Increased Monitoring of the Low-Income Taxpayer Clinics Is Needed to Ensure Compliance with the Grant Terms and Conditions

May 2002

Reference Number: 2002-10-085

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

May 10, 2002

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

Pamela J Gardiner

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Increased Monitoring of the Low-Income Taxpayer Clinics Is Needed to Ensure Compliance with the Grant Terms and Conditions (Audit # 200110019)

This report presents the results of our review of the financial records of eight Low-Income Taxpayer Clinics (LITCs). The overall objective of this review was to determine whether the LITCs complied with the grant terms and conditions and the applicable laws and regulations related to the management of federal funds.

In summary, we believe the clinics, overall, are trying to meet the terms and conditions of the grants and also meet the goals and objectives of the LITC program. However, we believe some improvements are needed in documenting expenses and in-kind contributions, allocating expenses, identifying qualifying activities and LITC expenses, complying with the ethical guidelines, and matching the grant funds with non-federal funds. Without ensuring the proper accounting of LITC grant funds, the Internal Revenue Service (IRS) has no assurance that the funds are being properly expended to provide low-income taxpayers and individuals for whom English is a second language with tax assistance, as the Congress intended.

Management's Response: IRS management agreed to implement corrective actions for each of our three recommendations. Specifically, the IRS will take action to verify or recover unsupported expenses and issue ethical guidelines to the LITCs. The IRS has implemented a monitoring schedule that includes educating grant recipients about Office of Management and Budget guidelines and accounting for grant funds. In addition, the IRS Grants Administration Office plans on conducting 30 site visits in Fiscal Year 2002. The IRS has also requested a General Legal Services determination as to whether or not the LITCs may use Legal Services Corporation funds to meet their matching requirement. Management's complete response to the draft report is included as Appendix V.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

Table of Contents

Background ....Page 1

Improvements Are Needed to Ensure Appropriate Use of Grant Funds..Page 2

Recommendations 1 and 2: .... Page 9

Recommendation 3: .... Page 10

Appendix I – Detailed Objective, Scope, and Methodology ....Page 11

Appendix II – Major Contributors to This Report.......................................Page 14

Appendix III – Report Distribution List ....Page 15

Appendix IV – Outcome Measures...Page 16

Appendix V – Management's Response to the Draft Report ....Page 17

Background

The Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] authorized the IRS, subject to the availability of funds, to provide up to $6 million annually in matching funds[2] for the development, expansion, or continuation of qualified Low-Income Taxpayer Clinics (LITCs). The RRA 98 limits the amount that an individual clinic can receive to $100,000 a year. The LITCs provide legal assistance to low-income taxpayers who are in controversies with the IRS and/or operate programs to educate and inform individuals for whom English is a second language (ESL) about their tax rights and responsibilities. These clinics give the IRS an opportunity to increase overall compliance by providing service to a large number of taxpayers who otherwise might not receive assistance.

Since its inception in Fiscal Year (FY) 1999, the IRS' LITC grant program has continued to expand. In FY 1999, the IRS awarded approximately $1.5 million to 34 clinics in 19 states; in FY 2000, over $4.4 million was awarded to 70 clinics in 33 states; and in FY 2001, 102 clinics in 39 different states received $6 million.[3]

The audit work was performed from April to October 2001 in the Stakeholder Partnerships, Education and Communication (SPEC) area, Customer Assistance, Relationships and Education (CARE) division of the IRS Wage and Investment Business Unit in New Carrollton, MD, and various LITCs in Atlantic City, NJ; Phoenix, AZ; Chicago, IL;[4] Richmond, VA; Long Beach, NY; Jacksonville, FL; and Window Rock, AZ. During the time of our review, the LITC program was moved to the Wage and Investment headquarters in Atlanta, GA. The audit was

---

[1] IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, 112 Stat 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

[2] LITC grant recipients must provide matching funds on a dollar-for-dollar basis for all LITC grant funds received.

[3] The number of states (19, 33, and 39) all include Washington, DC.

[4] Visited two clinics in Chicago, IL.

conducted in accordance with *Government Auditing Standards.* Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Improvements Are Needed to Ensure Appropriate Use of Grant Funds

The IRS incorporated monitoring techniques into the grant agreements. These techniques include requiring each LITC to submit an interim and final financial and program reporting package. These reports detail the actual program costs incurred, the amount of grant funds requested, the amount of program income earned, the amount and source of matching funds, and the amount of in-kind contributions.

While the monitoring techniques provide valuable information, we believe additional actions are needed to ensure the grant funds are appropriately managed. Specifically, the Grant Administration Office should periodically verify the accuracy of the financial and program reports submitted by the clinics and provide additional education on how to account for grant funds. This information can be verified either by performing site visits or by requesting additional documentation to support the data included in the reports.

We examined the financial records of eight clinics and believe the clinics, overall, are trying to meet the terms and conditions of the grants and also meet the goals and objectives of the LITC program. However, we determined that improvements are needed in:

- Documenting expenses and in-kind contributions.
- Allocating expenses.
- Identifying qualifying activities and LITC expenses.
- Complying with ethical guidelines.
- Matching grant funds with non-federal funds.

Without ensuring the proper accounting of LITC grant funds, the IRS has no assurance that the funds are being properly expended to provide low-income and ESL taxpayers with tax assistance, as the Congress intended.

Documenting expenses and in-kind contributions

Five of the eight LITCs reviewed were not maintaining adequate documentation to support expenses and in-kind contributions. We could not verify approximately 16 percent ($81,828 of $502,929) of the expenses and in-kind contributions reported by these 5 clinics. When expenses and in-kind contributions cannot be properly verified, there is no assurance that the grant funds were used appropriately.

The Office of Management and Budget (OMB) Circular A-110, *Uniform Administrative Requirements for Grants and Other Agreements with Institutions of Higher Education, Hospitals, and Other Non-profit Organizations,* stipulates that grant recipients' accounting records need to be supported by source documentation. The 2000 Grant Application Package and Guidelines requires the clinics to maintain financial records including supporting documents for 3 years. OMB Circular A-110 also provides that all in-kind contributions be verifiable from the grant recipients' records. The Circular further provides that rates for volunteer services shall be consistent with those rates paid for similar work in the recipient's organization or consistent with those paid for similar work in the labor market in which the recipient competes for the kind of services involved. Additionally, the value of donated supplies shall be reasonable and shall not exceed fair market value at the time of the donation.

The following are examples of missing or inadequate supporting documentation identified during our site visits:

- One clinic used a journal entry to record an employee benefit expense of $11,500. However, the clinic could not provide any invoice, contract, cancelled check, or other documentation to support this expense.
- One clinic recorded $23,143 of in-kind contributions and prepared a spreadsheet as support. The spreadsheet indicated the amount of wages, lodging, meals, and mileage. However, the clinic did not have any invoices, receipts, bills, or other documentation to verify the accuracy of the amounts on the spreadsheet. For

example, no hotel bill or letter from the hotel was obtained to verify the reasonableness of the reported amount. In addition, the number of miles and mileage rate could not be verified.

- One clinic claimed volunteer services for in-kind contributions but did not adequately document how the rates claimed were determined.
- One clinic used estimates instead of actual expense amounts.

We believe that the accuracy of the financial information needs to be periodically verified through the performance of site visits. The Treasury Inspector General for Tax Administration (TIGTA) recently completed a review focusing on the administration of the LITC grant program. In this audit report,[5] the TIGTA reported that the Grant Administration Office was not consistently conducting site visits of the LITC grant recipients. Site visits were planned but put on hold because of a lack of resources. In August 2001, the IRS added staff to the Grant Administration Office to assist in monitoring the grant recipients. Additionally, the IRS is currently in the process of hiring personnel to fully staff the Grant Administration Office. Site visits will allow the IRS to ensure that grant funds are appropriately managed and provide the clinics with additional education.

Allocating expenses

The clinics used various methods to allocate expenses to their LITC program and the IRS grant. The allocation basis used at five of the eight clinics was either not appropriate or not supported. As a result, we could not verify that approximately $294,841 of expenses allocated to the LITC program and reimbursed by the IRS was used to support the program.

---

[5] *The Internal Revenue Service Should Continue to Make Improvements to the Low-Income Taxpayer Clinic Grant Program* (Reference Number 2002-10-024, dated November 2001).

Expenses were allocated based on the number of clients assisted, square footage used, percentage of time spent on LITC activities, percentage of grant revenues,[6] and the Executive Director's knowledge. Although the number of clients assisted, square footage used, and percentage of time spent are reasonable allocation methods, the clinics using these methods did not maintain documentation to support the allocation basis. For example, one clinic using percentage of time spent did not maintain time reports indicating the employees' time spent performing duties related to the LITC program.

We believe that the percentage of grant revenue allocation method is not appropriate for assigning costs because this method does not accurately assign the expense to the activity which received the benefit. Similarly, the Executive Director subjectively allocating expenses based on personal knowledge is also not an appropriate allocation method.

The OMB Circular A-122, *Cost Principles for Non-Profit Organizations*, stipulates that the allocation basis should take into account the expenses to be allocated. The essential consideration is ensuring that the allocation basis selected is the best method for assigning the expenses to the program which derived the benefit. Furthermore, the allocation basis should distribute expenses equitably to the federal government and the organization.

The Grant Application Package and Guidelines required the clinics to describe the method for allocating expenses but referred the clinics to the OMB Circular for guidance. This allowed the clinics to interpret the OMB Circular in selecting and implementing an allocation method. However, we believe additional education is needed regarding reasonable allocation methods so the clinics can select an appropriate method that best fits their accounting system.

---

[6] The clinic allocated total expenses by dividing the amount of the LITC grant by the total funding received by the clinic.

Identifying qualifying activities and LITC expenses

The RRA 98 identifies two activities for LITC program purposes. These two qualifying activities are the representation or referral of low-income taxpayers in controversies with the IRS and operation of a program to inform ESL individuals about their tax rights and duties. The 2000 Grant Application Package and Guidelines provides two examples of a program to inform. Both examples involve LITC employees interacting directly with the ESL taxpayers.

One clinic generated revenue by selling training materials to other LITCs and conducting training seminars for other LITCs' employees. Such activity is not considered a qualifying activity under the LITC program guidelines.

The clinic developed training materials to assist its employees and its network of pro bono professionals in understanding the tax issues faced by low-income taxpayers and the related court proceedings for taxpayers in controversy with the IRS. The clinic discovered that other LITCs could benefit from the materials and they desired additional guidance regarding the LITC program. As a result, the clinic began to assist other LITCs by selling the training materials and conducting training seminars.

Since management at the clinic believed the training activities were qualified activities, the costs associated with the training activities were included when the LITC requested reimbursement. Although the training is not a qualifying activity, the expenditure of grant funds for such training may be considered "training directly and totally associated with the program." However, this clinic did not subtract the training revenue from the expenses for these training activities. In at least 2 instances, this resulted in double counting of expenses of approximately $1,500. The clinic providing the training activities initially incurred and claimed the expense. Also, the clinic purchasing the training materials and services claimed the expense. Therefore, both parties were reimbursed for the same expense.

The IRS needs to ensure that grant funds are only used to pay for qualifying activities. Additionally, if the IRS considers this type of expense to be "directly and totally associated with the LITC program," the IRS should ensure that multiple clinics are not claiming the expense.

Complying with ethical guidelines

One clinic failed to comply with the ethical guidelines outlined in the 2000 Grant Application Package and Guidelines. The clinic referred ESL taxpayers to an organization that charged fees for its service. This action appears to be in violation of Section VIII, Part H of the 2000 Grant Application Package and Guidelines which requires all referrals to be to pro bono organizations.

The clinic was referring ESL taxpayers with controversies with the IRS to a law firm charging fees for services performed, which is not the kind of referral activity that makes a clinic eligible for an LITC grant. Under the Grant Application Package and Guidelines, the grant-eligible activity is the "referral of low-income taxpayers to entities or organizations providing pro bono legal services to low-income individuals." Furthermore, the clinic appears to be in violation of the LITC program ethics guideline.

The Clinic Program Coordinator informed us that the clinic was not aware it was in violation of the ethics guideline. Additionally, the Program Coordinator indicated that the clinic has recently changed its policy of referring taxpayers to an organization that charges fees for its services.

Although the clinic did not intentionally violate the ethics guideline, this activity could result in serious consequences for the clinic. OMB Circular A-110 provides several actions that can be taken if a recipient materially fails to comply with the terms and conditions of a grant award. These range from temporarily withholding cash payments pending correction of the deficiency by the recipient to terminating the grant award. Additionally, the 2000 Grant Application Package and Guidelines allows the IRS, in its discretion, to require repayment of funds or terminate the grant agreement.

Matching grant funds with non-federal funds

One clinic used monies received from the Legal Services Corporation (LSC), a federally funded non-profit corporation, to match the LITC grant. In their grant application, the clinic indicated their intention to use LSC monies as matching funds. However, the clinic did not obtain written permission to use the LSC funds to meet their matching requirement, as required by law.

Under the Code of Federal Regulations,[7] recipients of LSC funds may use the funds to meet matching requirements for federal grants only if the federal agency whose grant funds are being matched has determined in writing that LSC funds may be used. The IRS 1999, 2000, and 2001 LITC Grant Application Package and Guidelines do not specifically provide for the use of LSC funds for LITC matching purposes, nor do they appear to include any provisions that could be interpreted as allowing for such use. Recipients of LSC funds, therefore, could not use such funds to meet the matching funds requirement. Allowing the clinic to use LSC monies without informing other potential grant applicants created an unfair competitive advantage.

The clinic provided us with a LSC Legal Counsel opinion which states that LSC funds may be used for the matching requirement with the written consent of the awarding agency. Clinic management explained they believed they could use LSC funds to meet the matching requirement of the LITC grant because of discussions with the former IRS program manager. However, they did not get this permission in writing.

Many organizations receiving monies from the LSC may have established an LITC and submitted an application for a grant if the ability to use LSC monies for the matching requirement had been publicized. If the IRS continues to allow LSC funds to be used to meet the matching requirement, this policy needs to be publicized to all potential grant applicants.

---

[7] 45 C.F.R. § 1630.3 (a)(8).

Recommendations

1. The Director, SPEC, should take appropriate action regarding the $83,328 of questioned costs and the noncompliance with ethical guidelines, including recouping grant funds, not awarding future grants, and/or providing technical advice to the LITCs.

   Management's Response: The IRS will obtain testimony or sworn affidavits from the grant recipients by July 15, 2002. The IRS will also pursue available verification and validation methods to justify the costs. If found to be inappropriate, the Grants Administration Office will take corrective actions on the specific noncompliance. If it is determined that recovery of undocumented grant funds is necessary, the Grants Administration Office will pursue this recovery by September 15, 2002. To address the noncompliance with ethical guidelines, the IRS will provide guidance to the LITCs by January 15, 2003.

2. The Director, SPEC, should provide additional education and ensure periodic site visits are consistently conducted to verify that the clinics are complying with the grant terms and conditions. Specifically, the education provided and the site visits should include the reasonableness, allowability, and support for expenses; the reasonableness and support for the allocation basis; the identification of qualifying and non-qualifying activities; the allocation of expenses between qualifying and non-qualifying activities; and the adherence to the ethical guidelines.

   Management's Response: In August 2001, the IRS added a staff member to assist in monitoring grant recipients. Monitoring activities, which include educating grant recipients about OMB guidelines and accounting for grant funds, are conducted in person and from the headquarters office. The Grants Administration Office has scheduled 30 site visits for FY 2002 during which it plans to use a check sheet to document the activities of the clinics. The site visits may be educational (for new clinics), random (after one year of operation), or technical (the check sheet is completed and books are reviewed).

3. The Director, SPEC, should evaluate whether to allow the clinics to use LSC monies to match LITC funds and, if so, publicize the decision in the Grant Application Package and Guidelines.

   Management's Response: The IRS has requested a General Legal Services' determination as to whether or not the clinics may use LSC funds to meet their matching requirement. If the determination is available, the IRS will include clarifying language in the 2003 Grant Application Package.

   Office of Audit Comment: IRS management agreed to implement corrective action for our three recommendations. However, the IRS response disagrees with two points in our report. Specifically, the IRS disagrees that improper accounting methods prevent the effective delivery of tax assistance to low-income and ESL taxpayers; and, that a LITC referred ESL taxpayers to an organization that charged fees for its services.

   We believe that without the proper accounting, there is no assurance that the funds the IRS is providing to the clinics are being used to provide tax assistance to low-income and ESL taxpayers. Therefore, there is no assurance that the LITC program is operating at an optimum level of effectiveness, commensurate with the funding provided. Additionally, our audit work shows that one clinic was referring ESL taxpayers to a law firm which charged a nominal fee. As noted in the report, the Clinic's Program Coordinator informed us they were not aware this was an ethical violation and the clinic has changed its policy.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine whether the Low-Income Taxpayer Clinics (LITCs) complied with the grant terms and conditions and the applicable laws and regulations related to the management of federal funds. To accomplish this objective, we:

I. Determined whether the LITCs were properly managing the grant funds.

   A. Reviewed the LITCs' Single Audit Act[1] reports and determined if the reports contained findings that would affect the adequacy of the LITCs' accounting systems or that specifically and directly deal with the LITC grant for our sample of grant recipients in test I.C.

   B. Reviewed the applicable legislation, Office of Management and Budget (OMB) policies, and Internal Revenue Service (IRS) procedures and determined the allowability and allocability of expenses. Obtained a Treasury Inspector General for Tax Administration (TIGTA) Counsel opinion for interpretation of applicable regulations, policies, and procedures.

   C. Judgmentally selected a sample of the LITCs and determined whether each LITC's reported expenses were allowable, allocable, and reasonable. A judgment sample was used because we did not plan on projecting the results to the universe.

      1. Prepared a sampling plan outlining the criteria used to select the sample of grant recipients. A sample of 8 LITCs was selected from the 60 LITCs which received a grant in both Fiscal Years (FY) 2000 and 2001. We considered the concerns raised by the IRS program office, prior issues found by the Treasury Inspector General for Tax Administration, significant increases in the amount awarded, decreases in the amount awarded, the dollar amount of the FY 2000 award, Single Audit Act report findings, and problems noted by the IRS Procurement Cost and Pricing branch.

      2. For grant recipients included in the sample of eight LITCs, judgmentally selected a sample of expenses. A judgment sample was used because we did not plan on projecting the results to the universe.

[1] Single Audit Act of 1984, Pub. L. No. 98-502 and Single Audit Act Amendments of 1986, Pub. L. No. 104-156.

a. Prepared a sampling plan outlining the criteria used. The expenses included in the sample were selected based on the accounting method used by the clinics. In some instances, we randomly selected a month to test expenses and then judgmentally selected other expenses throughout the year based on the type of expense. In other instances, we tested all the expenses.

b. Traced the expenses to the supporting documentation and determined the allowability, allocability, and reasonableness of the expenses.

3. Conducted interviews and determined how each LITC allocated expenses between qualifying and non-qualifying activities.

D. Determined whether the LITCs had any unexpended grant funds at the end of the grant period and if these funds were returned to the IRS.

1. Reviewed the requests for reimbursement and determined the amount of grant funds received by the LITC.

2. Compared the amount of grant funds received to the total expenses incurred and determined if the LITC had any unexpended funds at the end of the grant period and if these funds were subsequently returned to the IRS.

3. Conducted interviews and determined the process used to ensure that all grant funds received by the LITCs were either expended or returned to the IRS.

II. Determined whether the LITCs were appropriately matching the IRS grant funds.

A. Reviewed the applicable legislation, OMB polices, IRS procedures, and grant applications and determined the requirements for matching funds.

B. Using the sample of eight LITCs selected in test I.C., conducted detailed testing of grant recipients.

1. Reviewed the final financial status report and determined the amount of matching funds, donations, program income, and expenses and compared the amounts to the grant award.

2. Traced the donations counted as matching funds to the source documents.

a. For cash contributions, determined whether monies were federal funds.

b. For equipment donations, determined the source, inspected the equipment, and verified the accuracy and reasonableness of the fair market value calculation.

c. For donations of services, verified the accuracy and reasonableness of the fair market value calculations. Traced the hours worked to timekeeping records.

d. For other donations, determined the source of the donation. Verified the accuracy and reasonableness of the fair market value calculation.

3. Traced the nominal fees and program income to the source documents and bank statements. Determined whether the monies were federal funds.

Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)
John R. Wright, Director
Debra L. Gregory, Audit Manager
Regina Dougherty, Senior Auditor
Theresa Haley, Senior Auditor
Melvin Lindsey, Senior Auditor
Thomas Dori, Auditor
Niurka Thomas, Auditor

Appendix III

Report Distribution List

Commissioner N:C
Deputy Commissioner, Wage and Investment Division W
Director, Customer Assistance, Relationships and Education W:CAR
Director, Stakeholder Partnerships, Education and Communication W:CAR:SPEC
Director, Strategy and Finance W:S
Chief Counsel CC
National Taxpayer Advocate TA
Director, Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O
Office of Management Controls N:CFO:F:M
Audit Liaison: Wage and Investment Division W

Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Cost Savings, Questioned Costs (Unsupported) – Actual; $81,828 (see page 2).
- Cost Savings, Questioned Costs (Unallowable) – Actual; $1,500 (see page 2).
- Protection of Resources – Potential; $294,841 (see page 2).

Methodology Used to Measure the Reported Benefit:

To determine the unsupported questioned costs, we reviewed the financial records and documentation maintained to support the expenses and in-kind contributions reported by eight Low-Income Taxpayer Clinics (LITCs). We determined the amount of expenses and in-kind contributions that were not supported by invoices, payroll records, or independent verifications of the fair market value of the donations. We identified 5 clinics that did not maintain sufficient documentation for various expenses and in-kind contributions totaling $81,828.

To determine the unallowable questioned costs, we interviewed various personnel at the clinics, reviewed the clinics' financial records and related documents, and obtained a legal opinion. We determined that the training services provided by 1 clinic were double counted in the amount of $1,500. The clinic providing the training activities initially incurred and claimed the expense. Also, the clinic purchasing the training materials and services claimed the expense. Therefore, both parties were reimbursed for the same expense.

To determine the protection of resources, we interviewed various personnel at the clinics and reviewed the clinics' financial records and related documents. We determined that the allocation methods used at five of the eight clinics were inappropriate or unsupported. Therefore, we could not verify $294,841, which was the portion of LITC expenses the clinics received from the Internal Revenue Service for the LITC grant.

Appendix V

Management's Response to the Draft Report

COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

April 1, 2002

RECEIVED
APR 01 2002

MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

FROM: John M. Dalrymple
Commissioner, Wage and Investment Division

SUBJECT: Draft Report – Increased Monitoring of the Low-Income Taxpayer Clinics is Needed to Ensure Compliance with the Grant Terms and Conditions (Audit # 200110019)

Thank you for your report concerning our need to monitor low-income taxpayer clinics (LITC). The report underscores our already strong commitment to ensure that LITC grant monies are used effectively and for the purposes for which they were intended.

You note our significant expansion of the program from the year of inception, Fiscal Year (FY) 1999, through FY 2001. This expansion from 34 clinics in 19 states to 102 clinics in 39 states was accomplished with a dedicated IRS staff of three employees. While dealing with the challenges, we have taken the following additional steps toward our goal of reaching an under served taxpayer segment. One staff member executed a 3-day National LITC Conference for all awardees. The Grants Administration Office expects to complete a web-based application that will be available for the 2003 application open season. We have an inter-agency multiyear contractual relationship with the Department of Health and Human Services, which provides electronic management and distribution of grantee awards. To reduce stakeholder burden, we have analysts dedicated to serving as account representatives. Using other internal stakeholders, we established a Grants Advisory Board to provide input and guidance for grant administration. We also partnered with Communications and Governmental Liaison to develop a marketing strategy to assure that we reach low-income taxpayers in states without a LITC.

For Recommendation 1, we disagree that improper accounting methods prevent the effective delivery of tax assistance to low-income and English as a second language (ESL) taxpayers. We also disagree with your finding that a LITC referred ESL taxpayers to an organization that charged fees for its service. However, we agree with your other findings in Recommendation 1. We have implemented a record keeping monitoring program and will issue ethical guidelines for LITCs and take action to verify or recover unverified expenses. We also agree with Recommendations 2 and 3.

Our corrective actions are detailed below.

RECOMMENDATION # 1

The Director, SPEC, should take appropriate action regarding the $83,328 of questioned costs and the noncompliance with ethical guidelines, including recouping grant funds, not awarding future grants, and/or providing technical advice to the LITCs.

ASSESSMENT OF CAUSE

Five of the eight LITCs reviewed were not maintaining adequate documentation to support expenses and in-kind contributions. The TIGTA could not verify approximately 16 percent ($81,828 of $502,929) of the expenses and in-kind contributions reported by these five clinics.

One clinic failed to comply with the ethical guidelines outlined in the 2000 Grant Application Package and Guidelines. The clinic referred ESL taxpayers to an organization that charged fees for its service. This action appears to be in violation of Section VIII, Part H of the 2000 Grant Application Package and Guidelines, which requires all referrals be made to pro-bono organizations.

CORRECTIVE ACTIONS

We agree that validation of the $81,828 of unsupported expenses is critical. We plan to obtain testimony or sworn affidavits from the grant recipients by July 15, 2002. We will also pursue available verification and validation methods to justify the costs. If found to be inappropriate, the Grants Administration Office will take corrective actions on the specific noncompliance. If we determine that recovery of undocumented grant funds is necessary, the Grants Administration Office will pursue that action based on OMB Circular A-110 by September 15, 2002.

We disagree with the finding that improper accounting methods prevent LITCs from delivering tax assistance to provide low-income and ESL taxpayers. We believe that improvements in the documentation and record keeping process are the issues. To ensure that grant recipients are following acceptable record keeping methods, the Grants Administration Office instituted a monitoring program beginning March 15, 2002, which includes educating recipients on program management procedures.

We agree that we must address noncompliance with ethical guidelines. We will provide guidance to LITCs on these topics January 15, 2003.

We disagree with the finding that one clinic failed to comply with ethical guidelines by referring ESL taxpayers to an organization that charged fees for its service. We found that the clinic collected a nominal fee for clinic services (tax counseling and return preparation) and then referred taxpayer data to a pro-bono accountant. The pro-bono accountant used his office location to complete the verification process while the clinic was the recipient of the nominal fee. Internal Revenue Code section 7526 provides that clinics not charge more than a nominal fee for clinic services.

IMPLEMENTATION DATE

To obtain affidavits or testimony: July 15, 2002
To pursue recovery of undocumented fund disbursements: September 15, 2002
To institute a monitoring program: Completed March 15, 2002
To issue ethical guidance: January 15, 2003

RESPONSIBLE OFFICIAL

Director, Stakeholder Partnerships, Education and Communication (SPEC)

CORRECTIVE ACTION MONITORING PLAN

We will obtain status reports on each action item from the Grants Administration Office in biweekly reports.

RECOMMENDATION # 2

The Director, SPEC, should provide additional education and ensure periodic site visits are consistently conducted to verify that the clinics are complying with the grant terms and conditions. Specifically, the education provided and the site visits should include the reasonableness, allowability, and support for expenses; the reasonableness and support for the allocation basis; the identification of qualifying and non-qualifying activities; the allocation of expenses between qualifying and non-qualifying activities; and the adherence to the ethical guidelines.

ASSESSMENT OF CAUSE

Planned site visits were postponed due to a lack of resources. Site visits will enable the IRS to ensure that grant funds are appropriately managed and provide the clinics with additional education.

CORRECTIVE ACTION

In August 2001, a staff member was added to assist in monitoring grant recipients. Monitoring activities are conducted in person and from the headquarters office. We have implemented a rigorous monitoring schedule that includes educating grant recipients about OMB guidelines and accounting for grant funds.

The Grants Administration Office has 30 site visits scheduled for FY 2002. We plan to use the check sheet already developed as part of the monitoring process to document activities of the clinics.

Site visits may be educational (for new clinics), random (after 1 year of operation), or technical (the check sheet is completed and books are reviewed). All ESL clinics are visited.

IMPLEMENTATION DATE

January 15, 2003

RESPONSIBLE OFFICIAL

Director, SPEC

CORRECTIVE ACTION MONITORING PLAN

We will use the check sheet already developed.

RECOMMENDATION # 3

The Director, SPEC, should evaluate whether to allow the clinics to use LSC monies to match LITC funds and, if so, publicize the decision in the Grant Application Package and Guidelines.

ASSESSMENT OF CAUSE

Under the Code of Federal Regulations, recipients of Legal Services Corporation (LSC) funds may use the funds to meet matching requirements for federal grants only if the federal agency whose grant funds are being matched has determined in writing that they can use LSC funds. The IRS 1999, 2000, and 2001 LITC Grant Application Package and Guidelines do not specifically provide for the use of LSC funds for LITC matching purposes, nor do they appear to include any provisions that could be interpreted as allowing for such use. Recipients of LSC funds, therefore, could not use such funds to meet the matching funds requirement. Allowing the clinic to use LSC monies without informing other potential grant applicants created an unfair competitive advantage.

CORRECTIVE ACTION

We have requested a General Legal Services determination as to whether or not the clinics may use LSC funds to meet their matching requirement. If the determination is available, we will include clarifying language in the 2003 Grant Application Package.

IMPLEMENTATION DATE

December 15, 2002

RESPONSIBLE OFFICIAL

Director, SPEC

If you have any questions or need additional information regarding this response, please contact Keith Restaino, Chief, Grants Administration at (404) 338-8723.