Legal Services Corporation
America's Partner For Equal Justice

OFFICE OF LEGAL AFFAIRS
EXTERNAL OPINION

External Opinion # EX-2005-1002

To: Michael D. Mason, Board Chair
Thomas J. Matsuda, Executive Director
Legal Aid Services of Oregon

Date: July 15, 2005

Subject: Program Integrity Analysis of Configuration Proposal

---

On May 2, 2005, you wrote to LSC with a proposal to reconfigure the Oregon program for our review. Your program, Legal Aid Services of Oregon (LASO) would like to merge with the Oregon Law Center (OLC), which engages in restricted activities and would continue to do so as a division of the new entity. LSC requires that all recipients maintain program integrity from any entity that engages in restricted activities. We have reviewed your proposal and conclude that it does not meet the program integrity requirements of Part 1610 of the LSC regulations.

This analysis is limited to the application of the program integrity requirement to your proposal. We recognize that your stated goals are to improve the efficiency and effectiveness of delivery of legal services in Oregon. In doing so you are trying to take into account LSC's state planning goals and those of the Oregon State Bar Association. Our role is not to evaluate the delivery merits of your plans. Rather, we can only look at whether or not it fits within the limitations imposed by Congress and LSC.

In formulating Part 1610, LSC implemented the 1996 statutory restrictions while permitting LSC grantees alternative avenues for expression under the First Amendment. LSC does not require absolute separation. LASO and OLC may be able to coordinate in ways that would increase efficiency and effectiveness consistent with Part 1610. This proposal goes too far though. It fails to meet critical elements of the program integrity requirement. We hope that this opinion will explain why in ways that will enable you to continue to improve your delivery of services model while adhering to the requirements and restrictions set by Congress and LSC.

SUMMARY

LASO is an LSC grantee serving parts of Oregon that would merge with OLC to form a single unnamed corporation. OLC is a non-LSC program in Oregon that engages in LSC restricted activities and will continue to do so as a division of the new entity. LASO will be the other division of the new entity. The two divisions will share physical space, an executive director, other staff and equipment.

3333 K St, NW, 3rd Floor
Washington, DC 20007-3522
Phone 202.295.1500 Fax 202.337.6519
www.lsc.gov

The proposal does not meet two Part 1610 program integrity requirements. First, §1610.8(a)(1) requires legal separation between an LSC grantee and any entity engaging in restricted activities. As a single legal entity, the new corporation cannot have legal separation from its OLC division. Second, even if LASO remained legally separate from OLC, the proposal would not have sufficient overall physical and financial separation required under §1610.8(a)(3) because of the extensive sharing of space, staff (including an executive director) and equipment.

PROPOSAL

This is our understanding of the Oregon proposal based on your letter. LASO and OLC are separate corporations with co-extensive boards of directors. You state that the two corporations currently are physically and financially separate with no shared staff or offices. OLC receives no LSC funds nor any LSC funded subsidization. OLC engages in LSC restricted activities.

LASO proposes to merge with OLC and form a new unnamed corporation with two divisions: New LASO and New OLC. Only the New OLC division would engage in restricted activities. The new corporation would become the LSC grantee and use LSC funds only for LSC allowable activities to be provided by the New LASO division. No LSC funds would go to the New OLC division. It is proposed that strict accounting and timekeeping would prevent any LSC funded subsidies of New OLC other than economies of scale.

A single executive director would run both divisions with "centralized administrative and accounting staff" that would "direct the operations, provide accounting and financial oversight, and supervise the management of each division of the corporation." In addition, the two divisions "may share personnel" who "may work part-time for each division."

Both divisions "will operate in the same physical premises," "will share equipment, such as telephone systems, computers and networks, case management systems, libraries, office furnishings, printers, fax machines, and copiers" and "may share a common intake mechanism . . . ." The divisions will have separate registered business names and "will ensure that clients, judges, government officials and the general public are informed that the divisions are funded separately . . . [and] . . . that LSC neither endorses nor funds any of the activities of New OLC." There is no indication in the proposal of any separation of physical facilities, public or otherwise.

LEGAL BACKGROUND

45 C.F.R. §1610.8 sets out three separate requirements for a grantee to have program integrity from an organization engaging in restricted activities. All three requirements must be met. 1) "The other organization is a legally separate entity." §1610.8(a)(1). 2) "The other organization receives no transfers of LSC funds, and LSC funds do not subsidize restricted activities." §1610.8(a)(2). 3) "The recipient is physically and financially separate from the other organization." §1610.8(a)(3). The physical and financial separation requirement "will be determined on a case-by-case basis and will be based on the totality of the facts." While separate accounting and timekeeping is a factor, "[m]ere bookkeeping separation of LSC funds from other funds is not sufficient." The separation factors include, without limitation, separate personnel, separate accounting, separate timekeeping, separation from facilities in which restricted activities

occur, extent of restricted activities and extent of signs and forms of identification distinguishing the recipient from the other organization. *Id.*

An LSC Program Letter on August 7, 1997, discussed program integrity. LSC cautioned grantees regarding physical and financial separation that "sharing space, equipment and facilities with another organization which engages in restricted activity . . . may give the impression that the recipient is engaged in such activity . . . [particularly] if the two organizations employ any of the same personnel or use any of the same facilities that are accessible to clients or the public." *Guidance in Applying the Program Integrity Standards,* 3 (attachment to Aug. 7, 1997, Program Letter). Furthermore, "the more staff 'shared,' or the greater the responsibilities of the staff who are employed by both organizations, the more danger that program integrity will be compromised." *Id.* For example, sharing an executive director "inappropriately tends to blur the organizational lines between the entities. Likewise, sharing a substantial number or proportion of recipient staff calls the recipient's separateness into question." *Id.*

The U.S. Courts of Appeal for the Second and the Ninth Circuits have upheld the program integrity requirement as facially valid. *Velazquez v. LSC.,*164 F.3d 757 (2d Cir. 1999) *aff'd in part on other grounds,* 531 U.S. 533 (2001) and *LASH v. LSC,* 145 F.3d 1017 (9th Cir. 1998). It allows grantees to have alternative avenues for expression through affiliations with unrestricted entities and/or through funding such entities with non-LSC funds. In your letter you mention the recent decision by Judge Block of the Eastern District of New York in *Velazquez v. LSC* and *Dobbins v. LSC.* 349 F. Supp. 2d 566 (2004) *modified by* 356 F. Supp. 2d 267 (2005). Generally that decision does not affect your situation because it is an as applied case brought in a different federal circuit and district than yours and limited to the specific proposals put forth by those plaintiffs. *See LSC memorandum to LSC Grantees*, January 11, 2005. Furthermore, the Second Circuit is hearing appeals of that decision from all parties and the United States as intervenor. As per the regulation, each program integrity analysis is, and must be, conducted on a case-by-case basis. Parenthetically, it is worth noting that your proposal is very different from the proposals considered in that decision—the physical and financial separation factors are significantly different and your proposal lacks the legal separation required by the regulation and the district court in *Dobbins*.

ANALYSIS

Your proposal does not meet the §1610.8(a)(2) legal separation requirement because the new unnamed corporation would not have legal separation from its New OLC division engaging in restricted activities.

Even if LASO and OLC were to modify the proposal to provide for legally separate entities, the proposal would fail the physical and financial separation requirement. While the proposal provides for separation of accounting and timekeeping, the regulation specifically provides that "[m]ere bookkeeping separation of LSC funds from other funds is not sufficient." §1610.8(a)(3). As per the 1997 Program Letter, sharing an executive director alone can tend to blur the organizational lines, as could sharing physical space while having overlapping personnel. It is proposed that LASO and OLC would not only share 100% of physical space, but would also have one executive director; share phones, computers, and other equipment; and share an unspecified amount of staff (including "centralized administrative and accounting

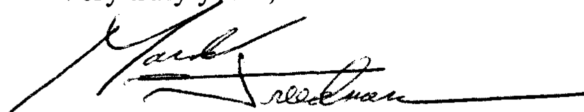
staff"). There is no indication in the proposal that there would be separation of any physical spaces, not even the public spaces. Furthermore, the proposal emphasizes presenting LASO and OLC as funded separately, but Part 1610 requires greater separation. For physical and financial separation it must be clear that the two organizations are, in fact, separate entities operating separately, notwithstanding limited permissible coordination and overlap. All of these factors, taken as a whole, would clearly blur the organizational lines between the two entities and thus fail to provide LASO with sufficient separation from OLC.

CONCLUSION

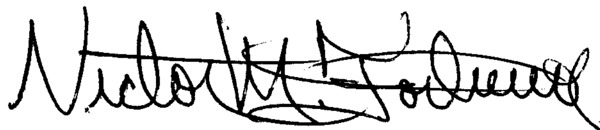
The proposal as submitted does not meet two separate program integrity requirements: legal separation and physical and financial separation. In order to maintain program integrity from OLC, LASO must be a legally separate entity and must have greater physical and financial separation than set forth in the proposal.

Please contact us if you would like to discuss further how these requirements affect your ongoing efforts to improve the delivery of legal aid in Oregon.

Very truly yours,



Mark Freedman
Assistant General Counsel
Office of Legal Affairs



Victor M. Fortuno
General Counsel
Office of Legal Affairs

mfreedman@lsc.gov
(202) 295-1623