLS board to obtain expertise from an independent consultant or volunteer during 2008 so as to assist it in implementing appropriate ongoing program and board financial oversight systems. The NLS board took appropriate actions to obtain outside expertise both in

⁴ 45 CFR § 1607.3 requires board members to not have "significant individual institutional conflicts of interest with the recipient or the recipient's client community that could reasonably be expected to influence their ability to exercise independent judgment as members of the recipient's governing body. ..."

⁵ 45 CFR § 1607.4(b) prohibits "the governing body or any member thereof" from interfering with "any attorney's professional responsibilities to a client or obligations as a member of the profession or interfere with the conduct of any ongoing representation."

⁶ Although the current board policy, created at the request of LSC, did ask for board members to execute individual statements under the policy, these statements were not created. However, board records and interviews indicate that board members did discuss potential conflicts to ensure that no issues were created by their service on the board. LSC recommends that these individual statements now wait until the current policy is enhanced as described in this letter, and that the board leadership then obtain statements from each board member, the first statement to be obtained promptly, with subsequent statements requested as needed (should an individual's situation change) and/or on some periodic basis.

⁷ The 2008 SGC focused on significant fiscal corrective actions through the board. LSC made this emphasis on board action and responsibility due to LSC's concerns about the quality and reliability of information being produced and upon which the board relied.

the short and long terms. A volunteer consultant was used in the summer of 2008. Further, and most importantly, a CPA was added to the NLS board and continues to serve to this day. SGC-3A has been fully addressed.

SGC-3B required the NLS board to review the staffing of the NLS financial operation to determine whether there is appropriate and sufficient staff capacity to ensure the proper handling of financial matters, and then the board was required to act on its findings to ensure proper staffing for the future. The NLS board conducted the necessary review and determined to hire a new fiscal manager. In addition, other staff and assignment changes occurred within the NLS fiscal unit such that at the present time all staff working in the unit is new to that unit. However, even though this SGC can be considered fully addressed in terms of the 2008 assessment required by LSC, there appears to be a new issue of proper supervision and accountability for the fiscal unit. This is discussed most critically in the section on cash disbursements, but it also involves certain other areas discussed in this letter in which concerns are noted.

SGC-3C required the NLS board to review the financial oversight systems used by NLS staff to determine what overall improvements are needed and to then adopt a new financial oversight system that would specifically correct several specific listed weaknesses. The new oversight system was required to have: timely identification and correction of costs that are mistakenly charged to incorrect accounts; a system to monitor and prevent significant cost overruns in budgeted line items; and methods to ensure that LSC funds are fully protected and not expended directly or indirectly on any activity prohibited by LSC or designated by NLS as non-LSC funded. Further, SGC-3D required the NLS board to ensure that NLS cease paying any disbursements lacking adequate supporting documentation, and to revise the cash disbursements policy and practices as needed to ensure proper internal controls. As part of this corrective action, several items were listed as necessary for cash disbursements, including that: the payment is attributed to a specific budget line; there is current funding available, within the budget, to make such payment; there is adequate supporting documentation that clearly evidences the expense as reasonable and necessary with a legitimate business purpose; the expenditure does not involve any conflict of interest; and where required, an appropriate competitive bidding process has been followed.

The review of the SGC monthly submissions of 2008, and those of 2009, along with a review of board minutes and of the fiscal systems in place during the May 2009 visit evidenced that the board undertook the extensive corrective action required by SGC-3C and SGC 3-D.

The program's current cash disbursements process *as designed* is adequate to ensure that program and LSC funds are protected and that payments made are supported by adequate documentation. However, as discussed below, the process has not always been followed, which is a significant problem.

During the May 2009 visit, there was one very troubling observation regarding cash disbursements. Staff had submitted several travel expense reports that did not comport with the program's new policy. More critically however, these were paid by the NLS fiscal unit despite

the fact that they did not follow the program's new policy. In some instances, the requests did not include all necessary supporting documentation. For example, one expense report clearly disclosed when and where a trip was taken, but there was no explanation as to the purpose of the trip or its relation to LSC eligible work. Also, the program's policy includes a summary form requirement – however some reviewed expense reports did not contain this documentation. The fiscal manager explained that he was aware of the purpose of the staff's travel and its business purposes and so he allowed the requests to be paid. This is an insufficient rationale and raises very serious concerns regarding whether NLS fiscal unit staff understand the seriousness with which LSC funds must be safeguarded and expended in light of the recent-year financial issues confronted by NLS. All SGCs and corrective actions implemented by NLS that involve the adoption of standard and new financial controls must be followed without exception. Also, as the above exceptions were identified by outside reviewers (LSC team members), it is uncertain how long it would have continued and raises questions and concerns regarding when or if it would have been identified by the NLS board or other NLS staff or management.⁸

NLS was required to improve its reimbursement systems due to numerous unjustified costs and other questionable expenditures by prior management. The new procedures have met the approval of LSC as they included sufficient internal controls. It is partially because NLS designed, adopted and then agreed to follow the new fiscal policies that LSC decided to increase NLS's funding from month-to-month to longer grant terms. If the new fiscal policies and procedures are not uniformly followed (especially for cash disbursements) then LSC funds continue to be at risk, raising new compliance issues. This lack of enforcement by the NLS fiscal unit of the cash disbursements and travel request policies is serious. Should there be any continued failure to follow board-adopted fiscal policies such as for cash disbursements, this will be the basis for questioned costs. NLS management and the fiscal unit management was informed that in the future *any* request for reimbursement of any kind that does not fully follow the NLS policy should be rejected for payment by the NLS fiscal unit, and returned to the individual for correction, without exception. As discussed below, this observation also raises issues with SGC-3L compliance regarding board oversight of financial policy enforcement.

Finally, there was also one fund coding error noted that affects compliance with SGC-3D. NLS uses a funding code "99" that is a shared cost pool used by NLS for allocation of certain costs that it plans to allocate across several grant sources, including LSC. However, code "99" was found to have been used for a few items for which LSC funds could not be expended. This was discussed with the fiscal unit staff who agreed to make the necessary changes for those items.

⁸ It is noted that NLS took immediate action to correct this finding and an email was sent to staff during the review stating that future expense reports would need to follow the policy and have adequate and proper backup documentation. However, this email alone does not resolve this finding – NLS should examine how to build more effective oversight of the fiscal unit so as to ensure that policies are followed without exception. As part of this, it is recommended that the NLS board and executive director assess how the three members of the fiscal unit could be used to provide enhanced cross-checking of each other's work. Management should also ensure that NLS staff members understand their responsibility to identify and disclose any instances in which NLS fiscal policies are not followed.

However, as a result of this, special attention to the use of “99” should be given during the oversight of the program’s financial practices by the executive director and the board.

SGC-3E required that the NLS board and management initiate a disciplined annual budgeting process whereby NLS ceases any deficit spending. As part of this, the NLS board was required to review a monthly variance report that contrasts actual expenditures with the budget line items. Monthly reporting in 2008 evidenced that NLS, under the direction of its board, began to conduct monthly reviews of finances so as to comply with this SGC. Further, the monthly variance reports themselves underwent significant revision, with the assistance of LSC, during 2008 so as to ensure that these reports included all necessary information in a fully disclosing and understandable format. While it can be concluded that NLS has adopted proper basic budgeting, and that the program has brought current expenditures within available resources, there remain various errors in monthly reporting, budget updates, and other fiscal reports that raise serious concerns about how these documents are being produced and reviewed. For a recent example, the NLS Variance Report dated June 30, 2009 (provided to LSC by email dated July 29, 2009), shows “0” in all of following categories related to Vacation Accrual: Current Period Actual; Current Period Budget; Current Budget Variance; YTD Actual; YTD Budget; and YTD Budget Variance. This is a significant omission, as it is not possible for NLS to have no amounts in any of these categories, as the program provides vacation leave for its employees as a standard benefit. No explanation of this was provided as a note or otherwise in or with the variance report.

An explanation regarding this omission was requested from NLS via email, and a response was provided by the NLS fiscal unit dated August 20, 2009. The response explained that the absence of information was intentional. It was further stated that these monthly variances would “...vary wildly from month to month” and stated that the program wished to continue with its current plan of waiting until year-end to reconcile leave accrual. In order to cover potential liabilities the program set aside a lump-sum annual liability of approximately \$70,000 that it anticipates would cover all possible liabilities. NLS also supported its decision by stating that it has been a “standard practice” of NLS – however this was strongly contradicted by prior information provided and earlier variance reports sent to LSC.⁹ Nevertheless, LSC requests that NLS include vacation/leave figures in its future monthly budget variance reports.

⁹ The August 20, 2009 explanation stated: “this method has been the standard practice at NLS...” This statement is very troubling for several reasons. First, LSC found no evidence that monthly variance reporting occurred under prior NLS management, which is why accurate variance reporting was made a specific SGC. Second, the February 28, 2009 variance report provided by the program had figures in the vacation accrual line items for each of the following: “Current Period Budget”, “Current Budget Variance”, “YTD Budget”, and “YTD Budget Variance”, and also stated that Vacation Accrual “will be adjusted quarterly”. This is directly inconsistent with claiming in August 2009 that there is a standard practice to wait until year-end. Third, the fiscal management of the program prior to 2008 resulted in the program losing its LSC grant in mid-2008, created a significant deficit for the program, and resulted in numerous potential questionable costs for the program. With its continued funding, LSC requested that NLS fiscal policy and practice be designed anew. There should be no reliance on any practice inherited from the period prior to 2008. As discussed elsewhere in this report, this also raises questions about the program staff’s understanding of the seriousness of the new discipline needed.

As a matter of background, during 2008 and 2009 LSC requested monthly budget variance reports for several reasons, primary among them to ensure that the program was able to bring expenses in line with revenue and cease all deficit spending. These reports were also reviewed as part of LSC's determination as to whether an average board member was being provided sufficient and clear information so as to understand program budgeting, spending and the overall financial outlook. Under previous management, one significant contributing factor to the program's inability to control spending was the insufficient financial reporting provided to the board. As such, LSC has expected best practices to be used at all times for financial and budget variance reporting.

However, the budget variance reports themselves became a separate issue for LSC over time, as the reports presented to LSC continuously needed specific follow-up in order to be fully understood, or lacked necessary information. In addition to the above example of the lack of vacation detail in the most recent report, another example includes the February 2009 budget variance report. In the February 2009 budget variance report, there were 17 items with variances over 5% for which no explanation was provided to explain the variance. Budget variance reports should contain notations explaining significant variations in line items so as to flag particular issues and provide needed detail. The variances noted on the February 2009 report that lacked any explanation ranged from a -356% to a + 66% difference. In response to the February report, LSC then found it necessary to specifically add a written requirement, in the next set of SGCs that NLS "is required to provide a detailed narrative explanation for any budget line item variance of more than five (5) percent." See March and April 2009 SGC.

The ongoing inability by NLS to produce fully inclusive and descriptive budget variance report and other financial reports raises continued concerns for LSC.

It is unclear whether the NLS fiscal unit is utilizing standardized templates for all of the various key monthly reports. The presentation of data in monthly reports has changed at times from one report to the next. These changes could be based on affirmative decisions to change the format. However, there have been other observations, such as a line item that failed to have a descriptive identity, that reports might be typed anew each month or otherwise generated without a set template. With this letter, LSC will be requesting the templates used for various key fiscal reports. See section titled "Future Actions", *infra*.

The NLS board and management must take further actions to ensure that NLS fiscal practices follow the policies as adopted, and that the NLS board receives all financial reporting necessary for it to fully conduct its oversight of program finances and operations. As this was part of the 2008 SGC process and is not yet fully implemented, this area is pending. However, from the issues noted above and discussed elsewhere in this letter, LSC has *new concerns* regarding NLS fiscal practices and oversight systems. The NLS board should again review the operation of the fiscal unit and all related oversight systems, including the board's role, so as to ensure that at all times NLS policies are fully followed. As part of this review, NLS should adopt additional

systems and oversight processes as necessary to provide additional cross-checking to ensure proper safeguarding of LSC funds. These new oversight and cross-check systems should ensure that the NLS board is quickly able to determine future instances in which any fiscal unit staff fails to follow board-established policy. There should be no future instances of patterns in which staff fails to fully follow proper internal controls and board-adopted policies. Additional board or volunteer non-board members dedicated to the fiscal committee might be considered, if necessary.

SGC-3F required the NLS board to adopt a quarterly cost allocation assessment as part of the program's overall yearly budgeting process. As part of this assessment, LSC required that the NLS board conduct its own independent determination that LSC funds have not been used for activities designated as non-LSC or otherwise for activities prohibited by LSC. Throughout 2008 and into 2009, the NLS board, through its board chair, and subsequently through its board fiscal committee did conduct active reviews of actual expenditures of LSC funds, as required. Moving forward, the special actions of SGC-3F should be able to be successfully executed through the board's ongoing monthly assessment of budget variance reports.

SGC-3G required the NLS board to ensure that LSC funds are used solely for activities and costs that qualify as eligible for LSC funds and to adopt a related policy to prohibit the program from using any restricted funds, directly or indirectly, for activities prohibited by those funds, and prohibiting the use of restricted funding as "loans" for other activities. Under the prior management, NLS had inadequate internal controls and financial recordkeeping to ensure that restricted funds, such as LSC funds, did not get spent on inappropriate or non-compliant activities. Further, the program had inappropriately used restricted funds as loans to other accounts that were overspent. This item received extensive LSC attention during the SGC monthly reporting process, and was the subject of ongoing telephone update and technical assistance calls held between current NLS management/board members and LSC staff. Further, during the May 2009 onsite review, LSC staff reviewed the policies adopted, the oversight conducted by the board, and the current allocation methodologies and practices of NLS. The above review indicates that substantial corrective action was taken. However, until NLS has fully satisfied LSC's requirement to have a clearly applied direct and indirect cost allocation process that is correctly applied in practice to all significant cost centers, a final assessment as to whether this SGC has been fully addressed is pending. This allocation issue is discussed further, *infra*.

Closely related to SGC-3G above, SGC-3H required the NLS board to conduct all necessary oversight to ensure that NLS fiscal practices and internal controls are extensively improved so as to ensure the proper segregation of restricted and unrestricted funds. SGC-3H required that NLS ensure that LSC funds not be used directly or indirectly to support any activities restricted by LSC. Under prior management, as discussed above, LSC funds and other funds were not clearly maintained in the financial records so as to ensure that LSC funds were spent only on LSC-eligible activities. As with SGC-3H, this item received extensive LSC attention, and technical assistance, and was actively addressed by the NLS board during 2008. Again, the actions taken

by the NLS board did establish sufficient new controls and systems to protect LSC funds. NLS took substantial corrective action to address SGC-3H. LSC considers SGC-3H to have been adequately addressed.

Also closely related to SGC-3G and 3H discussed above, SGC-3I required that until better financial recordkeeping was adopted, that the NLS board should ensure that the program would not undertake any activities prohibited by LSC funds, with limited exceptions. SGC-3I also required that until 3-H is fully implemented, that NLS will not enter into any consultant contracts, unless every activity of the consultant is fully permissible under LSC funding restrictions. The NLS board took the necessary steps under SGC-3G to direct program activities to ensure that all such activities in the short-term were LSC compliant. After the adoption of better financial systems, the program appropriately relaxed these requirements so as to handle different eligibility requirements for different grants. Importantly, clear steps were taken to ensure that LSC funds are dedicated to LSC eligible activities.

To comply with SGC-3I, problems identified with prior consulting and contract agreements were handled by NLS in 2008 by placing stricter controls on the activities of the contractor. The controls served to ensure that all LSC-funded activities were LSC-compliant. Under prior NLS management, the activities of this consultant had presented certain identified issues and non-compliance with Part 1612. Under the new executive director, NLS immediately took all necessary corrective action, changing the requirements by which this consultant could operate for the remainder of this 2008 contract. NLS required that the activities allowed by and paid by NLS were clearly defined to exclude any activities that could raise questions or issues. Further, more detailed reporting by this consultant was required so as to provide assurance to NLS and LSC that the activities conducted on behalf of NLS were fully permissible. As of January 2009, the NLS board and management decided to not continue this contractual relationship.

Regarding 45 CFR Part 1612 in general (that prohibits lobbying and demonstrating except under certain circumstances), the current relevant NLS policies and procedures are consistent with this regulation. Interviews with staff indicate that no lobbying is taking place at the present time. It was noted that some Part 1612 activity has taken place in the past, at the specific request of governmental officials, and as allowed. NLS staff members interviewed evidenced precise clarity regarding LSC lobbying and other Part 1612 restrictions.

SGC 3-J required that the NLS board adopt a program policy to provide immediate LSC notification in the event that any budget deficit is projected or possible in the LSC account, and to otherwise follow the requirements of 45 CFR Part 1628. Under prior program management, NLS was running budget deficits that were not clearly disclosed within fiscal records, and that had not been clearly disclosed to the NLS board or to LSC. The NLS board took full actions to satisfy the elements of SGC 3-J through extensive improvement of financial policies and practices, including adoption of a policy that would comply with the requirements of Part 1628 should a relevant deficit occur in the future.

Under prior program management, NLS was providing salary advances to certain staff without proper internal controls, and without board awareness. SGC 3-K required the NLS board to amend the program's policy on salary advances and to take steps to ensure that NLS follows the revised policy. The board took effective action to change the program's policy, and through its review of fiscal records took steps to ensure that any salary advances were properly tracked and repaid according to the program's policy. Further, the new NLS executive director took steps to ensure that salary advances occurred only as needed. NLS has fully complied with SGC 3-K.

SGC-3L, LSC required the NLS board to ensure that the program completed a revision and adoption of a new Accounting Manual. Further, this SGC required that sufficient policies and procedures have been adopted to address the multiple financial oversight corrective action items that were part of the 2008 SGC. NLS adopted a new Accounting Manual through an interactive process that included ongoing LSC input for several policies and proper internal control standards. The current Accounting Manual is an appropriate document which NLS should now continuously update and revise as needed, to ensure that it stays current with changing practices, and various grant requirements.

A second part of SGC-3L required the NLS board to adopt and implement an effective monitoring and oversight system for financial activities. The monitoring system was required so as to ensure that NLS (both the board and staff) follow all adopted program policies. While there was substantial evidence of board oversight regarding program finances and adoption and implementation of new program policies, as specified in the second part of SGC-3L, the above discussed finding of SGC-3D involving the failure to follow the program's cash disbursement policies does raise current and future concerns about how the fiscal unit will be properly supervised. LSC requests the NLS board to review this and determine how the fiscal unit staff, program managers, and the board can be used to create some additional oversight for the fiscal unit so as to ensure that core fiscal policies are followed.

The review concluded that the NLS board has taken effective action to address SGC 3-M that required the creation of a yearly calendar system establishing due dates for annual review and approval of all critical board oversight actions. Having this information in a clear yearly plan should serve the NLS board in the future with various LSC and other grant requirements.

The NLS board and the new executive director conducted the necessary assessments, and directed needed changes, regarding certain program activities that did not involve the provision of legal services to eligible clients. As part of this, NLS has taken effective corrective action to ensure that legal advice is appropriately supervised and provided by designated professionals.

A group of related SGC involved prior NLS staffing for non-legal service activities. A series of four separate SGCs found under SGC-4 requested that the NLS board review two particular current arrangements: one involving the staffing of a county sponsored self-help clinic, and the

second involving an NLS unit that was dedicated solely to self-help services. In general, SGC-4 required that the NLS board conduct an assessment of all program activities in which no direct legal services are provided. This requirement arose from several concerns identified by LSC regarding self-help and other services provided to unscreened persons.

SGC-4A required an extensive assessment of the NLS relationship with another entity (Clark County Family Law Self Help Center (CCFLSHC), for which NLS provides approximately four staff. After an NLS board assessment, and then a closer LSC review of this arrangement under the program integrity requirements of 45 CFR Part 1610, LSC concluded that there was no prohibition regarding this arrangement as long as non-LSC funds were used. NLS committed to use non-LSC funds for the CCFLSHC arrangement and through its budgeting process, established a reasonable cost assessment for these staff and sources of non-LSC funding for the project. These actions brought NLS into substantial compliance with SGC-4A.

Related to the above, SGC-4B required the NLS board to ensure that as of January 1, 2008 and in the future, that no LSC funds are used for any cost, direct or indirect, incurred for any staff provided to CCFLSHC. Review of financial records, budgeting data, and costs related to CCFLSHC indicated that NLS took effective corrective action thus far to address this SGC. NLS should periodically review the CCFLSHC budget to ensure that it includes all appropriate related costs, such as leave accrual and other benefits for the CCFLSHC assigned staff, as well as all appropriate indirect costs.¹⁰

Two other SGCs related to a second prior NLS effort, the Self-Help Housing Center (SHHC) unit that was located in the Las Vegas office. Under SGC-4C, the NLS board was required to assess whether the structure, purpose and work of this unit represent an efficient and effective use of LSC funds. Under SGC-4D, the NLS board was required to ensure that management oversight of the SHHC was improved so as to ensure that non-attorneys cease providing legal advice, except as permitted in Nevada under the direct supervision of an attorney, and only for properly screened eligible clients.

The May 2009 review assessed the current NLS delivery of legal services via telephone and paralegal delivery, and verified changes made to staff and service structure that were of concern to LSC. In particular, 2008 SGC 4-D required NLS to ensure that non-attorneys cease providing legal services except as permitted in Nevada under the direct supervision of an attorney. Further this SGC required that no legal advice be provided unless the applicant is fully screened and established as LSC-eligible and accepted as a client.

Review of program priorities, board minutes, monthly SGC Reports, and interviews conducted during the May 2009 review evidenced clearly that the NLS board conducted a full and appropriate review required by SGC-4 and that the NLS board and program management took all necessary steps to ensure that services are provided to LSC-eligible persons, that legal advice is

¹⁰ At the time of the May 2009 review the CCFLSHC budget was being revised as that grant cycle begins in mid-year and was soon up for renewal. The review team shared this finding with the NLS fiscal staff during the review.

appropriately supervised, and that legal advice is not provided unless a client is eligible and a case accepted (for at least brief service).

During the May 2009 review, the Tenants Rights Center (TRC), a new NLS initiative that replaced the SHHC, was reviewed in depth. Two of the three current intake/paralegal staff had worked previously in the SHHC and had been part of the entire transition from the unscreened to screened services. Staff explained that in immediate reaction to the January 2008 LSC visit NLS began immediately to conduct screening for SHHC applicants. Next, in the Fall 2008 the unit name was changed and legal services began to be provided in appropriate and eligible cases. It is noted that both legal information and legal advice can be provided by the TRC, but both are provided only to screened individuals. Ineligible applicants are directed towards web sources, general legal information materials and/or provided a referral. Importantly, in 2008 the TRC came under the management of a different supervising attorney (who was already leading the senior hotline efforts). Review of documents, cases and interviews evidenced that this supervising attorney's active role in managing the TRC has fully corrected the previously noted problems. In addition to ongoing availability and individual case oversight and review, the supervising attorney holds regular weekly joint meetings of the TRC and Senior Hotline staff to identify trends, answer questions and discuss areas of change or improvement. The review indicated that this attorney's oversight is effective, active, and useful to staff. Further, the review indicated that the TRC staff are effectively conducting client screening to ensure that clients accepted comply with the necessary NLS and LSC standards and policies.¹¹

During the May 2009 onsite LSC review, the large waiting room sign for the SHHC was still posted above the now TRC service window. As the SHHC is defunct, NLS should promptly remove this old signage.

Finally, it is noted that certain other appropriate services also occur under other NLS funding. For example, the paralegal in the Carson City office is IRS certified to provide tax service to IRS-eligible clients (those making \$45,000.00 or less). The services focus on helping qualifying taxpayers to obtain tax credits. Further, the paralegal is also IRS certified to train other NLS personnel to provide this service. For example, the office manager in Reno, who is neither an attorney nor a paralegal, is IRS certified to handle these cases. All these cases are reflected in NLS's case lists under code 23 and 24.

¹¹ One observation is noted for future consideration by NLS. There is reliance on paper forms in several circumstances by TRC staff when conducting intake. After the client has left (in-person), or the telephone call is completed, the information will then be entered into the computer. At a future point, NLS should consider the efficiencies of having staff directly use the automated intake form in the computer for live intakes (in-person or by telephone) in which a computer is available.

NLS has made measurable gains in the involvement of private attorneys in the delivery of legal services. NLS developed PAI plans for 2008 and 2009, albeit adopted late, and continues to expand the types of activities and outreach efforts to private attorneys.

A related set of nine SGCs addressed the program's compliance with 45 CFR Part 1614 involving Private Attorney Involvement (PAI). Under prior management, NLS had very little valid PAI activity, and the accounting for the negligible PAI activity conducted was inaccurately conducted. Further, substantial allocations previously made to PAI had no PAI elements and did not qualify for such allocation. NLS essentially needed to create a new PAI plan to include appropriate activities to involve private attorneys, and proper accounting for all such activities. As discussed below, multiple corrective actions relating to PAI were made by NLS as required by 2008 SGCs, and the program continues to make ongoing additions and improvements to its range and level of activity.¹²

SGC-5A required that NLS create a PAI plan following 45 CFR Part 1614 regarding the creation of an annual PAI plan. As was to be expected, the development of a truly effective plan occurred in stages, as NLS identified new and creative methods for the involvement of private attorneys, and tested these new programs to determine their effectiveness. Under prior management, NLS did not have a compliant or reasonable PAI plan for several years. Under the new Executive director who began in early 2008, NLS needed to develop a completely new PAI plan and group of activities to address the requirements of 45 CFR Part 1614. A 2008 PAI plan was developed, revised, and formally approved by the NLS board at its October 11, 2008 board meeting. Directly related to SGC-5A, SGC-5B required that commencing with 2009 that NLS shall ensure that a fully compliant PAI plan is annually developed and adopted, with a corresponding and appropriate budget approved by the NLS board, prior to January 1st of the year in which the plan is to be implemented.

For 2009, NLS drafted a PAI plan that was approved by the NLS board of directors on March 25, 2009. The timing of this 2009 plan did not comply with the time requirements of SGC-5B. However, LSC finds that the timing of these plans, occurring during the year in which they are effective, is excusable due to the significant work that was required by NLS to design a PAI plan from the start. 45 CFR §1614.4 also requires that programs consult with significant segments of the client community, private attorneys, and bar associations, including minority and women's bar associations in the recipient service area as part of the development of the PAI plan. Despite

¹² As of the May 2009 review, NLS appeared to be at the beginning of an entirely new and very positive level of activity and effectiveness for PAI, in part due to each of the following: several creative and new opportunities identified by the executive director and staff; the commitment of the NLS board to PAI; concerted outreach to community legal and other providers and partners; and the hiring of a full-time PAI coordinator who began by June 2009. As this area was experiencing frequent positive change at the time of the May 2009 review, it was subsequently updated after the visit. This letter contains updated PAI information that includes activities through July 2009. The rate of increase in activity is impressive. LSC also recognizes that additional time is needed, and that the success and breadth of PAI will continue to change. NLS is not expected at this time to have fully completed the design and implementation of its ultimate PAI plan that will ensure full compliance with the expenditure percentage.

being developed and adopted out of a normal cycle for PAI plans, the program still conducted activities to involve the bar and the client community in the plan under Part 1614 albeit during the year in which the plan should already be operative. NLS management has indicated that beginning with the 2010 PAI plan that NLS will conduct the necessary consultations under the regulation in advance of the operative PAI year, and that the plan will be adopted before, and operative on January 1, 2010.

NLS's PAI plan includes one significant carryover activity (a reduced fee panel in Washoe County) but otherwise most PAI activities of 2008 and 2009 involve newly created projects. New activities include involvement of private attorneys in the newly created Tenants' Rights Center, the Senior Help Line, Low Income Tax Clinic, and in the Mortgage Foreclosure Program.

As of mid-2009, PAI activities have continued to increase and to expand the diversity of private attorneys who can assist in the delivery of legal services to the eligible community. Activities related to PAI include several new initiatives already underway or in the final planning stages, including:

- The addition of a full-time PAI coordinator for the entire program, who recently joined the program. This individual already has been working to increase NLS's outreach, and has been working on development of new relationships and coordination, including production of pro bono publicity and marketing materials that NLS will use at CLEs and other planned events.
- Conducting CLE trainings for attorneys on the new mortgage foreclosure and mandatory mediation programs with a related pitch to join the pro bono program. So far in 2009, 63 new attorneys have signed up to be NLS pro bono attorneys under this program.
- Increased outreach to the Clark County Bar Association to obtain volunteer attorneys in Clark County. In Clark County several attorneys are now volunteering, providing representation on various case types including mobile home park eviction and guardianship. Another new pro bono attorney has volunteered to serve as the Qualified Tax Expert for the NLS Low Income Tax Clinic. Further, the Tenant's Rights Center in Las Vegas now has four volunteer attorneys who assist with the provision of brief legal advice by telephone or in person to persons in Las Vegas.
- Working with Washoe Legal Services to enhance cooperation between NLS and WLS pro bono efforts. Under this new collaboration, two pro se clinics have been held thus far in 2009 in Elko. Courts refer potential clients and pro bono attorneys volunteer to present the clinics and provide assistance to clients.
- Work with a new three-county bar association that has recently formed between the Nye, Esmeralda, and Mineral Counties. Conversations have already occurred as to how this new bar association can conduct pro bono assistance to clients with the assistance of NLS. NLS has also agreed to do three CLE trainings in Pahrump over the next year – one on Elder Law issues, one on consumer law/predatory lending, and one on mortgage foreclosure. NLS will use such CLE trainings to increase the number of private attorneys willing to volunteer with the program.

- Planning a Champions of Justice Luncheon for October 2009 as part of a “Celebrate Pro Bono Week” in Nevada.
- Outreach with a PAI attorney to a Nellis Air Force Base Department of Defense event, in which clients were screened, accepted and provided legal assistance.
- Obtaining 11 pro bono attorneys to participate in a HUD sponsored mortgage foreclosure event held over two days, in which screened and accepted clients obtained legal counsel by the volunteer attorneys. In addition to the advice cases, NLS accepted 25 cases for extended representation, with some pro bono attorneys indicating that they would assist in some of these cases at the new mandatory mediation required in Nevada.
- The Judicare Panel in Reno has begun taking new cases, with three attorneys accepting new family law cases in the past two months.

An important positive PAI development is that NLS has reestablished their relationship with Volunteer Attorneys for Rural Nevadans (VARN). VARN is an organization that previously had an ongoing and close collaboration with NLS. However, under prior program management, there was a severing of this relationship with a financial dispute involving monies owed by NLS to VARN.¹³ Under the new Executive director, and after extensive work, the relationship with VARN was mended and reestablished. This has positively affected the PAI area, as NLS is supporting a full time pro bono coordinator housed at VARN offices, who will accept LSC-eligible pro bono cases from VARN. Currently, 51 attorneys have indicated a willingness to accept cases. However, as discussed below, there are some areas needing improvement regarding this PAI activity area.

Since the VARN program’s reactivation in May 2008, and as of the date of the May 2009 visit, there have been 76 cases opened under the new NLS-VARN collaboration. However, since reactivation, no cases have been closed and reported in the CSR. It was explained that VARN had not sent any case closing information to NLS. However, it also appears that NLS did not conduct tight follow-up regarding these cases. VARN does have a case closure memorandum, but as of May 2009 none have been sent to NLS. According to the memorandum of agreement between NLS and VARN, the VARN PAI coordinator is responsible for all oversight and the interim PAI coordinator indicated that all PAI attorneys who have opened cases are sent an open case status memorandum on a quarterly basis. In the event the attorney does not respond to the memorandum, a telephone call is made. In discussions with VARN personnel and NLS personnel in Carson City it appears as though there are a number of cases that have been closed and should have been closed sometime ago but that VARN did not send the closing information to NLS and NLS’ did not actively seek closing information. This should be easy to remedy. As

¹³ As part of the reestablishment of this relationship, NLS agreed to repay past monies owed to VARN. NLS has agreed to a repayment plan for these funds. It should be noted that these payments for past monies owed are not allocable to PAI. However, monies allocated for present PAI activities should be fully allocable to PAI.

these cases are pro bono, NLS is strongly encouraged to ensure that all completed cases from 2008 be closed prior to the end of 2009, as they will then be still reportable in the 2009 CSR.¹⁴

According to VARN staff members there are basically three stages a prospective client goes through from initial intake to case closing. The first stage involves intake, the second an "awaiting placement" list and the third is "cases placed." VARN supplies additional reporting to NLS regarding intake, supplemental eligibility forms, and case status reports. It is recommended that the new NLS pro bono coordinator review the status reporting format and process used by VARN. This review should ensure that the formats and information systems are clear for any NLS staff relying upon these reports.

This collaboration requires that VARN obtain and return significant necessary intake or other information to NLS. However, NLS is opening cases before knowing whether the case will actually be placed with a private attorney. As a result of this set-up, there is concern that a significant number of these cases could end as an "X" case when the client does not return all necessary paperwork to VARN.¹⁵ It is suggested that NLS review other options for opening and sharing of these cases, and perhaps consider the cases being held as "pending" and only opened once all intake data has been received by NLS and the case is actually placed with a pro bono attorney.

In addition to the above issue with no cases being yet closed, there is need for improvement in the information obtained to ensure selection of the proper CSR closing code. The current VARN closing memorandum form requests the PAI attorney to indicate the level of service provided and to include a brief description of the services provided. The current CSR closing codes on this form do not conform to those in the revised 2008 CSR Handbook. The LSC team informed VARN staff that the LSC CSR Handbook and Frequently Asked Questions are both available on-line so that they could update the forms, and ensure familiarity with proper closing code usage. However, a better system is for the PAI attorneys to be asked to provide sufficient description of the services provided and then an appropriately trained VARN or NLS staff member can choose the proper closing code.

It is noted that VARN was to hire a new PAI coordinator soon after the May 2009 visit, and as such both programs have an excellent opportunity to together review and improve where needed, the documentation, case tracking and reporting systems, and the observations discussed above. Training for the VARN PAI coordinator should also be offered that includes basic LSC regulations and the 2008 CSR Handbook. It is also recommended that the new NLS pro bono coordinator review the VARN procedures and forms in use to ensure maximum efficiency and

¹⁴ According to the 2008 CSR Handbook, *PAI pro bono cases* have one extra year after completion in which they may still be reported and considered timely. Under this rule, even if a case was completed in early 2008, it may still be reported in 2009 by NLS under the flexibility allowed for this one case type.

¹⁵ In the past NLS did not intend to report VARN cases in the CSR. It was determined during the May 2009 review that these cases should be reported, to the maximum extent possible, as they are fully valid PAI cases and are necessary to report to demonstrate the effectiveness of the VARN PAI involvement.

success. Finally, corrective action should be taken by NLS to adopt an active follow-up system by NLS that ensures that VARN provides case closing information in an ongoing manner.

Despite the above-discussed observations, the few open cases tested did evidence that VARN did successfully capture all necessary information regarding financial as well as citizenship eligibility of the clients accepted for placement with PAI attorneys. The intake form used by VARN is a slight but acceptable modification of NLS' intake form. The form contains a separate and appropriately worded citizenship attestation. A small sample of seven open files was reviewed. These selections were taken from the VARN status reports. Three files requested could not be found in NLS' office and it is possible that these are examples of what would become "X" files as no legal work was likely performed. The remaining four cases were all financially eligible per LSC guidelines and each had citizenship documentation. Some cases also involved §1611.4 exceptions that were appropriately documented. As discussed above, there have been no VARN cases yet formally closed, so no closed cases could be tested.

Cases were also tested for two other active PAI efforts. In Las Vegas, sample PAI closed cases from the Tenants Rights Center and Senior Hotline were reviewed. All cases were fully compliant with LSC screening and eligibility requirements. Importantly, all cases had strong evidence of legal advice provided by a private attorney. One very minor CSR deviation was observed that should be corrected going forward. In three cases reviewed, a PAI attorney met with the client on two different occasions. Work completed after the first meeting was properly identified as an "A" service level. However on each of the second meetings, the attorney helped the client draft pleadings, and thus the category "B" was now the accurate closing code. However, all three cases remained closed as an "A".

Certain corrective actions related to PAI accounting issues were resolved. Other PAI accounting issues remain unresolved. Also, the 2008 audit used a defective formula and process for calculation of PAI with the result that the audited PAI figures for 2008 are unreliable.

SGC-5C required that no part of the program's expenditures for CCFLSHC be allocated towards the PAI calculation. The May 2009 review determined that NLS is clear and committed to keeping any CCFLSHC allocations away from PAI. However, as discussed below, until such time that a full and reliable indirect allocation formula is implemented by NLS, no overall final decision on proper PAI allocation can be made.

There were two related SGCs that addressed staff timekeeping for PAI. SGC-5D required NLS to ensure that only time specifically recorded as PAI be attributed to the PAI calculation. SGC-5E required that NLS take steps to ensure that its staff was properly recording PAI time as such as part of the contemporaneously timekeeping system. For SGC-3E, the May 2009 visit reviewed multiple PAI time samples and conducted multiple interviews of staff. This review evidenced that NLS took effective educational and oversight efforts to ensure that staff are

keeping appropriate PAI time. Regarding SGC-5D, until such time that a fully reliable cost system, including indirect costs, is implemented by NLS, no final decision regarding compliance with this SGC can be reached.¹⁶

SGC-5F required NLS to develop a written methodology for correctly allocating direct and indirect costs to the PAI effort. As of the May 2009 review, NLS had yet to demonstrate to LSC that it has created a clear method and practice in which to produce an accurate year-to-date PAI cost statement and related PAI budget variance. LSC has been requesting action in this area since May 2008 and it is a serious shortcoming that no clear final allocation method was in place and being used to assess PAI costs as of the May 2009 review. Without tracking PAI costs with such discipline, the NLS board is not positioned to have any clear idea of whether NLS might comply with the 12.5% PAI allocation.

During the May 2009 onsite review, NLS was provided clear instruction as to three effective methods by which it could allocate indirect costs to a funding source such as PAI. These are: (1) an allocation method using hours by taking the total number of PAI hours reported in timesheets and dividing it by the total number of hours (including vacation and leave); (2) an allocation method using salaries by taking the total amount of salaries as calculated from PAI time sheets and dividing it by the total amount of compensation paid to all staff (including vacation and leave); and (3) an allocation method using closed cases numbers in which the total number of PAI closed cases is divided by the total number of closed cases for the program. The final percentage used for any given year under any of the above three methods would not be clear until year-end. However, using one of the above methods each month will provide reasonable results for program management to determine whether the program is on track to meeting the minimum PAI allocation, and importantly if not, to make adjustments to increase the commitment of resources towards PAI activities.

From an attachment to its June 2009 monthly report NLS indicated that it had chosen to use "hours" to calculate its allocation percentage. However, the accompanying PAI cost figures did not clearly reflect how this was done consistently. Further, an attached three-page document titled "NLS Cost Allocation Method" had several statements that were unclear and confusing. This is a significant area of concern to LSC and remains an area of non-compliance with the 2008 SGCs. Further, the length of time that this has been an open item is problematic.

Related to the above, information obtained and reviewed during the May 2009 on-site review evidenced clearly *that the 2008 PAI audit calculations* were done under the outdated PAI allocation formula. This is a significant problem, as LSC had already rejected that formula as unsupported, outdated and erroneous. Further, it was this old formula that made necessary the specific 2008 corrective action to formulate a new method (SGC-5F). LSC had specifically required NLS to adopt and use a new PAI allocation formula as part of a set of SGCs provided in

¹⁶ NLS is reminded that all attorney and paralegal salaries must be allocated on a direct basis and only as supported by time sheets. In comparison, the allocation for administrative and support staff should be done on an indirect cost basis.

May 2008. Despite this, the NLS fiscal unit manager stated that he affirmatively recommended to the auditor to use the old formula in early 2009 when conducting the 2008 audit. Using the outdated formula for the 2008 audit with the existence of SGC-5F is a serious violation of the SGC process.

Other mistakes were noted with 2008 PAI cost allocations. In LSC PAI, certain direct PAI costs should be allocated strictly on a direct basis, and not be subjected to an indirect allocation formula. Typical costs included here are travel and training, although other direct costs, such as a publication subscription, would also be subject to direct costing only. While indirect cost formulas, discussed above, are applied to most general program costs, the general cost figures must first have specific PAI direct costs removed.¹⁷ For example, it was noted that indirect cost allocations were attributed in error to certain types of direct costs, such as a business trip. It is not a normal or acceptable practice to allocate indirect costs for business travel – rather only that portion of the direct cost that is allocable to a particular fund should be charged as such. Another error noted was that some of the direct costs identified as allocated in whole or in part to PAI did not evidence any connection to PAI activities.

Through 2008, there was also continued confusion in some fiscal records reviewed regarding the proper allocation of certain VARN related payments towards PAI, and the proper exclusion of other VARN payments that do not qualify for PAI allocation. Again, current year payments for current year PAI-related activities conducted by VARN are fully eligible for PAI reporting. However, “settlement” payments by NLS to VARN that represent repayments of monies owed to VARN (due to the actions by prior NLS management) do not qualify for current year PAI allocation.

As a result of these above accounting errors, and use of an outdated formula, the audited PAI figures for 2008 are fully unreliable.¹⁸

¹⁷ For example, if a program’s total publication costs for a year was \$2,000, but \$500 was for specific PAI only magazines, the \$500 would be directly applied to PAI, and the remaining \$1500 would then have the overall indirect cost allocation applied, for a further cost allocation that could be applied to PAI. As this example makes clear, the direct costs should be removed prior to applying an indirect cost formula.

¹⁸ This is also troubling as both NLS and LSC were anticipating that the program’s total PAI expenditures for 2008 would not reach the required 12.5% allocation, due to the need for continued PAI program development, and LSC was not requiring that this be fully resolved in 2008. However, what was important for 2008 was that the audited PAI figures were an accurate accounting of the PAI activities and related indirect costs that were properly conducted in 2008. This would have established 2008 as the first accurate PAI financial report for many years. Instead, 2008 PAI audited figures were again inaccurate with the result that the area of PAI financial accounting continues as an open issue.

Required improvements to judicare attorney contracts and related financial controls were fully implemented.

Three special grant conditions involved specific improvements to internal controls regarding judicare attorney payments, contracts and related procedures. SGC-5G required a new judicare attorney contract. SGC-5H required that all judicare attorneys execute a new contract with NLS. SGC 5-I required specific additional internal control procedures regarding judicare payments. All three of these interrelated SGCs have been fully implemented. LSC reviewed judicare records, contracts, procedures and tested related financial records during the May 2009 visit. Appropriate new judicare contracts, and payment procedures, are in place. Also, all judicare contracts were reviewed to ensure that updated agreements were on file, and there were no exceptions noted. These three SGCs and the underlying corrective action necessary have been fully addressed by NLS.

The NLS board and management took the necessary actions to comply with 45 CFR Part 1620 regarding the establishment of priorities.

The NLS board and management were required, under SGC-6, to adopt updated priorities following the procedural or other requirements of 45 CFR Part 1620. SGC-6A required NLS to complete a priorities survey and adopt an updated priorities statement by December 1, 2008. SGC-6B required specific attention to the annual board review requirement of 45 CFR §1620.5(b), and required that sufficient records be maintained to evidence its annual discussion and consideration of these criteria.

As discussed in the separate OPP letter provided to NLS regarding the May 2009 visit, the program, through the leadership of its board, took the appropriate and broad actions needed to update its priorities. In addition, the program followed the regulatory requirements regarding the priority setting process. It is also noted that a highly experienced consultant was used by NLS to assist in the priority setting process.

Certain specific compliance requirements related to priorities were successfully completed. The requirements of 45 CFR § 1620.6, which requires that all staff authorized to make case acceptance decisions must sign an agreement regarding implementation of the program's priorities, had been fully completed. NLS adopted three different forms that case handlers and staff must sign. The forms used comport, *inter alia* with the requirements of §1620.6.

A final test on priorities is that cases accepted must comply with program priorities. A targeted review of program case lists along with review of sampled cases evidenced that current NLS work is focused in priority areas.

NLS fully complied with SGC-7 that required immediate and full withdrawal from all hotel fire tort cases. Current NLS management quickly and fully terminated all prior activity on fee generating cases. NLS is in compliance with 45 CFR Part 1609 that prohibits fee generating cases, and with 45 CFR Part 1642 regarding claiming or collecting attorney fees.

45 CFR § 1609.2(a) defines a fee generating case as a case, which, if undertaken on behalf of an eligible client by a private attorney, could reasonably expect to result in a fee for legal services from an award to a client, from public funds or from the opposing party. Fee generating cases do not include those where (1) a court appoints a recipient or an employee of a recipient to provide representation in a case defined as fee generating under Sub Section A or (2) the recipient undertakes representation under contract with a government agency or other entity. 45 CFR 1609.3 provides that a recipient cannot provide legal assistance in a fee generating case unless (1) the case has been rejected by the local lawyer referral service or by two private attorneys or (2) neither the referral service nor two private attorneys will consider the case without the payment of a consultation fee. Also, 45 CFR Part 1642 prohibits the recipient or employee of a recipient from claiming or collecting attorney fees in a case undertaken on behalf of a client of a recipient except cases filed prior to April 26, 1996.

Under prior NLS management, there were numerous violations of 45 CFR Part 1609 caused by program involvement in several tort cases surrounding a fire in a Reno hotel. Under the new executive director, NLS took immediate corrective action to remove any NLS participation in these cases. Early in 2008, all Reno fire cases were closed via a closing memo from the Reno managing attorney to all clients informing the clients that NLS can no longer represent them in any way in that litigation. Further, review of program records evidenced that all of the Reno fire cases were coded as landlord tenant cases (69) and were all identified in Reno's "X" files, thus deselecting them as cases under the program's records.

Further, as required, staff and the board were trained on the requirements of these regulatory restrictions. Appropriate program policies have been adopted by NLS regarding these regulatory requirements. In the May 2009 visit, numerous staff members were interviewed regarding compliance with Parts 1609 and 1642. In addition, LSC conducted an extensive review of open and closed case lists, and targeted inspection of selected cases to test for regulatory compliance. The reviews and interviews discussed above evidenced that NLS has taken full corrective action as necessary and that the program is in compliance with these regulations. Finally, the certification provided by NLS in 2008, that addressed the requirements of SGC-7 regarding removal from the tort cases was found to be fully accurate.

NLS took effective actions to bring NLS into compliance with 45 CFR Part 1638 regarding the prohibition against solicitation.

45 CFR Part 1638 is designed to ensure that neither the recipient nor any employee solicits clients. 45 CFR § 1638.2(b) prohibits unsolicited advice to obtain counsel or take legal action by

a recipient or its employee to an individual who did not specifically seek the advice and with whom the recipient does not have an attorney client relationship.

Under prior management, NLS had violated Part 1638 through direct solicitation of clients involved with the Reno fire cases. As discussed above, under the new executive director, NLS quickly removed itself from the fire related cases. NLS was also required to train staff and take other actions that would ensure future compliance with Part 1638. NLS staff received related training regarding the program's responsibilities under Part 1638, and the regulatory restrictions. During the May 2009 review, the current state of program policy and staff awareness regarding the prohibition on solicitation was reviewed. Staff interviews and review of targeted sample cases evidenced that NLS is not engaged in the solicitation of cases. All staff members interviewed evidenced appropriate familiarity with this prohibition and none were aware of any violations of the program policy or regulation in 2008 and 2009. NLS has taken effective correction action as required and is now in compliance with 45 CFR Part 1638.

NLS took effective corrective action to address SGC-8 requiring targeted attention be given to compliance with the timekeeping requirements of 45 CFR Part 1635.

45 CFR Part 1635.2 requires case handler time keeping on all cases including PAI cases which will ensure proper allocation of the expenditure of LSC funds. Further, SGC-8 required NLS to implement enforcement and control procedures to ensure full compliance under the timekeeping requirements of 45 CFR Part 1635. LSC required that program procedures include a connection between proper time reporting and payroll, in that staff should not be paid unless they have correctly accounted for their time in sufficient detail. Under prior program management in late 2007, some serious non-compliance with the timekeeping regulation was identified by LSC by a few staff.

The prior noted non-compliance has been fully corrected by current NLS management. Interviews with staff, file reviews of sample cases for accurate use of time, and extensive review of program financial records, including several tests on employee timekeeping in all three offices evidenced that NLS is current in compliance with Part 1635. Time spent by NLS attorneys and paralegals in each case are documented in time records through NLS's computerized case system, thereby ensuring that time spent by a case handler is documented to the appropriate file. Sample time-related tests for selected cases indicated that attorneys, paralegals and staff input their time into NLS's computer program and identify specific cases. Further, review of total time records for sampled weeks evidenced that NLS staff record time as required to demonstrate that they account for at least 37.5 hours per week for full-time work and to support payroll. SGC-8 has been resolved by NLS.

NLS took all necessary actions required to comply with SGC-9 regarding compliance with LSC Grant Assurances.

Prior NLS management had violated certain LSC Grant Assurances. Further, when asked by LSC to correct this non-compliance, prior program management did not agree to full compliance with the LSC Grant Assurances. As a result, a special grant condition, SGC-9 required the NLS board to adopt a policy directing and ensuring that all staff and board fully comply with LSC Grant Assurances.

The NLS board promptly adopted the required policy and NLS provided required training regarding this requirement. Staff interviewed in May 2009 clearly indicated familiarity with grant assurance compliance and indicated that new program management had explained to them in trainings that staff are expected to follow the LSC Grant Assurances, wherever required. Further, LSC notes that the issue of Grant Assurance compliance appears limited to prior NLS staff who have since departed the program. LSC considers SGC-9 to have been fully and properly addressed.

NLS has fully complied with SGC-10 that requires the NLS board to adopt a policy for direct confidential staff reporting to the board.

SGC-10 requires the NLS board to adopt a written policy for direct confidential staff reporting to the board of any potential violations of the LSC Act which policy must contain a “whistle blower” protection policy statement. This special grant condition emanates from the Reno fire cases in which staff was apparently concerned about repercussions for coming forward to the board with evidence of clear violations of LSC regulations by prior program management.

The NLS board complied with this special grant condition by adopting a written “whistle blower policy” in 2008. As required by SGC-11, training for staff on this new policy was provided also in 2008. The May 2009 visit tested the awareness and quality of this policy. Interviews with staff and case handlers indicate that all were familiar with the written policy adopted by the NLS board and were aware of their ability to contact the NLS board directly and confidentially. Further, as required, staff and the board were aware of the LSC OIG Hotline as a source for reporting future issues. Further, several staff commented that they believe the program’s policy to be in good faith, and stated that they would feel safe approaching the current board under the policy should the need exist.

Extensive training required by LSC as part of the SGC process was effectively conducted.

SGC-11 required NLS to conduct all-staff training session(s) regarding all LSC rules, regulations, appropriations acts, restrictions, other guidance, and certain new program practices

and policies. This SGC also specified several items that required particular attention due to previous non-compliance noted at the program.

Training materials used to conduct the mandatory training of SGC-11 were reviewed. Further, several staff were interviewed regarding the training to determine the scope and depth of the topics covered. In addition, current staff awareness regarding areas of compliance covered by the training was assessed and tested in all offices visited during the May 2009 onsite review.

Looking to the future, NLS intends to have a detailed staff orientation and training process whereby all necessary compliance standards are taught so as to ensure continued staff awareness with the items of SGC-11.

The above actions evidenced that NLS fully complied with SGC-11 by providing effective training for staff to ensure the corrective of several areas of non-compliance.

Other Compliance Observations

In addition to reviewing all areas targeted by SGCs, the May 2009 review also assessed a few compliance requirements related to the proper screening and handling of LSC-funded cases. Findings regarding these assessments appear below.

NLS is in substantial compliance with the financial eligibility requirements of 45 CFR Part 1611.

NLS's case acceptance policy provides that legal services may be provided to an applicant whose income exceeds 125% of the Federal Poverty Guidelines (FPG) but not more than 200%. Approval is necessary to approve the provision of legal services to a client whose income is between 125% and 200% of the federal poverty guidelines. NLS procedures are fully compliant with regulatory requirements. Several sampled cases involved clients whose income was between 125% and 200% of FPG. In each of these instances there was documentation supporting the program's decision, including managing attorney approval for acceptance of the case.

NLS is in substantial compliance with the citizenship and residency screening requirements of 45 CFR Part 1626. Some additional attention to Reno cases for compliance with Part 1626 is however warranted.

Interviews with case handlers, staff and file reviews indicate that NLS has adequate guidelines to ensure the eligibility of applicants for legal services based on their citizenship or legal resident alien status. NLS policy requires all intake workers to obtain citizenship attestations in cases in

which the client makes a personal appearance to an NLS office or meets with an NLS case handler in person. In the case of a documented non-citizen, NLS requires the intake worker or case handler to record the type of document and the number of the document that verifies the applicant's eligibility for legal services. The only exception to this rule is the provision of legal services in abuse cases in which the verification of legal status is not required (although it is usually still obtained by NLS).

All files reviewed in which the applicant was not a citizen had the appropriate documentation required by 45 CFR Part 1626. Almost all files which required a citizenship attestation or other proper evidence of citizenship screening had the required documentation, with the exception of the three cases discussed below.

There were three citizenship attestation exceptions noted in sampled Reno cases. In the first case, the client was provided legal services to the point that a judgment was obtained without citizenship attestation or a retainer agreement. This case was closed under category "X" and not counted as an LSC funded case, which was a proper reaction to the mistake. *See* Reno Case No. 08-1021090. However, a citizenship attestation should be obtained for such cases in the future, especially when a court decision is obtained. Another Reno case was closed under category "X" due to the absence of a verification of citizenship (although there was also no evidence that legal services were provided to the applicant apart from the opening of a case and a referral to Reno's PAI judicare program). *See* Reno Case No. 06E-2012674. Finally, a third open Reno case was lacking several items: the file contained no citizenship attestation nor did it note the client's citizenship or residency status. As this case is an open case, the appropriate documentation should be quickly obtained. *See* Reno Case No. 08-1018382. As a result of these three cases, NLS should review the procedures and oversight processes of case intake, acceptance and review to ensure that required documentation under Part 1626 is obtained where needed, and at the beginning of the case.

Sampled cases evidenced substantial compliance with the client retainer agreement requirements of 45 CFR § 1611.9 and with the statement of facts requirements of 45 CFR Part 1636.

LSC recipients are required to execute a retainer agreement with each client who receives extended legal services from the recipient. *See* 45 CFR § 1611.9. The retainer must contain a statement identifying the legal problem for which representation is sought, and the nature of the legal service to be provided. *See* 45 CFR § 1611.9(a). NLS has an appropriate retainer agreement and NLS requires its case handlers to record the scope and subject matter of the legal assistance to be provided. Cases sampled evidenced substantial compliance with § 1611.9.¹⁹

¹⁹ There were two non-compliant cases noted: Case No. 08-1020263 that involved substantial legal services and that resulted in a judgment for the client but had no retainer; and Case No. 08-1020213 had a retainer agreement that was executed but contained no scope of services and had no date.

LSC recipients are required to obtain a statement of the client facts along with the client's identity for certain affirmative action cases. Interviews with staff and sampled cases indicate that NLS staff is properly aware of this requirement and that NLS is complying with 45 CFR Part 1636. NLS has drafted a form for statement of facts and client identity. However, cases sampled indicated that compliance with Part 1636 is often accomplished through either a verified petition or verified affidavit by the client setting forth the facts on which the case is based.

Future Actions

Consistent with the above discussion, the following additional recommendations or corrective action has been identified by LSC. As in the past, should the staff or board of NLS wish any assistance in the consideration and implementation of any of the following, please feel free to contact the team leader for your review.

Corrective Action

1. With its next SGC report due to LSC, NLS should provide to LSC its *templates* (no financial figures, just columns and lines with line item and column descriptions) for each of the following: Yearly Budget; Monthly Budget Variance report; PAI Year-to-Date expenditure report and PAI Budget Variance report.²⁰ Also, the indirect PAI allocation process, and any related template used to compute that part of the PAI costs should be provided.
2. NLS should periodically review the CCFLSHC budget to ensure that it includes all appropriate related costs, such as leave accrual and other benefits for the CCFLSHC assigned staff, as well as all appropriate indirect costs.
3. The NLS board should again review the operation of the fiscal unit and all related oversight systems, including the board's role, so as to ensure that at all times NLS policies are fully followed. As part of this review, NLS should adopt additional systems and oversight processes as necessary to provide additional cross-checking to ensure proper safeguarding of LSC funds. These new oversight and cross-check systems should ensure that the NLS board is quickly able to determine future instances in which any fiscal unit staff fails to follow board-established policy.
4. NLS and its board should again review and assess the process and results of PAI direct and indirect expenses to ensure that only PAI eligible direct activities are included, that

²⁰ If the PAI year-to-date and PAI budget variance are on the same accounting report, please provide only the one template that includes both of these items.

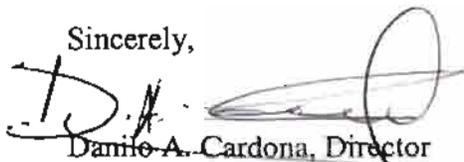
activities allocated to PAI clearly indicate their relation to this grant activity area, and that proper designation of direct and indirect expenses is conducted.

5. NLS should review the citizenship attestation findings of this letter and take appropriate action to ensure that the Reno office takes some additional steps to ensure that required attestations are required in all necessary circumstances.
6. NLS should take quick action to ensure that all VARN cases closed in 2008 and 2009 to date get appropriately closed and reported in the 2009 LSC CSR.
7. NLS should take immediate corrective action to reduce its excess fund balance so as to remove this pending issue and avoid possible LSC recovery of such amounts in the future.

Recommendations

1. NLS should adopt a new board conflicts policy that incorporates the prohibitions of 45 CFR §1607.3(3) and §1607.4(b). Subsequent to the adoption of a new policy, the NLS board should request all board members to execute a conflicts statement as required by the NLS policy.
2. The new NLS pro bono coordinator should review the findings and recommendations regarding the NLS/VARN relationship so as to consider and make any improvements that could improve the processing and timely closing of cases to be counted in the LSC CSR report, or other aspects of this relationship. As part of this review, NLS should consider adoption of a system whereby an appropriately trained NLS or VARN staff member is responsible for selecting an appropriate LSC closing code, based on the detail obtained from the private attorney regarding the services provided.

Sincerely,



Danilo A. Cardona, Director
Office of Compliance and Enforcement