May 22, 2003

By hand delivery

Hon. Frederic Block, U.S.D.J.
United States District Court
for the Eastern District of New York
225 Cadman Plaza East
Brooklyn, New York 11201

Re: *Velazquez v. Legal Services Corporation*, 97 CV 00182 (FB), and
Dobbins v. Legal Services Corporation, 01 CV 8371 (FB)

Dear Judge Block,

I write in further support of plaintiffs' April 25, 2003 submission to this Court, and in response to the May 9, 2003 letters from counsel for the Legal Services Corporation ("LSC") and the United States, as well as to the May 8, 2003 External Opinion of LSC's Office of Legal Affairs ("LSC External Opinion"). I also submit a supplemental "Clarification of April 25, 2003 Proposal" (attached as Appendix A) designed to allay certain concerns raised by LSC about plaintiff-grantees' proposed April 25, 2003 "Configuration Proposal." *See* LSC External Opinion at 4-9 (inviting clarifications from plaintiffs).

I. Defendants have failed to justify any greater requirement of "separation" than is described in plaintiffs' April 25, 2003 Configuration Proposal.

A. LSC admits that the requirement of "legal separation" is satisfied.

LSC expressly admits that plaintiffs' April 25, 2003 Configuration Proposal (the "proposal") satisfies LSC's requirement of "legal separation." *See* LSC External Opinion at 4.

B. LSC admits that plaintiffs' proposal will not result in any direct or indirect subsidy.

LSC admits, as a matter of principle, that no direct or indirect subsidy will occur under plaintiffs' proposal since no LSC funds will be transferred to a non-LSC affiliate entity, and each non-LSC affiliate will pay its LSC grantee affiliate "'fair market' value" for the use of any shared resources. *Id*. In particular, LSC concludes: "The cost-sharing goals in [plaintiffs' proposal] are

consistent with the non-subsidization requirement of the regulation."[1] *Id.* LSC's admission finally puts to rest any real concerns that LSC funds would be used by plaintiffs to subsidize, directly or indirectly, any of the activities prohibited under the challenged restrictions.

C. The Department of Justice's attempt to argue that an indirect subsidy will result is unpersuasive.

The Department of Justice admits that no direct subsidy will occur under plaintiffs' proposal. *See* Ltr. from LoBue to the Hon. Frederic Block, U.S.D.J., dated May 9, 2003, at 5 (the "Department of Justice letter"). However, in contrast to LSC's plain admission that neither direct nor indirect subsidy will occur under plaintiffs' proposal, the Department of Justice implies that some form of inherent indirect subsidy continues under the proposal, evidently as a consequence of increased efficiencies benefitting both the government and private donors that result from the use of certain shared resources. *Id.* at 8. The Department of Justice's claim is contrary both to LSC's own position (indeed, LSC's External Opinion defines "subsidy" to make clear that any subsidy is eliminated if a non-LSC affiliate entity provides "fair value" to an LSC grantee for any services received), and to the position taken by Presidential Executive Order No. 13279, 67 Fed. Reg. 77141 (Dec. 12, 2002), entitled Equal Protection of the Laws for Faith-based and Community Organizations (declaring nonprofit "faith-based" groups may share facilities and staff between their federally funded secular programs and privately funded religious programs without creating an impermissible subsidy of the religious programs).[2]

The Department of Justice's position is also unpersuasive as a matter of law. In related contexts, Supreme Court holdings have repeatedly rejected the indirect subsidy argument made by the Department of Justice. *See, e.g., Lynch v. Donnelly*, 465 U.S. 668, 681-83 (1984) (holding government funding for publicly displayed creche does not create impermissible indirect subsidy or endorsement of religion); *Tilton v. Richardson*, 403 U.S. 672, 682-84 (1971) (holding federal grants for college buildings of church-sponsored institutions of higher education do not impermissibly subsidize religion, provided that the government is reimbursed for the fair market value of any portion of any building used for sectarian instruction).

An example further illuminates the wholly untenable nature of the Department of Justice's position: if government helps to finance a new science building at a university or a new building for a museum, does the government gain the subsequent right to control all activity that goes on in the entire building, including constitutionally protected activity, on the theory that it is

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[1] LSC also notes that certain additional information could be supplied by plaintiffs that would be "useful" in tracking expenditures to prevent subsidy. LSC External Opinion at 5. Plaintiffs have endeavored to provide this information in Appendix A.

[2] *See also* White House Office of Faith-Based and Community Initiatives, Guidance to Faith-Based and Community Organizations on Partnering With the Federal Government, p. 7 (Dec. 12, 2002), attached as Ex. B to Decl. of Laura K. Abel, dated March 6, 2003.

indirectly subsidizing the activity, even though the particular offending activity is entirely and independently financed with private funds? The Department of Justice would apparently say "yes." The correct answer must be "no," however, since such a limitless and unprecedented grant to the federal government of the power to regulate vast segments of the private sector, through its spending authority, would radically expand the scope of federal authority under the Spending Clause, Article I, § 8 of the U.S. Constitution.

D. The Department of Justice is wrong in suggesting that the government has any legitimate interest in demanding greater separation as a means to control "the focus" of the privately funded expressive activities of privately incorporated LSC grantee organizations.

The Department of Justice also introduces a new argument that even if no actual subsidy occurs under the plaintiffs' proposal, the regulatory requirement of "physical separation" is still justified "to ensure that the LSC program operated by plaintiffs is confined to the purposes for which it was authorized." Department of Justice letter at 5. However, the Department of Justice's argument ignores the plain fact that the LSC Act did not give rise, in LSC, to a traditional federal agency with component "programs" serving as appendages of government. Rather, the LSC Act authorizes LSC to transfer federal funds to private entities, incorporated under local law, that are encouraged to rely on LSC funds and a broad array of non-LSC funds to advance entirely private speech, over which the government exercises no substantive control. *See Legal Servs. Corp. v. Velazquez*, 531 U.S. 533, 536-37, 542-43 (2001).

In light of this statutory structure, the Department of Justice's claimed interest in controlling "the program" is plainly illegitimate. *See* Pls.' Mem. of Law in Supp. of Mot. for Prelim. Inj., dated Dec. 14, 2001, at 23 (discussing public-private partnership embodied by LSC program). The government's interest extends only to the activities financed with LSC funds. There is no legitimate government interest in deterring a grantee from spending its own funds on activities that go beyond the scope of the federal program, as long as the government receives full value for its money. *See* Pls.' Reply Mem. of Law, dated June 19, 2002, at 29-31 (discussing *FCC v. League of Women Voters*, 468 U.S. 364 (1984)).

E. No concern about "endorsement" warrants any greater separation.

As described at length in plaintiffs' moving papers, this is not a case in which separation is justifiable as a means of preventing confusion about the government's own message. Nor can the government claim that its desire to prevent an appearance of endorsement justifies the enormous burdens imposed by requiring physical and personnel separation. The Department of Justice argues that "the disclaimers in question would be more likely to deceive than to inform the public," suggesting that such deception would occur if the underlying "programs" are in actuality a single integrated enterprise. Department of Justice letter at 6. However, the disclaimers described in plaintiffs' proposal can and will make clear the activities that LSC is supporting, and the different activities that Congress refuses to allow LSC to support. These

extensive disclaimers are explicitly provided for in the grantee-plaintiffs' April 25, 2003 proposal and the attached Clarification of August 25, 2003 Proposal. *See* Appendix A, at 3-4 (proposing specific disclaimers that include the following statement: "The Justice Center does not receive any LSC funds. Congress has refused to allow LSC funds to be used to finance the work of the Justice Center."). Under these circumstances, disclaimers and signage are clearly sufficient. *See* Pls.' Mem. of Law in Supp. of Mot. for Prelim. Inj., at 36 (discussing Supreme Court precedents rejecting fear of public confusion over government endorsement as justification for burdening speech).

II. **The Court should accept as true plaintiffs' unrebutted evidence that the program integrity regulation imposes an undue burden on LSNY, SBLS and Farmworker Legal Services.**

Defendants adamantly refuse to contest the merits. At no point have they challenged any of the detailed factual assertions by plaintiffs — including the facts contained in the declarations of Andrew Scherer, President of Legal Services for New York City ("LSNY"); John C. Gray, Project Director of South Brooklyn Legal Services ("SBLS"); Jim Schmidt, Executive Director of Farmworker Legal Services of New York; and Peggy Earisman, Interim Project Director, LSNY Manhattan — describing the concrete programmatic, administrative and financial burdens imposed by requiring physical and personnel separation.

Accordingly, on this motion for a preliminary injunction, the Court must accept as true these unrebutted statements of fact. *See Itek Corp. v. First Nat'l Bank of Boston*, 511 F. Supp. 1341, 1342 (D. Mass. 1981) ("In considering a motion for preliminary relief plaintiff's factual assertions, insofar as they are unrebutted by defendants, are accepted as true."); *Walter E. Heller & Co., Inc. v. Cox,* 379 F. Supp. 299, 302 (S.D.N.Y. 1974); Federal Procedure, Lawyer's Edition, §§ 47:58 (updated Mar. 2003).

III. **Judicial review is appropriate at this time**.

Having received LSC's clear rejection of plaintiffs' April 25, 2003 proposal, and of plaintiffs' August 12, 1997 proposal (the "Queens Proposal"), the Court is now positioned to rule in the context of a concrete, as-applied challenge. With respect to each proposal, LSC has argued that significant physical and personnel separation is required to satisfy the program integrity regulation. Yet, in the context of plaintiffs' as-applied challenge, LSC has failed to show that its requirement of significant physical and personnel separation does not constitute an "undue burden" on plaintiffs' exercise of their First Amendment rights. Instead, plaintiffs have shown that once the legitimate government concerns over subsidy and public confusion have been resolved by the creation of separate legal entities, scrupulously fair cost allocation rules, and vigorous signage and disclosure, the substantial burdens imposed by a requirement of separate physical space, separate equipment, and separate personnel simply cannot be justified by any legitimate government interest. Since the parties disagree, sharply, over whether further

separation can be required of plaintiffs without violating their First Amendment rights, the matter is clearly ripe for judicial review.

Respectfully,

Burt Neuborne David S. Udell

Enclosures

cc: by fax and first class mail
Stephen L. Ascher, Esq.
Joseph W. Lobue, Esq.

APPENDIX A

Clarification of April 25, 2003 Proposal

May 22, 2003

The grantee-plaintiffs[1] each submit this document to clarify their April 25, 2003 Configuration Proposal in response to questions raised by the Legal Services Corporation ("LSC") in its May 9, 2003 letter to the Court.[2] Each of the grantee-plaintiffs desires authorization from LSC to operate affiliate organizations pursuant to their April 25, 2003 proposal as clarified herein:

1. **Legal separation** — Each of the grantee-plaintiffs (also referred to as "LSC grantee affiliates") proposes to establish a legally separate corporation (the "non-LSC grantee affiliate") with its own articles of incorporation and bylaws, in accordance with the laws of the State of New York.

2. **Easily distinguishable names** — The LSC grantee affiliates propose, at this time, to use the following names for each respective non-LSC grantee affiliate:[3]

LSC grantee affiliate	Non-LSC grantee affiliate
Legal Services for New York City	New York City Justice Center
South Brooklyn Legal Services	South Brooklyn Justice Center
Farmworker Legal Services of New York	Farmworker Justice Center

3. **Separate boards of directors** — The boards of directors of the LSC grantee affiliates, and of the non-LSC grantee affiliates, will be separate: a) the boards of the respective LSC and non-LSC affiliates will meet separately and maintain separate records; and b) the membership of the boards of directors of the LSC and non-LSC affiliates will be

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[1] The phrase "grantee-plaintiffs" refers to Legal Services for New York City ("LSNY"), South Brooklyn Legal Services, and Farmworker Legal Services of New York.

[2] As instructed by the Court, the grantee-plaintiffs each submitted their Configuration Proposal for review by LSC on April 25, 2003. *See* Ltr. from Burt Neuborne to the Hon. Frederic Block, U.S.D.J., dated April 25, 2003. Two weeks later, LSC rejected the grantee-plaintiffs' Configuration Proposal. *See* Ltr. from Stephen Ascher to the Hon. Frederic Block, U.S.D.J., dated May 9, 2003 (attaching LSC External Opinion # EX-2003-1008, LSC Office of Legal Affairs, dated May 8, 2003).

[3] The plaintiff-grantees are willing to confer with LSC, at its request, on the exact names of each non-LSC grantee affiliate.

coextensive at the outset,[4] but this may change over time depending on various factors. Moreover, plaintiff-grantee LSNY would prefer to operate through an affiliate structure in which LSNY would possess authority to determine the composition of the board of the New York City Justice Center.

4. **No subsidy** — No LSC grantee affiliate will transfer any LSC funds to a non-LSC grantee affiliate.[5] Affiliated organizations will apportion fair value for expenses in accordance with generally accepted accounting principles and the requirements of the LSC Accounting Guide for LSC recipients, the LSC Office of Inspector General Audit Guide for Recipients and Auditors, and LSC regulation 45 C.F.R. § 1630, Cost Standards and Procedures, which provides "uniform standards for allowability of costs" charged to LSC grants, including both direct costs (e.g., salaries) and indirect costs (e.g., utilities and other forms of overhead costs). In particular, affiliated organizations will allocate indirect costs pursuant to 45 C.F.R. § 1630.3(f), which governs the allocation of indirect costs by LSC grantees, and by separately identifying the total costs for restricted activities and treating these costs as disallowed costs pursuant to 45 C.F.R. § 1630.2(d).[6]

5. **Employee timekeeping measures** — Any employee in the category of "legal personnel" who is employed part-time by an LSC grantee affiliate and by a non-LSC grantee affiliate, will maintain detailed time records for the work performed for each affiliate. These records will comply with LSC's timekeeping regulation, 45 C.F.R § 1635, including the requirement that an LSC grantee:

> shall require any attorney or paralegal who works part-time for the recipient and part-time for an organization that engages in restricted activities to certify in writing that the

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[4] LSC's program integrity regulation expressly permits an LSC grantee to control the activities of its non-LSC grantee affiliate through such overlapping board membership, as is required by the First Amendment. *See Legal Aid Soc'y of Haw. v. Legal Servs. Corp.*, 981 F. Supp. 1288, 1297 (D. Haw. 1997); Use of Non-LSC Funds, Transfers of LSC Funds, Program Integrity, 62 Fed. Reg. 27695, 27697 (May 21, 1997) (codified at 45 C.F.R. § 1610) (stating that "because the [LSC program integrity] standards will allow control at the Board level, recipients will have an avenue through which to engage in restricted activities"); LSC, Guidance in Applying the Program Integrity Standards, attached to LSC External Opinion # EX-2003-1008 ("A recipient may have the same or overlapping Board of Directors as another organization which engages in restricted activity.").

[5] *See* LSC External Opinion at 8 (requesting explicit statement concerning no transfer of LSC funds).

[6] *See* LSC External Opinion at 9 (requesting "some sense" of how apportionments will be made).

> attorney or paralegal has not engaged in restricted activity during any time for which the attorney or paralegal was compensated by the recipient or has not used recipient resources for restricted activities. The certification requirement does not apply to a *de minimis* action related to a restricted activity**.**

45 C.F.R. § 1635.3(d).

Additionally, any employee in the category of "non-legal personnel" (i.e., support personnel) who is employed part-time by an LSC grantee affiliate and by a non-LSC grantee affiliate, will maintain personnel activity reports, pursuant to LSC regulation 45 C.F.R. § 1630.3(d), for work performed for each affiliate. The regulation, which provides standards governing allowability of costs under LSC grants or contracts, incorporates the detailed guidance about personnel activity reports contained in Office of Management and Budget ("OMB") Circular A-122, Cost Principles for Non-Profit Organizations, Attachment B, para. 6(*l*)(2) (Aug. 29, 1997), a copy of which is attached hereto as Ex. 1.[7]

No legal personnel, and no non-legal personnel, will engage in any LSC-funded activities while working as an employee of a non-LSC grantee affiliate.[8]

6. **Signage and disclaimers** — A "disclaimer" will be provided in writing individually to all clients, prospective clients, opposing attorneys and other visitors entering the premises of the LSC grantee affiliate and of the non-LSC grantee affiliate. The disclaimer will also be provided in writing individually to all clients and prospective clients who otherwise meet in-person with an employee of an affiliate. The written disclaimer will be printed on an 8.5 x 11 inch sheet of paper in 12-point type. It will also be published on web sites maintained by the affiliates, and in the places and manners described in paragraph six of the grantee-plaintiffs' April 25, 2003 proposal.

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[7] LSC itself has determined that these timekeeping and cost allocation rules are adequate to ensure that no LSC funds are spent to directly or indirectly subsidize certain privately funded activities, such as lobbying a state legislature for increased legal services funding, that LSC grantees are permitted to conduct in the same offices and with the same employees as they conduct their LSC-funded activities. *See* Ltr. from Burt Neuborne to the Hon. Frederic Block, U.S.D.J., dated April 25, 2003, at 5-6 & nn.12, 13.

[8] This point responds to LSC's stated concern that "[i]f any personnel of the non-LSC affiliate engage in LSC-funded activities then the non-LSC affiliate is subject to LSC restrictions." *See* LSC External Opinion at 4 n.3. In fact, performance of work in such circumstances would seem to have the opposite effect, as it would constitute a subsidy of the LSC grantee by the non-LSC affiliate.

An oral disclaimer will be made in-person, and in telephone communications, to all individual clients and prospective clients. In addition to the written disclaimers to courts and government officials provided in paragraph six of the grantee-plaintiffs' April 25, 2003 proposal, disclaimers will also be made orally to all individual judges, opposing attorneys, government officials, journalists and others who come into contact with either affiliate.

For example, South Brooklyn Legal Services and the affiliated South Brooklyn Justice Center will present the following written and oral disclaimer (or a disclaimer containing similar text to the same effect) to all clients, prospective clients, and others identified above in this paragraph six:

> South Brooklyn Legal Services ("SBLS") and the South Brooklyn Justice Center (the "Justice Center") are separate, independent non-profit corporations. SBLS receives funds from the Legal Services Corporation ("LSC") to provide certain approved categories of legal assistance. Use of these funds from LSC is restricted by federal law. The Justice Center does not receive any LSC funds. Congress has refused to allow LSC funds to be used to finance the work of the Justice Center. Nevertheless, SBLS and the Justice Center cooperate to serve the legal needs of low-income individuals and families in South Brooklyn.[9]

In addition, the non-LSC grantee will include the following disclaimer (or similar text to the same effect) in all client retainer agreements:

> I have read and understood the following: The South Brooklyn Justice Center (the "Justice Center") is representing me. The Justice Center does not receive any Legal Services Corporation ("LSC") funds. Congress has refused to allow LSC funds to be used to finance the work of the Justice Center.

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[9] This text derives in part from a disclaimer that the LSC Office of Inspector General ("OIG") has required to be published, in accordance with the LSC program integrity regulation, on a web site shared by an LSC grantee affiliate and a non-LSC grantee affiliate in Oregon. *See* Lane County Legal Aid Service and Lane County Law and Advocacy Clinic homepage, *at* http://www.lanecountylegalservices.org/ (last visited May 19, 2003), attached hereto as Ex. 2; LSC OIG, Review of Grantee's Transfer of Funds, and Compliance with Program Integrity Standards, Grantee: Lane County Legal Aid Service, Inc., Report No. AU 02-01 (Oct. 2001), attached as Ex. 26 to Decl. of Laura K. Abel, dated Dec. 14, 2001.

In addition, the LSC grantee will include the following disclaimer (or similar text to the same effect) in all client retainer agreements:

> I have read and understood the following: South Brooklyn Legal Services ("SBLS") is representing me. SBLS receives funds from the Legal Services Corporation ("LSC") to provide certain approved categories of legal assistance. Federal law restricts the use of these LSC funds and all other funds provided to SBLS.

Affiliates will produce these disclaimers in both English and Spanish, and will, pursuant to existing office policies, provide additional translation into other languages.

7. **Equipment** — The respective affiliates propose to share equipment and physical resources, including, telephone lines, computers, case management systems, libraries, legal research facilities, office furnishings, printers, fax machines and web sites.

8. **Physical premises** — The respective affiliates propose to operate in one physical location with no physical separation beyond that degree of physical separation required of other non-profit federal grantees by Presidential Executive Order No. 13279, 67 Fed. Reg. 77141 (Dec. 12, 2002), entitled Equal Protection of the Laws for Faith-based and Community Organizations. The standards contained in Executive Order No. 13279, applied in the context of legal services programs, would permit the LSC and non-LSC affiliates to operate in a single physical location, but would require the non-LSC grantee affiliate to provide LSC-restricted services "separately in time or location from any programs or services supported" with LSC funds. *Id*.

   More specifically, these standards would require, for example, that a non-LSC grantee affiliate conduct its LSC-restricted activities either in a room separate from any room in which its LSC grantee affiliate is simultaneously conducting LSC-approved activities, or in the same room but at separate times. *See* White House Office of Faith-Based and Community Initiatives, Guidance to Faith-Based and Community Organizations on Partnering With the Federal Government, p. 7 (Dec. 12, 2002), attached as Ex. B to Decl. of Laura K. Abel, dated March 6, 2003.

9. **Employee time** — The LSC and non-LSC affiliates propose to share all legal, support and supervisory personnel (including an Executive Director, who will direct both programs). No personnel will engage in LSC-funded activities while working in the capacity as an employee of a non-LSC grantee affiliate.

10. **Intake** — The respective affiliates propose to share a common intake and allocation mechanism to refer clients and cases between the affiliates. As described in paragraph six above, an individual disclaimer will be provided to each individual client or prospective client who contacts either affiliate.