



OFFICE OF LEGAL AFFAIRS

MEMORANDUM

TO: Operations and Regulations Committee

FROM: Victor M. Fortuno
Vice President & General Counsel

DATE: October 17, 2008

SUBJ: Staff Report on Alternative Sanctions: Follow-Up on Committee Information Requests and Management Recommendation

This report follows up from the August 1, 2008 meeting of the Operations and Regulations Committee. At that meeting the committee asked for additional information from Management on the use of particular enforcement tools and the situations in which they have been employed and Management's position on why the existing set of enforcement tools are not sufficient. The Committee also asked Management to follow up a concern expressed by some of the grantee participants at the Alternative Sanctions Rulemaking Workshop regarding instances in which compliance problems were caused by confusing or conflicting guidance provided by LSC with respect to various regulations. This Staff Report responds to those requests.

Selection and Use of Particular Enforcement Tools; Insufficiency of Existing Tools

The Committee asked for some specific statistics on the number of time particular enforcement tools have been used in recent years. Numbers have been compiled for the years 2002-2008 and are set forth below:

Enforcement Tool	Number of Times Used
Termination (in whole or part)	2
Debarment	1 (in process)
Suspension	1
Failure to Award a New Grant	1
Imposition of Month-to-Month or Other Short Funding	13*
Imposition of Special Grant Conditions	125*
Recovery of Funds Through a Questioned Cost Proceeding	11
Imposition of Corrective Action Plans	140

* Of these totals, 6 instances of imposition of month-to-month or short funding and 11 instances of imposition of special grant conditions were in connection with an ongoing compliance matter. LSC has used these mechanisms in additional instances to address other issues, such as quality or client services concerns.

It is clear from the statistics provided above, that LSC relies primarily upon the imposition of Corrective Action Plans (CAPs) to remedy compliance problems. This is not surprising, for as Management has noted before, most compliance problems found by LSC are easily corrected and most grantees work cooperatively with LSC to remedy compliance problems. Indeed, the Office of Compliance and Enforcement (“OCE”) estimates that in approximately 90% of cases, grantees implement CAPs on a timely and satisfactory basis. However, that does leave 10% of cases in which the recipient fails to implement CAPs on a timely or satisfactory basis.

The statistics also show that in at least some instances in which a grantee failed to remedy compliance problems through timely appropriate implementation of a CAP, LSC later imposed compliance measures in the form of special grant conditions. Although not substantively different than the measures contained in the CAPs, a special grant condition represents an higher level of formality and ensures that the Board Chair, who has to sign the special grant conditions, is aware of an ongoing problem. However, to the extent that special grant conditions, like CAPs, are not associated with any immediate sanction, a grantee unwilling to comply with a CAP may not be more persuaded to comply with a special grant condition. In fact, LSC has encountered instances in which a grantee, after failing to satisfactorily implement a CAP, similarly failed to implement special grant conditions addressing the exact same matters. Moreover, special grant conditions may only be imposed at the beginning of a grant year. As such, their utility can be limited by the timing of a particular compliance action.

As demonstrated by the chart, short term funding (as a compliance mechanism) is a measure that LSC has used only a limited number of times in the last several years, although it has been availing itself of short term funding as a compliance tool more in the very recent past (five of the six instances in which short term funding has been used have been in the period of 2006-2008). However, the utility of short funding is limited by the fact that it can only be employed when a grantee is at the end of a grant term and competing for a new grant. Further, depending on the grantee’s other funding, the effect of short term funding by LSC can vary significantly from one grantee to another (for example, if LSC funds are the only source of funding, month-to-month or other short term funding can potentially be destabilizing or debilitating). Thus, although short term funding can, in certain circumstances, be a powerful enforcement mechanism, it is one likely to be available and/or appropriate only in limited situations.

The statistics also demonstrate that LSC rarely invokes its most serious enforcement tools, termination and debarment. As has been noted previously, there are several reasons for this. First, in most instances, termination and debarment are simply unwarranted. However, even in situations in which such an ultimate sanction might be warranted, these particular tools are still rarely used because of the process required and the resource drain which the processes represents both for LSC and for recipients. In addition, with a sanction such as termination or debarment, LSC must consider the disruption such a sanction will cause to client services in the area. This is especially a problem with so many grantees providing services for an entire statewide service area. Finding new providers is a significant challenge and serves as a disincentive to the Corporation to employ tools that will eliminate or disqualify existing grantees.

With respect to suspension, the chart shows that it, too, is very rarely invoked. As with termination and debarment, there are several reasons for this. Foremost among these reasons is the fact that suspension is really a tool best suited only to certain types of compliance problems. Suspension is not a useful tool in a situation where the grantee has committed a violation that cannot be “remedied” by future action. For example, in an instance in which a grantee improperly collected attorneys’ fees, even though the violation was significant, there was nothing the grantee could do to “undo” that violation. As such, suspending the grantee’s funding would not have accomplished anything (in terms of remedying the violation). Similarly, suspension is not a good tool for violations requiring numerous or longer term remedies. For example, LSC has encountered at least one situation in which a grantee had systemic management problems and the necessary corrective action included the development and adoption of fiscal control policies. For the grantee, taking those actions, of necessity, required several months. Also, ensuring that the new policies were being properly implemented required additional time. In that situation, suspending the grantee and depriving the grantee of the funds necessary to operate and accomplish its longer term improvements would have been counterproductive.

Rather, suspension is most useful to force a grantee to perform a specific action which can be accomplished in a quick and discrete period of time. In the one instance during the period reported in which a suspension notice was issued, it was for the failure of the grantee to provide access to its auditors to enable the auditors to complete their work. In that instance, LSC notified the grantee that it intended to withhold the grantee’s funding in whole until the grantee provided the auditors with access to the necessary files. In that case, the grantee provided the access to the auditors, the proposed suspension was withdrawn before the proposed effective date and the grantee experienced no interruption in funding. However, even in circumstances in which suspension might usefully be imposed, the fact that for violations not involving the failure to provide an acceptable audit to the OIG the maximum suspension period is 30 days limits the utility of suspension as an enforcement mechanism. In a few instances in which LSC might have otherwise considered suspension, LSC determined that the resources required to pursue the suspension process would not be well invested given that any funds withheld would just have to be returned at the end of 30 days time, regardless of whether the violation had been remedied.

The inherent limitations on the practicality and propriety of termination, debarment and suspension, which has resulted in their very rare application, has another important implication – by and large these sanctions do not serve as effective deterrents. The value of a sanction should not be measured only in its application, but must also be considered in the context of its deterrent value. Although it is impossible to say, in the few instances in which LSC has elected not to refund a grantee in the competition process, debarred a grantee from future funding or has otherwise been able to convince a grantee to voluntarily relinquish a grant (without having to conduct a termination hearing), it is at least reasonable to consider whether the availability of additional sanction authority and additional enforcement tools would have provided LSC with sufficient leverage to convince such grantees to take the steps necessary to come into compliance prior to ending up in a situation in which cessation of funding was the only remaining appropriate option.

More specific examples may help to illustrate the issues discussed above. It is, of course, impossible to say for sure what exact course of action management would have followed in each of these cases if additional enforcement/sanction mechanisms had been available. In each case, it is fair to say, however that if additional tools been at management's disposal, management would have been able to consider whether and how their use could have been appropriate. At the least, the examples illustrate some of the constraints management has had to face with the set of enforcement and sanction mechanisms currently available to it.

Case Study #1

An LSC recipient was found to have violated the prohibitions and restrictions on involvement in fee generating cases (1609), solicitation (1638), and claiming attorneys' fees (1642). In this case, management did institute a questioned cost proceeding and recovered a sizeable amount funds (since the violations began with solicitation which rendered all of the program's activity impermissible, LSC was able to question all of the expenditures of LSC funds spent on the entire case) and the program was placed on short funding for a period and special grant conditions were imposed. However, a questioned cost proceeding is only remedial in nature. Similarly, the short funding and special grant conditions were designed to alleviate the conditions under which the violations occurred (and to our knowledge no future violations of this kind have occurred), but could not address the violations themselves. Management considered suspension, but it was deemed inadequate and not appropriate for the circumstances.

Case Study #2

An LSC recipient which was attorney of record in a dormant class action lawsuit continued participating in the case when it later became active again, in violation of the 1996 LSC restrictions and Part 1617. LSC contemplated instituting a questioned cost proceeding and instead reached an informal settlement with the program by which the program refunded money to LSC. Because LSC had no authority to impose a monetary penalty (without triggering the termination process), LSC had only limited leverage in its informal negotiations with this particular grantee.

Compliance Problems Related to LSC Interpretation/Application of Regulations

The Committee asked Management to follow up on one comment raised during the Rulemaking Workshop. Specifically, during the Workshop, some of the grantee participants expressed a concern regarding instances in which compliance problems were caused by confusing or conflicting guidance provided by LSC with respect to various regulations. The Committee asked Management to invite the Workshop participants to offer specific examples of instances in which the concern manifested itself.

Management issued such an invitation and only one Workshop participant responded. The comments of that participant, Tom Matsuda, Executive Director, Legal Services of Oregon (LASO) are provided for your reference. However, because Mr. Matsuda's comments focus on the requirements of Part 1610, Use of Non-LSC Funds, Transfers of LSC Funds and Program

Integrity and because LSC is currently in litigation with LASO over the applicability of this regulation, Management believes it is inappropriate to comment on that issue at this time.

Management Recommendation

Management recommends that the Committee recommend to the Board of Directors that the Board approve publication of the attached Draft Notice of Proposed Rulemaking (NPRM) in the Federal register for public comment. The Draft NPRM proposes amending LSC's regulations on termination and suspension of funding to provide additional flexibility. The Draft NPRM is essentially the same as the one presented to the Committee for its consideration in April, except that the preamble has been revised to conform to Federal Register publication requirements and the proposed regulatory text on suspension has been amended to expressly state that a suspension will be lifted when the grantee comes into compliance.

Specifically, it is proposed that the termination rule at 45 CFR Part 1606 be amended to include procedures for the imposition of reductions in funding of less than 5% of a grantee's annual level of funding from LSC. The new section that the Draft NPRM proposes be added to Part 1606 sets out a procedure that is largely modeled on the suspension procedure in Part 1623. The proposed revision to Part 1606 provides a straightforward process with significant opportunity for recipient input and due process. However, because the sanctions to which it would apply would be reductions of less than 5% of the recipient's LSC funding, as opposed to the temporary withholding of funds such as occurs in a suspension of funding, Management believes that it is appropriate to provide a process that goes beyond that used for suspensions. The Draft NPRM thus proposes to include a recommended determination step with the opportunity for appeal prior to the imposition of a limited reduction in funding. These proposed steps are modeled on similar provisions elsewhere in the termination rule. The Draft NPRM also contains several proposed conforming amendments.

It is also proposed that the suspension rule at 45 CFR Part 1623 be amended to increase from 30 to 180 days the maximum duration allowed for suspensions of LSC funding. The Draft NPRM's proposal to change the maximum duration for a funding suspension is a straightforward substitution of the term "180 days" for "30 days" in the relevant section of the existing regulation. A longer maximum suspension period would be a useful option due to its expected deterrent effect (thereby also enhancing the efficacy of non-monetary sanctions) and as a meaningful sanction in itself in the infrequent instances in which it would be needed. The Draft NPRM also includes in the regulation a statement clarifying that a suspension will be lifted when the grantee comes into compliance

Attachment