

regulations to allow VA to make lower payments based on such negotiations.

DATES: *Effective Date:* November 7, 2000.

FOR FURTHER INFORMATION CONTACT: Tony Guagliardo, Health Administration Service, (10C3), Veterans Health Administration, Department of Veterans Affairs, 810 Vermont Avenue, NW., Washington, DC 20420, (202) 273-8307. (This is not a toll-free number.)

SUPPLEMENTARY INFORMATION:

Administrative Procedure Act

This document allows VA to pay hospitals and physicians the amount that they on their own or through agents have negotiated to receive from VA. Accordingly, this document reflects contract actions that are exempt from the prior notice-and-comment and delayed effective date provisions of 5 U.S.C. 553.

Unfunded Mandates

The Unfunded Mandates Reform Act requires (in section 202) that agencies prepare an assessment of anticipated costs and benefits before developing any rule that may result in an expenditure by State, local, or tribal governments, in the aggregate, or by the private sector of \$100 million or more in any given year. This rule would have no consequential effect on State, local, or tribal governments.

Regulatory Flexibility Act

The Secretary hereby certifies that this rule will not have a significant economic impact on a substantial number of small entities as they are defined in the Regulatory Flexibility Act, 5 U.S.C. 601-612. This rule would affect only a small portion of the business of the affected entities. Accordingly, pursuant to 5 U.S.C. 605(b), this rule is exempt from the initial and final regulatory flexibility analysis requirements of §§ 603 and 604.

Catalog of Federal Domestic Assistance Numbers

The Catalog of Federal domestic assistance numbers for the programs affected by this rule are 64.005, 64.007, 64.008, 64.009, 64.010, 64.011, 64.012, 64.013, 64.014, 64.015, 64.016, 64.018, 64.019, 64.022, and 64.025.

List of Subjects in 38 CFR Part 17

Administrative practice and procedure, Alcohol abuse, Alcoholism, Claims, Day care, Dental health, Drug abuse, Foreign relations, Government contracts, Grant programs health, Grant programs-veterans, Health care, Health facilities, Health professions, Health records, Homeless, Medical and dental

schools, Medical devices, Medical research, Mental health programs, Nursing homes, Philippines, Reporting and record-keeping requirements, Scholarships and fellowships, Travel and transportation expenses, Veterans.

Approved: October 31, 2000.

Hershel W. Gober,

Acting Secretary of Veterans Affairs.

For the reasons set out in the preamble, 38 CFR part 17 is amended as set forth below:

PART 17—MEDICAL

1. The authority citation for part 17 continues to read as follows:

Authority: 38 U.S.C. 501, 1721, unless otherwise noted.

2. In § 17.55, a new paragraph (k) is added; and the authority citation at the end of the section is revised, to read as follows:

§ 17.55 Payment for authorized public or private hospital care.

* * * * *

(k) Notwithstanding other provisions of this section, VA, for public or private hospital care covered by this section, will pay the lesser of the amount determined under paragraphs (a) through (j) of this section or the amount negotiated with the hospital or its agent.

(Authority: 38 USC 513, 1703, 1728; § 233 of P. L. 99-576)

3. Remove the undesignated center heading immediately before § 17.56.

4. In § 17.56, a new paragraph (e) is added to read as follows:

§ 17.56 Payment for non-VA physician services associated with outpatient and inpatient care provided at non-VA facilities.

* * * * *

(e) Notwithstanding other provisions of this section, VA, for physician services covered by this section, will pay the lesser of the amount determined under paragraphs (a) through (d) of this section or the amount negotiated with the physician or the physician's agent.

(Authority: 38 U.S.C. 513, 38 U.S.C. 1703, 38 U.S.C. 1728)

5. Add an undesignated center heading immediately before § 17.57 to read as follows:

Use of Community Nursing Home Care Facilities.

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LEGAL SERVICES CORPORATION

45 CFR Part 1628

Recipient Fund Balances

AGENCY: Legal Services Corporation.

ACTION: Final rule.

SUMMARY: This final rule revises the Corporation's rule on recipient fund balances to provide the Corporation with more discretion to determine whether to permit a recipient to maintain a fund balance of up to 25% of its LSC support for a particular reporting period and to specify a limited number of extraordinary and compelling circumstances for which LSC has discretion to permit a recipient to maintain a fund balance in excess of 25% of its LSC support. The final rule also adds additional requirements and limitations applicable to waiver requests and the use of excess fund balances. Finally, the rule is restructured for clarity and for consistency with other Corporation regulations.

EFFECTIVE DATE: This final rule is effective on December 7, 2000.

FOR FURTHER INFORMATION CONTACT: Victor M. Fortuno, Vice President for Legal Affairs, Legal Services Corporation, 750 First Street, NE.—Suite 1000, Washington, DC 20002-4250; 202-336-8800.

SUPPLEMENTARY INFORMATION: On September 11, 1998, the Operations and Regulations Committee ("Committee") of the Legal Services Corporation ("LSC" or "the Corporation") Board of Directors ("Board") met to consider proposed revisions to the Corporation's rule governing recipient fund balances, 45 CFR part 1628. The Committee adopted a proposed rule that was published in the **Federal Register** for public comment at 63 FR 56591 (October 22, 1998). Nineteen comments were received and considered by the Corporation.

Following the close of the comment period, the Committee met on February 21, 1999, to review the public comment on the proposed rule. No action was taken on the proposed rule at that time as the Committee was advised by the Corporation's staff that additional time was needed to consider fully a number of issues raised by the public comment and to formulate informed recommendations for the Committee's consideration in adopting a final rule.

The Committee was briefed by staff on two issues raised by one commenter which challenged the legal sufficiency of the proposed rulemaking and the legal authority for the Corporation to permit any carryover of fund balances

by recipients. The commenter's legal sufficiency claim was mistakenly based on the Administrative Procedures Act, a law which does not apply to LSC rulemaking, and a similarly erroneous allegation that the public record failed to include certain "factual information" on which LSC relied—or, in the eyes of the commenter, should have relied—in developing the proposed rule. As explained to the Committee, the preamble to the proposed rule properly incorporated by reference information which was already a matter of public record and readily made these materials and any other factual information available to the public upon request. The commenter further asserted that the Corporation's proposed fund balance provisions were contrary to federal law, specifically relying on the Office of Management and Budget Circular A-110, Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations (OMB Circular A-110). Contrary to the commenter's assertion, OMB Circular A-110 expressly authorizes the recipients to carry forward unobligated balances to subsequent funding periods. OMB Circular A-110, § .25(e)(3), 58 FR 62992, 62999 (November 29, 1993).

On June 11, 1999, the Committee again met to consider public comments on the proposed rule. The Committee adopted a number of revisions to the rule, but deferred action on the final rule pending additional staff research into the policies and practices of other agencies awarding federal grants and contracts with regard to extraordinary and compelling circumstances for the carryover of an excess fund balance. The Committee took under consideration the need to permit a fund balance in excess of its 25% limitation in extraordinary cases, where a recipient received a large, lump-sum infusion of funds, for example, from the sale of real property, insurance proceeds, or a court-awarded judgment. Where such funds are derived from the past expenditure of LSC funds, they may, because of the amount or timing of their receipt, cause a fund balance in excess of 25% of the recipient's total LSC support for that year. In particular, the Committee sought additional information from staff on the policies adopted by federal agencies with regard to grantee fund balances and whether fund balances in excess of 25% of a grantee's annual federal support are ever permitted, and, if so, under what circumstances.

On November 19, 1999, the Committee met to consider the staff's report on the outstanding issues raised

at its last meeting and to again receive public comment. The Committee was advised that in 1993, OMB Circular A-110, the governing authority for most federal grants to non-profit organizations, was amended to expand the authority of discretionary grantees to undertake certain types of administrative actions without prior agency approval, including the ability to carry forward unobligated fund balances into a subsequent funding period (58 FR 62992, November 29, 1993). Having reviewed the regulations and policies issued by more than twenty federal agencies under the amended OMB guidelines, LSC staff advised the Committee that the Corporation's proposed fund balance policies were more strict than those adopted by most federal agencies. Few federal agencies employ a cap on the amount of funds that may be carried over by a grantee, with or without prior agency approval. Most agencies require notification of fund balances, and some reserve the discretion to disallow the carryover or to offset it against future grant funds under particular circumstances, such as when it exceeded 25% of the grant award, or the grantee was at high risk of failure to comply with statutory requirements. Staff also provided the Committee with a breakout of the fund balances reported by recipients for fiscal year 1997, the most recent, complete data available. After considering the staff report and taking other public comment on the rule, the Committee made a number of additional revisions to the rule and voted to recommend to the Board that the rule as revised be adopted as a final rule. On November 20, 1999, the Board did adopt as final the rule as revised and reported by the Committee.

This final rule is intended to provide the Corporation with more discretion to determine whether to permit a recipient to maintain a fund balance of up to 25% of its LSC support for a particular period and sets forth the requirements and limitations applicable to waiver requests and the uses of fund balances. The final rule also authorizes the Corporation to exercise its discretion to waive the 25% cap on excess fund balances in three specific circumstances when extraordinary and compelling reasons exist for such a waiver. Finally, the rule is restructured for clarity and consistency with other LSC regulations.

A section-by-section analysis is provided below.

Section-by-Section Analysis

Section 1628.1 Purpose

The final rule adopts the revisions to this section as proposed. Those revisions deleted or moved parts of the section because they were not statements of the purpose of the rule. As revised, the purpose of the rule is stated as setting forth the Corporation's policies and procedures for recipient fund balances. The final rule retains the underlying intent of the current rule which is to ensure the timely expenditure of LSC funds for the effective and economical provision of high quality legal assistance to eligible clients.

Section 1628.2 Definitions

The proposed rule clarified and updated the meaning of three of the current terms to make them consistent with other changes in LSC regulations, and retained a fourth term without change.

In the final rule, "excess fund balance" has been added as a defined term for clarity. "Excess fund balance" is defined to mean the amount of a recipient's LSC fund balance that exceeds the amount the recipient is authorized to retain under the regulation.

As proposed, the term "LSC support" was defined as the sum of three amounts: (1) The recipient's LSC carryover funds from the prior fiscal year; (2) the amount of the recipient's LSC grant for the year in question; and (3) any LSC derivative income earned by the recipient during the year in question. In the final rule, the Corporation has deleted a recipient's prior year carryover funds from the definition of LSC support. As pointed out during the comment period, including carryover funds in LSC support could artificially inflate the amount of funds permitted to be carried over under the percentage ceilings used in the rule. As this result was not intended by the Corporation, the reference to the prior year's carryover funds has been deleted and the remaining components of the definition of "LSC support" renumbered accordingly. The language was further amended to make clear the fiscal year being referenced and that one-time and special purpose grants were not to be included in the definition of "LSC support" as either financial assistance or derivative income. The rules governing fund balances for one-time and special purpose grants are discussed in more detail in § 1628.3(g) below.

The final rule replaces the defined term "fund balance amount" with "fund balance" for ease of use and clarity. Other minor language changes were also incorporated for clarity. The final definition makes clear that a "fund balance" is the amount by which LSC support, together with the prior year's carryover amount of LSC Funds, exceeds the recipient's expenditures of LSC Funds, including capital acquisitions, as these amounts are reported in the recipient's annual audit. Some commenters recommended doing away with the term "fund balance" altogether as that term is inconsistent with generally accepted accounting principles set forth in the Statement of Financial Accounting Standards (FASB) No. 117, Financial Statements for Not-for-Profit Organizations. The current FASB Statement No. 117 speaks in terms of three categories of "net assets" rather than fund accounting. This issue was addressed by the Corporation in 1997 when it republished its Accounting Guide for LSC Recipients (August, 1997) following the FASB Statement No. 117 change. To permit the separate reporting of LSC revenue and expenditures, while at the same time adhering to Statement No. 117, Section 2-4 of LSC's Accounting Guide requires separate reporting, preferably through a supplemental schedule to be attached to audited financial statements prepared in accordance with FASB Statement No. 117. The supplemental schedule details the receipt and expenditure of LSC funds and permits the calculation of the LSC "fund balance." Therefore, the final rule retains the term "fund balance."

The final rule retains the meaning of the term "fund balance percentage" but has revised the language to be consistent with its use as a defined term. The fund balance percentage is the percentage ratio of the LSC fund balance to the recipient's LSC support.

The final rule adopts without change the proposed definition of "recipient," which was updated to reflect the current law limiting grants for financial assistance to those authorized by § 1006(a)(1)(A) of the LSC Act and to be consistent with the meaning of the term as defined elsewhere in the regulations.

Section 1628.3 Policy

The proposed rule restructured this section to consolidate statements of general policy on recipient fund balances in this section and to move provisions that dealt more with procedure to other sections of the rule.

Paragraph (a) states the Corporation's long-standing policy that recipients may, without any prior LSC approval,

retain a fund balance of up to 10% of their LSC support. While this policy has not changed from the current rule, the Corporation received significant comment urging that the ceiling on fund balances be raised. A number of commenters argued that their own accountants or auditors recommended higher fund balance retention in the interests of sound financial management for nonprofit corporations. The commenters, however, differed on the appropriate level for such fund balances, with recommendations ranging as low as one month's operating expenses to three or six months of expenses, or even higher. The majority of the recipients that commented suggested increasing the fund balance which could be retained without specific LSC approval to between 15% and 25% of LSC support. Several commenters noted that their other funders generally did not permit their funds to be included in fund balances, making the inclusion of LSC funds for this purpose more critical for the recipient's stability as an ongoing enterprise and to ease the transition for the recipient should it lose some or all of its LSC funding.

The Corporation has retained the 10% ceiling on the level of fund balances that recipients may carryover without specific LSC approval. The Corporation was not convinced by the comments that a higher level was either necessary or appropriate at this time. The primary purpose of LSC funding is to enable the recipient to provide a maximum of high quality legal assistance to eligible clients, rather than to underwrite the long term fiscal stability of the recipient. There is an inherent tension between the purpose of the grant funds and the non-expenditure of these funds solely to underwrite the entity's viability as an ongoing enterprise. Nothing in the comments persuades the Corporation that an amount in excess of the current 10% ceiling is necessary.

In 1980, the GAO was critical of fund balances between 20% and 31% of a recipient's annual grant. While OMB introduced more flexibility into grantee administration of its federal funding through its amendments to Circular A-110, there is no empirical evidence that the GAO criticisms of fund balances for LSC recipients are any less valid today. Nor have the commenters demonstrated any compelling need for higher fund balances. Additionally, large fund balances could create the potential for misuse of such funds. In 1997, the last year for which complete records were available, recipients carried over \$17.9 million in LSC funding, compared to \$49.6 million in non-LSC funding. The

data further reflect that most recipients report carry over of funds and that, of those that do, the majority carried over significantly more non-LSC funds than LSC funds. These data tend to refute the argument of the commenters that LSC funds are necessary for an adequate fund balance because of the general lack of non-LSC funds available for this purpose. Nor does the Corporation adhere to the principle underlying these claims, that LSC funds should be used to underwrite a recipient's financial stability when other funders will not do so. Especially with the advent of competitive grants, LSC would prefer to have its grants go to client service rather than to reserve funds for grant transition activities and needs. Where such needs exist, LSC can provide the necessary funding.

Paragraph (b) permits recipients to request a waiver from LSC to retain a fund balance of up to 25% of their LSC support. Such waivers are granted at the discretion of LSC and require a showing of special circumstances to justify the waiver. As discussed above, several commenters sought a fund balance ceiling of 25% or higher to be automatic, rather than by waiver. However, the Corporation disagreed with these comments and has retained the ceiling of 10% for fund balances which can be retained without prior LSC approval, and up to 25% only upon a waiver request to LSC, supported by a showing of special circumstance. Consistent with the proposed rulemaking, however, LSC has relaxed somewhat the showing required to obtain a waiver for a fund balance of up to 25% of a recipient's LSC support. The particular standards are discussed below in § 1628.4.

In the final rule, the Corporation has added a new paragraph (c) which permits a recipient to request a waiver to retain a fund balance in excess of 25% of their LSC support in extraordinary and compelling circumstances. The rule further limits "extraordinary and compelling circumstances" by specifying only three possible sources for such funds: (1) An insurance reimbursement; (2) the sale of real property; and (3) the receipt of monies from a lawsuit in which the recipient was a party.

Although the Corporation did not find it necessary or appropriate to raise the ceilings in effect for routine fund balance carryovers or waivers, it was swayed by the comments concerning unusual and compelling circumstances which could arise that may justify retention of a fund balance in excess of 25% of a recipient's LSC support. In general these circumstances arise when

there is a sudden and unexpected infusion of funds which are derived from prior LSC grant funds but are not part of the current year's funding. By their nature, these funds may be substantial in amount. Instances discussed included the settlement of an insurance claim resulting in the payment to the recipient of a large insurance reimbursement; the receipt of a substantial amount as proceeds from the sale of real property; or, the receipt of an award based on a judgment or settlement in a lawsuit to which the recipient was a party. In these cases, because of the timing of the receipt of the funds or the amount of such funds or both, it may be more prudent to permit the recipient to carryover the funding into the next fiscal year, even if the amount of the carryover will exceed 25%, than to require the recipient to spend the funds in the fiscal year received. The recipient can better plan and find the best use for the funds, rather than being forced into a hasty expenditure simply to avoid the limitation on the carryover of fund balances and the resultant surrender of the excess fund balances to the Corporation.

The Committee considered using a standard of "extraordinary and compelling" for these waivers with the three specific circumstances discussed as examples. However, it was felt that more guidance was required to avoid erosion of the standard. Therefore, the Board ultimately decided to limit the permissible circumstances for these extraordinary waivers to the three conditions which have in the past been known to give rise to the sudden infusion of large sums, and hence may precipitate the need for a waiver. By limiting the circumstances justifying such waivers, the Corporation intends to provide notice to recipients of the limited types of circumstance in which extraordinary excess fund balances will be tolerated, thereby avoiding any misunderstanding, abuse, or erosion of the standard.

In the final rule, proposed paragraph (c) is relettered as (d) and otherwise retains the policy that the granting of any waiver request is at the discretion of the Corporation. The final rule makes explicit that the discretion to grant a waiver applies to both requests for waivers of up to 25% of a recipient's LSC support and for waivers in excess of 25%. In addition, the final rule refers to the criteria in § 1628.4(d) which governs the Corporation's exercise of its waiver discretion.

In the final rule, proposed paragraph (d) is relettered as (e) and continues to state that, absent a waiver, a fund

balance in excess of 10% of LSC support is to be repaid to the Corporation. In addition, the final rule continues the policy requiring repayment to LSC of any amount in excess of the amount permitted under a waiver granted by the Corporation. As suggested during the comment period, the two sentences describing the alternative means of repayment have been moved to the section on procedures (see § 1628.4(c)).

In the final rule, proposed paragraph (e) is relettered as (f), but is otherwise unchanged. It continues to clarify LSC policy that the recovery of excess fund balances does not constitute a termination of funds under Part 1606 of the Corporation's regulations.

Finally, the final rule reletters paragraph (f) as (g) and retains the substance of the proposed rule to make clear that one-time and special purpose grants awarded by the Corporation are not subject to the fund balance rules in this part, are not part of the calculation of fund balances pursuant to this rule, but are to be separately accounted for and reported. The rule also continues LSC's policy that unexpended funds from one-time and special purpose grants must be returned to the Corporation at the end of the grant term unless the Corporation has approved the expenditure of those funds in writing. The Corporation Office of Compliance and Enforcement is planning to update the LSC Accounting Guide to reflect the revisions to the rule, including treatment of one-time and special purpose grants as provided for in this provision.

Section 1628.4 Procedure

This section sets out the procedures applicable to recipient fund balances. It has been revised to provide the basis on which the Corporation will exercise its discretion to grant a waiver of an excess fund balance and the requirements which are intended to ensure careful oversight by the Corporation of a recipient's fund balances. The procedures apply to both waivers of the 10% ceiling for a fund balance of up to 25% of a recipient's LSC support and waivers of the 25% ceiling in extraordinary and compelling circumstances. The final rule consolidates the procedural requirements in the current rule in this section and updates those requirements as necessary.

Paragraph (a) of the final rule sets out the timeframe for recipients whose fund balance exceeds the 10% ceiling to request a waiver from the Corporation and the required content of such waiver requests. The final rule provides a recipient with 30 days from the

submission of the recipient's annual financial audit in which to request a waiver. By tying the waiver request to the submission date for the recipient's annual financial audit, the Corporation intends to place recipients on notice of a fixed date for such requests. As used in this paragraph, the submission date for the recipient's annual financial audit is the date on which such audit is due to be submitted to the Corporation, which is currently specified in the LSC Audit Guide as 120 days from the close of the grantee's fiscal year.

Several comments urged that the rule provide for advance or preliminary approvals. According to the comments, advance approval would permit better fiscal planning and would allow the expenditure of fund balances earlier in the following fiscal year. Although these concerns have merit, approval is by definition based on the amount of fund balance indicated in the recipient's audit, and that audit is not available until after the end of the fiscal year. This rule does not preclude the recipient's request for a Corporation action on a waiver prior to the close of the fiscal year, it simply does not require the Corporation to provide for advance approval. The Corporation already has a practice of providing informal guidance to recipients who inquire early about their anticipated fund balances. This practice will continue to be available to recipients, but need not be required by regulation.

Paragraph (a) of the final rule incorporates the content of waiver requests which was specified in paragraph (c) of the proposed rule. The final rule continues to require that waiver requests specify: (1) The fund balance as reported in the recipient's annual audit; (2) the reason for the excess fund balance; (3) the recipient's plans for use of the excess fund balance; (4) the fund balance, if any, that the recipient projects for the current fiscal year; and (5) the circumstances justifying retention of the excess fund balance. The Corporation revised item (3) to delete the proposed reference to a Technology Investment Plan and other specific requirements related to information technology systems. The Corporation decided there was insufficient support for singling out information technology systems for special treatment under its fund balance rules. The need to acquire or update the hardware or software related to a recipient's information technology systems is simply one example of equipment or property acquisition for which an excess fund balance may be used. Other stylistic and clarifying language changes have been made,

including expanding the reference to circumstances in item (5) to include both the special circumstances required to justify the retention of an excess fund balance of up to 25% of the recipient's LSC support and the extraordinary and compelling circumstances specified in § 1628.3(c) necessary to justify retention of a fund balance in excess of 25% of the recipient's LSC support.

The Corporation proposed in paragraph (b) of this section to identify its obligations to consider the recipient's final audit, fund balance statements, and waiver requests, if any, and to provide timely written notice to the recipient of any fund balance amount to be recovered and the method of recovery. In the final rule, the scope of paragraph (b) was narrowed to focus on the Corporation's obligation to respond in a timely fashion to a recipient's request for a waiver or to notify the recipient that the excess fund balance must be repaid to the Corporation. In addition, the final rule requires that the Corporation respond within 45 days of its receipt of a waiver request. The 45 day period for the Corporation's decision and response to a waiver request was deemed reasonable and necessary because of the likelihood that multiple requests would be submitted at about the same time each year. In this regard, the written response to a waiver request or notice of demand for repayment of the excess fund balance may be provided by the Corporation by physical delivery, such as regular mail, or electronically, such as e-mail, when feasible. Either method is likewise acceptable for the submission of waiver requests.

The final rule contains a new paragraph (c) which consolidates the information previously located in paragraph (b) (discussed above) concerning the timeliness of repayment notices and in the policy section (see § 1628.3(e), *supra*) concerning the methods of repayment. The final rule continues to require written notice of repayment of an excess fund balance at least 30 days prior to the date when repayment is due. Furthermore, the final rule continues to authorize the Corporation to decide, after consultation with the recipient, on the method of repayment. Two repayment methods are contemplated: a lump sum payment or a pro rated deduction from the recipient's monthly grant payments spread over a specified number of months. Irrespective of the recovery method used, however, the recipient should generally expect the recovery to be complete within the term of the current grant.

Paragraph (d) of the proposed rule stated that excess fund balances could not be expended by the recipient prior to approval by the Corporation of a waiver request. This paragraph has been deleted from the final rule as unnecessary and redundant. It remains the policy of the Corporation that a recipient needs to obtain LSC's approval of a waiver request before it may expend any excess fund balances.

In the final rule, proposed paragraph (e) is relettered as paragraph (d) and continues to identify the standards governing the Corporation's decision to grant a waiver request. The overarching standard continues to be that recipients provide high quality legal assistance to clients in an effective and economical manner. While prohibiting excess fund balances promotes this purpose, regulated use of carryover funds under certain circumstances is also consistent with this purpose. Based on changing needs and the Corporation's experience with fund balances since 1984, the standards enumerated in paragraph (d) are intended to reflect both generally and specifically the circumstances under which the Corporation may grant a fund balance waiver.

The first standard under paragraph (d) garnered the most comment. The Corporation had proposed relaxing the standard from "emergencies, or unusual or unexpected occurrences, or extraordinary circumstances" to "emergencies, unusual or unexpected occurrences, or circumstances" which give rise to an excess fund balance. Commenters generally approved the broader discretion available to the Corporation under the proposed standard. According to the commenters, justifiable reasons for waiving the 10% ceiling on fund balance retention exist which do not rise to the current standard of "extraordinary circumstances." One commenter, however, critiqued the proposed standard as too lax and feared it may result in a *de facto* increase in the ceiling on fund balances from 10% to 25%.

In the final rule, the standard has been changed to refer to the "circumstances giving rise to the existence of a fund balance in excess of 10% of LSC support set out in § 1628.3(b) or (c)." Thus, the final standard incorporates by reference the need for "special circumstances" to justify a waiver to retain an excess fund balance of up to 25% of a recipient's LSC support and "extraordinary and compelling circumstances" as specified in § 1628.3(c) to justify a waiver for a fund balance in excess of 25% of a recipient's LSC support. For waivers of

up to 25% of LSC support, the Corporation has more flexibility and discretion than under the current standard to grant a waiver, while at the same time requiring a showing of a special circumstance to avoid such waivers from becoming the norm. Moreover, to obtain a waiver in excess of 25% of LSC support, the recipient must demonstrate that one of the three circumstances specified in § 1628.3(c) gave rise to the excess fund balance in order to show extraordinary and compelling circumstances to justify a waiver. Thus, the ability of a recipient to obtain a waiver to retain a fund balance in excess of 25% of its LSC support is narrowly circumscribed.

Moreover, the circumstances giving rise to the excess fund balance remain but one of four factors to be considered by the Corporation in granting or denying a waiver request. The final rule retains without change two factors from the current rule: the special needs of clients and the recipient's financial management record. The final factor combines subparagraphs (3) and (4) of the proposed rule into a single subparagraph (3) in the final rule. As revised, subparagraph (3) in the final rule retains authority for the Corporation to consider the recipient's need for a cash reserve for payments to private attorneys participating in the recipient's private attorney involvement ("PAI") program and adds language authorizing the consideration of the recipient's need to acquire equipment or property or for other expenditures which are reasonable and necessary for the performance of the LSC grant. The additional language, in part, replaces the proposed rule's subparagraph (4) which separately stated as a factor the recipient's need for a cash reserve to replace or update information technology systems. Only a few comments addressed the technology issue and a review of past fund balance requests and prior approval requests under Part 1630 (Cost standards and procedures) indicated no need for a specific regulatory factor related solely to information technology systems. The language in the final rule is expected to provide the Corporation with sufficient discretion and flexibility to deal with a variety of requests for waivers, not merely those related to information technology systems. For example, a cash reserve in a coming fiscal year may be needed to acquire new property or to acquire equipment that may make the program more accessible to handicapped clients, or for additional staff necessary to handle an anticipated influx of clients due to changes in

medical, housing or other benefits adversely impacting on the client community.

In the final rule, the proposed new paragraph (f) is re-lettered as paragraph (e), and its substantive provisions for tighter controls on the use of fund balances by recipients are retained without change. Thus, the Corporation's written approval of waiver request will specify the time period within which the excess fund balance must be expended and the uses for which the funds may be expended. In specifying the time period for the expenditure of any excess fund balances, the Corporation's written approval will indicate whether the expenditure may be permitted beyond the end of the current fiscal year.

The final rule retains as paragraph (f) the current and proposed requirements for the separate reporting of any excess fund balance retained by a recipient for expenditure pursuant to an approved waiver request. Revisions to this paragraph clarify that approved excess fund balances should be reported separately by natural line item in the current fiscal year's audited financial statements. "Natural line item" or "natural expense classification" is a term of art in the accounting field which means the itemizing of expenses according to the kinds of economic benefits received by incurring the expense. Examples of natural line items or natural expense classifications include salaries and wages, employee benefits, supplies, rent, and utilities. See the American Institute of Certified Public Accountants Audit and Accounting Guide for Not-for-Profit Organizations, June 1, 1996 edition, Glossary, at 367.

Finally, in the final rule, a new paragraph (g) has been added. Paragraph (g) requires recipients to inform the Corporation of and seek its guidance with respect to changes in the conditions on the timing or purposes for the expenditure of excess fund balances as set out in the Corporation's written approval of a waiver request. The new paragraph is intended to place recipients on notice of their obligation to inform LSC of changes in circumstances which make compliance with the terms and conditions of their waiver difficult or impossible, for example, uncontrollable delays in settling on the purchase of new property, sudden and unexpected market changes that may alter the economics of a planned purchase, or newly emergent priorities for which the expenditure should be redirected. The Corporation will then provide the recipient with guidance on whether the

change in the purpose of the expenditure or the need for more time for the expenditure, or both, warrants a change in the conditions for the waiver. Failure of a recipient to notify the Corporation and obtain approval for changes in its waiver conditions could result in any nonconforming expenditures being treated as a questioned cost by the Corporation under Part 1630.

Section 1628.5 Fund Balance Deficits

The final rule retains with only minor technical or clarifying changes the provisions of the current rules governing recipient deficits. Deficits continue to be discouraged and use of LSC funds to liquidate a deficit requires prior Corporation approval. Absent prior approval, LSC funds used for this purpose will result in a questioned cost. Only a few conforming language changes have been made to this section.

List of Subjects in 45 CFR Part 1628

Administrative practice and procedures, Legal services

For reasons set forth in the preamble, LSC revises 45 CFR Part 1628 to read as follows:

PART 1628—RECIPIENT FUND BALANCES

Sec.

- 1628.1 Purpose.
- 1628.2 Definitions.
- 1628.3 Policy.
- 1628.4 Procedures.
- 1628.5 Fund balance deficits.

Authority: 42 U.S.C. 2996e(b)(1)(A), 2996f(a)(3).

§ 1628.1 Purpose

The purpose of this part is to set out the Corporation's policies and procedures applicable to recipient fund balances. The Corporation's fund balance policies are intended to ensure the timely expenditure of LSC funds for the effective and economical provision of high quality legal assistance to eligible clients.

§ 1628.2 Definitions.

(a) *Excess fund balance* means a recipient's LSC fund balance that exceeds the amount a recipient is permitted to retain under this part.

(b) *LSC support* means the sum of:

(1) The amount of financial assistance awarded by the Corporation to the recipient for the fiscal year included in the recipient's annual audited financial statement, not including one-time and special purpose grants; and

(2) Any LSC derivative income, as defined in § 1630.2(c), earned by the recipient for the fiscal year included in

the recipient's annual audited financial statement, not including derivative income from one-time and special purpose grants.

(c) The LSC *fund balance* is the excess of LSC support plus the prior year carryover amount over expenditures of LSC funds (including capital acquisitions), as each is reported in the recipient's annual financial statements.

(d) The *fund balance percentage* is the amount of the LSC fund balance expressed as a percentage of the recipient's LSC support.

(e) *Recipient*, as used in this part, means any grantee or contractor receiving financial assistance from the Corporation under section 1006(a)(1)(A) of the LSC Act.

§ 1628.3 Policy.

(a) Recipients are permitted to retain from one fiscal year to the next LSC fund balances up to 10% of their LSC support.

(b) Recipients may request a waiver to retain a fund balance up to a maximum of 25% of their LSC support for special circumstances.

(c) Recipients may request a waiver to retain a fund balance in excess of 25% of a recipient's LSC support only for the following extraordinary and compelling circumstances when the recipient receives an insurance reimbursement, the proceeds from the sale of real property, or a payment from a lawsuit in which the recipient was a party.

(d) A waiver pursuant to paragraph (b) or (c) of this section may be granted at the discretion of the Corporation pursuant to the criteria set out in § 1628.4(d).

(e) In the absence of a waiver, a fund balance in excess of 10% of LSC support shall be repaid to the Corporation. If a waiver of the 10% ceiling is granted, any fund balance in excess of the amount permitted to be retained shall be repaid to the Corporation.

(f) A recovery of an excess fund balance pursuant to this part does not constitute a termination under 45 CFR part 1606. See § 1606.2(c)(2)(ii).

(g) One-time and special purpose grants awarded by the Corporation are not subject to the fund balance policy set forth in this part. Revenue and expenses relating to such grants shall be reflected separately in the audit report submitted to the Corporation. This may be done by establishing a separate fund or by providing a separate supplemental schedule of revenue and expenses related to such grants as a part of the audit report. No funds provided under a one-time or special purpose grant may be expended subsequent to the expiration date of the grant without the

prior written approval of the Corporation. Absent approval from the Corporation, all unexpended funds under such grants shall be returned to the Corporation.

§ 1628.4 Procedures.

(a) Within 30 days of the submission to LSC of its annual audited financial statements, a recipient may request a waiver of the 10% ceiling on LSC fund balances. The request shall specify:

(1) The LSC fund balance as reported in the recipient's annual audited financial statements;

(2) The reason(s) the excess fund balance resulted;

(3) The recipient's plan for disposition of the excess fund balance during the current fiscal year;

(4) The amount of fund balance projected to be carried forward at the close of the recipient's current fiscal year; and

(5) The special circumstances justifying the retention of the excess fund balance up to 25%, or the extraordinary and compelling circumstances set out in § 1628.3(c) justifying a fund balance in excess of 25%.

(b) Within 45 days of receipt of the recipient's waiver request submitted pursuant to paragraph (a) of this section, the Corporation shall provide a written response to the request and a written notice to the recipient of any fund balance due and payable to the Corporation as well as the method for repayment.

(c) In the event that repayment is required, the Corporation shall give written notice 30 days prior to the effective date for repayment. Repayment shall be in a lump sum or by pro rata deductions from the recipient's grant checks for a specific number of months. The Corporation shall determine which of the specified methods of repayment is reasonable and appropriate in each case after consultation with the recipient.

(d) The decision of the Corporation regarding the granting of a waiver shall be guided by the statutory mandate requiring the recipient to provide high quality legal services in an effective and economical manner. In addition, the Corporation shall consider the following factors:

(1) Emergencies, unusual or unexpected occurrences, or the circumstances giving rise to the existence of a fund balance in excess of 10% of LSC support set out in § 1628.3(b) or (c);

(2) the special needs of clients;

(3) The need to retain a cash reserve for payments to private attorneys

participating in the recipient's private attorney involvement (PAI) program; for acquisition of equipment or property; or for other expenditures which are reasonable and necessary for the performance of the LSC grant; and

(4) The recipient's financial management record.

(e) The Corporation's written approval of a request for a waiver shall require that the recipient use the funds it is permitted to retain within the time period set out in the approval and for the purposes approved by the Corporation.

(f) Excess fund balances approved by the Corporation for expenditure by a recipient shall be separately reported by natural line item in the current fiscal year's audited financial statements. This may be done by establishing a separate fund or by providing a separate supplemental schedule as part of the audit report.

(g) The recipient shall promptly inform and seek guidance from the Corporation when it determines a need for any changes to the conditions on timing or purposes set out in the Corporation's written approval of a recipient's request for a waiver.

§ 1628.5 Fund balance deficits.

(a) Sound financial management practices such as those set out in Chapter 3 of the Corporation's Accounting Guide for LSC Recipients should preclude deficit spending. Use of current year LSC grant funds to liquidate deficit balances in the LSC fund from a preceding period requires the prior written approval of the Corporation.

(b) Within 30 days of the submission of the recipient's annual audit, the recipient may apply to the Corporation for approval of the expenses associated with the liquidation of the deficit balance in the LSC fund.

(c) In the absence of approval by the Corporation, expenditures of current year LSC grant funds to liquidate a deficit from a prior year shall be identified as questioned costs under 45 CFR part 1630.

(d) The recipient's request must specify the same information relative to the deficit LSC fund balance as that set forth in § 1628.4(a)(1) and (2). Additionally, the recipient must develop and submit a plan approved by its governing body describing the measures which will be implemented to prevent a recurrence of a deficit balance in the LSC fund. The Corporation reserves the right to require changes in the submitted plan.

(e) The decision of the Corporation regarding acceptance of these deficit-

related costs shall be guided by the statutory mandate requiring the recipient to provide high quality legal services performed in an effective and economical manner. Special consideration will be given for emergencies, unusual occurrences, or other special circumstances giving rise to a deficit balance.

Dated: October 31, 2000.

Victor M. Fortuno,

Vice President for Legal Affairs.

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FEDERAL COMMUNICATIONS COMMISSION

47 CFR Parts 73 and 76

[MM Docket No. 83-484; FCC 00-386]

Repeal or Modification of the Personal Attack and Political Editorial Rules

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: This document concerns repeal of the personal attack and political editorial rules for broadcast licensees and cable system operators. This order repeals the broadcast and cable personal attack and political editorial rules. The order also vacates the Commission's earlier Order and Request to Update Record which had suspended for 60 days the personal attack and political editorial rules. The U.S. District Court of Appeals, D.C. Circuit, by order of October 11, 2000 directed the Commission to repeal the rules, noting that the Commission may institute a new rulemaking proceeding to determine whether, consistent with constitutional constraints, the public interest requires the personal attack and political editorial rules.

DATES: This rule is effective October 26, 2000.

ADDRESSES: Federal Communications Commission, 445 Twelfth Street, SW., Washington, DC 20554.

FOR FURTHER INFORMATION CONTACT: Cyndi Thomas, Policy and Rules Division, Mass Media Bureau, at (202) 418-2600.

SUPPLEMENTARY INFORMATION: This is a summary of the *Order* in MM Docket No. 83-484, FCC 00-386, adopted October 26, 2000; released October 26, 2000. The full text of this decision is available for inspection and copying during regular business hours in the FCC Reference Center, 445 Twelfth Street, SW., Room CY-A257,