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United States Government Accountability Office
Washington, DC 20548

B-308037

September 14, 2006

The Honorable Charles E. Grassley
Chairman, Committee on Finance
United States Senate

Subject: *Legal Services Corporation—Lease with Friends of Legal Services Corporation*

Dear Mr. Chairman:

This responds to your July 18, 2006, request for an opinion regarding activities of the Legal Services Corporation (LSC) and Friends of the Legal Services Corporation (Friends). LSC created Friends in 2001 in an effort to lower its costs of renting office space in the Washington, D.C., rental market. In this opinion, we address whether LSC had the legal authority to create Friends and to lease property from Friends. We address also whether LSC violated the Antideficiency Act in certain transactions with Friends, including a 10-year lease and the possibility of assuming Friends' assets if Friends' were to dissolve.¹ As explained below, Congress established LSC as a private, nonprofit corporation, and, as such, conferred broad powers on LSC enabling it to establish Friends and to lease property from Friends for LSC's operations. For the same reason, the Antideficiency Act is not applicable to LSC and therefore does not restrict LSC's ability to execute a 10-year lease or to assume assets of Friends, if it so chooses, were Friends to dissolve its corporate charter. Our opinion goes to the legal authority of LSC and is not an evaluation of the appropriateness of LSC's actions.

In reaching our conclusion, we developed our record from publicly available sources, including Inspector General reports, hearing testimony, and relevant financial information. Additionally, we solicited and received legal views and other information from LSC and its Office of General Counsel.

¹ In your letter, you also expressed concern that LSC might assume Friends' liabilities if Friends were to dissolve. Friends' Articles of Incorporation do not provide for LSC to assume Friends' liabilities upon dissolution. Instead, the Articles provide for the possibility that LSC will assume Friends' assets, but only after Friends' liabilities are extinguished. *Articles of Incorporation of Friends of the Legal Services Corporation*, Apr. 6, 2001, article 7, at 2 (Articles). Therefore, we do not address the possibility of LSC's assumption of Friends' liabilities.

BACKGROUND

Congress established LSC under the Legal Services Corporation Act of 1974, “for the purpose of providing financial support for legal assistance in noncriminal proceedings or matters to persons financially unable to afford legal assistance.” Pub. L. No. 93-355, § 2 [§1003], 88 Stat. 378, 379 (July 25, 1974), *codified at* 42 U.S.C. § 2996b(a). LSC provides financial assistance to programs furnishing legal assistance to eligible disadvantaged clients. 42 U.S.C. § 2996e.

LSC created Friends in 2001 as part of an effort to find an alternative to the high costs of renting office space in the Washington, D.C., rental market.² Letter from Victor M. Fortuno, Vice President and General Counsel, LSC, to Susan A. Poling, Managing Associate General Counsel, GAO, at 1, 3, Aug. 10, 2006 (Fortuno Letter). Friends was incorporated as a nonprofit corporation³ for multiple purposes, including “raising funds to provide funds to support all aspects of the missions of [LSC]” and “[a]cquiring, holding and managing assets for use by LSC where doing so may result in lower costs or greater efficiencies for Legal Services Corporation.” Articles, article 4, at 1.

In 2002, Friends and LSC identified a 65,000 square foot building for purchase in the Georgetown section of the District of Columbia, located at 3333 K Street, N.W. The Bill and Melinda Gates Foundation provided a \$4 million grant to Friends toward the purchase of this building. Additionally, to help Friends secure a mortgage, LSC signed a 10-year lease at an annual fixed rent with Friends. Fortuno Letter, at 3. The lease contains a termination clause providing LSC the right to terminate the lease in the event that LSC does not receive its annual appropriation from Congress. *3333 K Street, N.W., Washington, D.C., Office Lease Agreement*, July 1, 2002, article 26, at 21 (Lease). Friends leases space at 3333 K Street to several other tenants, in addition to LSC. *Oversight Hearing on Legal Services Corporation: Leasing Choices and Landlord Relations Before the House Subcomm. on Commercial and Administrative Law, Comm. on the Judiciary*, 108th Cong. 27–28 (testimony of Thomas Smegal, Chairman of the Board, Friends). LSC took possession of its leased premises in 2003.

At its inception, Friends’ Board of Directors consisted solely of officers of LSC. Fortuno Letter, at 3–4. LSC officers continued to occupy half of the seats of Friends’ Board of Directors until 2004 when LSC and Friends made a concerted

² By law, LSC must maintain its principal office in the District of Columbia. 42 U.S.C. § 2996b(b).

³ Both LSC and Friends are tax-exempt organizations under 26 U.S.C. § 501(c)(3). Application of the tax laws is outside the scope of this opinion.

effort to ensure Friends' independence from LSC.⁴ Fortuno Letter, at 3. LSC and Friends share a common business address. *See* Articles, at 3; *Bylaws of Friends of Legal Services Corporation*, Aug. 27, 2002, at 2 (Bylaws). Until May 2005, LSC employees satisfied some of Friends' staffing needs on a volunteer basis. Fortuno Letter, at 3–4. Friends' Articles of Incorporation state that if Friends ceases to exist, Friends' remaining assets, after Friends' liabilities are extinguished, would be contributed to LSC. Articles, article 7, at 2.

DISCUSSION

Congress established LSC as a private, nonprofit corporation in the District of Columbia, authorizing LSC to exercise the powers conferred upon corporations by the District of Columbia Nonprofit Corporation Act,⁵ to the extent consistent with its authorizing statute. 42 U.S.C. §§ 2996b(a), 2996e(a). Although a private corporation, LSC is similar to a federal agency in some respects. It is funded through annual appropriations;⁶ its Board of Directors is appointed by the President and confirmed by the Senate;⁷ its employees are eligible to receive some federal employee benefits;⁸ and it is subject to provisions of title 5 of the United States Code regarding freedom of information and open meetings.⁹ LSC is a designated federal entity for purposes of the Inspector General Act and has had an Inspector General since 1988. 5 U.S.C. app. § 8G(a)(2). These attributes of a federal agency notwithstanding, Congress in the Legal Services Corporation Act, as amended, clearly specified that, unless otherwise provided, “the Corporation shall not be considered a department, agency, or instrumentality of the Federal Government.” 42 U.S.C. § 2996d(e)(1).

GAO has previously had occasion to consider LSC's relationship to the United States government. In the past, we have determined that LSC is not an agency or establishment of the government subject to GAO accounts settlement authority,

⁴ LSC's and Friends' operational and fiscal relationship has changed significantly since 2004. According to LSC, it no longer has operational control of Friends. *See* Fortuno Letter, at 3.

⁵ D.C. Code §§ 29-301.01–29-301.114 (2001) (D.C. Nonprofit Corporation Act).

⁶ *See, e.g.*, Science, State, Justice, Commerce, and Related Agencies Appropriations Act, 2006, Pub. L. No. 109-108, title V, 119 Stat. 2290, 2330 (Nov. 22, 2005) (“For payment to the Legal Services Corporation to carry out the purposes of the Legal Services Corporation Act of 1974, \$330,803,000 . . .”).

⁷ 42 U.S.C. § 2996c(a).

⁸ 42 U.S.C. § 2996d(d), (f).

⁹ 42 U.S.C. §§ 2996d(g), 2996c(g).

B-204886, Oct. 21, 1981, and that LSC, as an independent, nonprofit corporation outside the executive branch, is not subject to Office of Management and Budget circulars, B-241591, Mar. 1, 1991. We have also found that even though it is a private, nonprofit corporation, by the terms of its authorizing statute, LSC may not expend appropriated funds to lobby in support or defeat of legislation. 60 Comp. Gen. 423 (1981); B-163762, Nov. 24, 1980. With this legal landscape, we turn to the questions presented.

Authority to Create Friends and Enter into a Lease with Friends

As part of the annual appropriations process, Congress appropriates amounts for an annual “payment to the Legal Services Corporation to carry out the purposes of the Legal Services Corporation Act of 1974.”¹⁰ *E.g.*, Science, State, Justice, Commerce, and Related Agencies Appropriations Act, 2006, Pub. L. No. 109-108, title V, 119 Stat. 2290, 2330 (Nov. 22, 2005). Since Congress has limited this payment to the purposes of the Legal Services Corporation Act, our analysis of LSC’s authority to use its federal funds must focus on the authorities Congress granted LSC in the Act.

Section 2996e of title 42 of the United States Code defines the powers, duties, and limitations of LSC under the Legal Services Corporation Act. The powers relevant to the issues we address in this opinion are those Congress conferred on LSC by reference to the D.C. Nonprofit Corporation Act. Section 2996e states, “To the extent consistent with the provisions of this [Act], the Corporation shall exercise the powers conferred upon a nonprofit corporation by the District of Columbia Nonprofit Corporation Act.” 42 U.S.C. § 2996e(a). Section 29-301.05 of the District of Columbia Code defines the general powers of each nonprofit corporation under the D.C. Nonprofit Corporation Act. Exercising these powers, LSC can purchase, take, receive, and lease real property, D.C. Code § 29-301.05(4), and “subscribe for, or otherwise acquire . . . use and deal in and with, shares or other interests in . . . domestic or foreign corporations, whether for profit or not for profit.” D.C. Code § 29-301.05(7). Additionally, the D.C. Nonprofit Corporation Act authorizes LSC “to have and exercise all powers necessary or convenient to effect any or all of the purposes for which the corporation is organized.” D.C. Code § 29-301.05(16). In our opinion, LSC, exercising powers authorized by the D.C. Nonprofit Corporation Act, may create a corporation.

Congress provided, however, that LSC may exercise such powers only “to the extent consistent with” the Legal Services Corporation Act. 42 U.S.C. § 2996e(a). In circumstances similar to this case, B-219801, Oct. 10, 1986, we examined whether the National Consumer Cooperative Bank (Bank) was authorized to

¹⁰ Under 31 U.S.C. § 1310, “The Secretary of the Treasury shall credit an appropriation for a private organization to the appropriate fiscal official of the organization. The credit shall be carried on the accounts of —(1) the Treasury; or (2) a designated depository of the United States Government.”

incorporate three subsidiaries to engage in corporate activities related to the Bank's statutory mandate. Congress created the Bank to encourage development of cooperative banks, authorizing the Bank to provide specialized credit and technical assistance to cooperatives. Although federally chartered, the Bank was owned and controlled by cooperative stockholders. Pub. L. No. 97-35, §§ 396(b), (h), 95 Stat. 357, 439–40 (Aug. 13, 1981). The purposes of the subsidiaries were to provide debt and equity financing and leasing services for cooperatives, and to develop sources of funding for the Bank's lending activities. While the Bank had no specific statutory authority to create the subsidiaries, the creation of subsidiaries was consistent with the Bank's broad authority to exercise "all such incidental powers as shall be necessary to carry on the business of banking."

In this case, we see no inconsistency between LSC's creating Friends and the purposes Congress set out in the Legal Services Corporation Act. Congress established LSC to provide "financial support for legal assistance in noncriminal proceedings or matters to persons financially unable to afford legal assistance." 42 U.S.C. § 2996b(a). LSC, in turn, established Friends to obtain financial support to further LSC's purposes. In incorporating Friends, LSC set out as the objects and purposes of Friends, "[r]aising funds to provide funds to support all aspects of [LSC's] mission"; educating the public "as to the wisdom and need (a) to provide equal access to the system of justice in our nation . . . ; (b) to provide high quality legal assistance to those who would otherwise be unable to afford adequate legal counsel; and (c) to provide legal counsel to those who face an economic barrier to adequate legal counsel"; and "acquiring, holding and managing assets for use by LSC where doing so may result in lower costs or greater efficiencies for LSC." Articles, article 4, at 1–2.

We do not view Friends' purposes as materially different from those of the National Consumer Cooperative Bank's subsidiaries that we considered in our 1986 opinion. The purposes outlined in Friends' Articles of Incorporation serve in various ways to advance LSC's mission of affordable legal assistance. Indeed, all of the activities permitted in the Articles of Incorporation are activities that LSC itself may perform. *Cf.* B-219801 (noting that the Bank's subsidiaries could not perform any activities that the Bank could not perform directly). We conclude therefore that LSC acted within its powers when it created Friends.

For the same reasons, we have no objection to LSC's lease of office space from Friends. As explained above, LSC's authorities permitted it to create Friends to assist LSC in performing activities that LSC itself may perform. Clearly, LSC has the authority to acquire office space by either purchase or lease. D.C. Code § 29-301.05(4), as incorporated by reference into the Legal Services Corporation Act. 42 U.S.C. § 2996e(a). Among the purposes set out in Friends' Articles of Incorporation is "[a]cquiring, holding and managing assets for use by LSC." Articles, at 1. In this regard, Friends acquired the Georgetown property for LSC's use, and the lease is the vehicle that helped finance Friends' acquisition of the property.

Long-Term Lease and Assumption of Assets

Whenever a federal agency, operating with fiscal year appropriations, enters into a 10-year lease, as LSC did, questions arise whether the lease violated the Antideficiency Act.¹¹ At issue here is whether the Antideficiency Act applies to LSC.

The Antideficiency Act provides, in relevant part, the following:

“An *officer or employee of the United States Government* or of the District of Columbia government may not—

“(A) make or authorize an expenditure or obligation exceeding an amount available in an appropriation or fund for the expenditure or obligation;

“(B) involve either government in a contract or obligation for the payment of money before an appropriation is made unless authorized by law.”

31 U.S.C. § 1341(a)(1) (emphasis added). Clearly, one of the touchstones for application of the Antideficiency Act is an action or actions of “an officer or employee of the United States Government.” *Id.*

As noted above, LSC, by law, is not a federal agency. Section 2996d(e)(1) of title 42 of the United States Code states that “[e]xcept as otherwise specifically provided . . . the Corporation shall not be considered a department, agency, or instrumentality of the Federal Government.” Its officers and employees, except for limited purposes not relevant here, are not officers or employees of the United States government. *Id.* (“Except as otherwise specifically provided . . . officers and employees of the Corporation shall not be considered officers or employees . . . of the Federal Government.”). As violations of section 1341 are predicated upon an obligation of federal funds by an officer or employee of the United States government, LSC’s transactions are not subject to the Antideficiency Act.¹² Indeed, by creating LSC as a private, nonprofit entity, Congress provided LSC with certain freedoms and independence to act in a manner similar to other private,

¹¹ Unless a federal agency has specific statutory authority to enter into long-term leases, as a fiscal law matter, the Antideficiency Act issue is whether the agency incurred a firm, fixed 10-year obligation in advance of appropriations for years 2 through 10. Also, if an agency were to assume the assets of another entity, without statutory authority to do so, the agency may have augmented its appropriation.

¹² Given our conclusion, we need not address whether other elements of the Antideficiency Act may apply to the LSC.

nonprofit corporations.¹³ *See* B-241591, Mar. 1, 1991 (holding that LSC was not subject to requirements in Office of Management and Budget circulars). *See also* B-131935, July 16, 1975 (stating that the Corporation for Public Broadcasting, as a private, nonprofit corporation, is generally not subject to the same restrictions and controls on its expenditures as are federal agencies and establishments); B-307317, Sept. 13, 2006 (State Justice Institute, as a private, nonprofit corporation, is not subject to the miscellaneous receipts statute and thus could retain fees for use of advertising space in its newsletter).

Because LSC's transactions are not subject to the Antideficiency Act, LSC's authority to enter into a 10-year lease is not governed by federal fiscal law.¹⁴ LSC's authority to assume Friends' assets, as provided in Friends' Articles of Incorporation if Friends were to dissolve, is governed by the Legal Services Corporation Act. The Act authorizes LSC to accept money and property "in furtherance of the purposes of" the Act, 42 U.S.C. § 2996e(a)(2), i.e., to provide "financial support for legal assistance in noncriminal proceedings or matters to persons financially unable to afford legal assistance." 42 U.S.C. § 2996b(a).

CONCLUSION

This opinion does not address the appropriateness of LSC's actions but only whether LSC acted within the confines of its legal authority. Congress created LSC as a private corporation conferring broad powers upon its Board of Directors to make business decisions. *See* 42 U.S.C. §§ 2996a, 2996b; D.C. Code § 29-301.05. Although it receives payments in annual appropriations, LSC, as a private,

¹³ Congress, of course, could choose to subject LSC to the Antideficiency Act by amending the Legal Services Corporation Act or imposing restrictions specifically when it appropriates funds to LSC. For an example of a restriction in an annual appropriations act subjecting specific appropriations received by private entities to the restrictions of the Antideficiency Act, see Department of Transportation and Related Agencies Appropriations Act, 1998, Pub. L. No. 105-66, 111 Stat. 1425, 1435 (Oct. 27, 1997) ("any obligation or commitment by [Amtrak] for the purchase of capital improvements with funds appropriated herein which is prohibited by this Act shall be deemed a violation of 31 U.S.C. § 1341").

¹⁴ Were LSC a federal agency, without long-term leasing or contract authority, LSC's 10-year lease, in all likelihood, would have violated the Antideficiency Act. Generally, a federal agency using fiscal year funds may enter into such a multiyear lease only so long as the contract includes options to renew after the first fiscal year that may be exercised only by the agency, not the contractor, and require affirmative action by an authorized agency official. *See Leiter v. United States*, 271 U.S. 204, 206-07 (1926). While LSC included a clause in the lease reserving a right to terminate subject to the availability of appropriations (Lease, article 26, at 21), the lease does not include an option to renew exercisable only by LSC.

nonprofit corporation, is not subject to many of the fiscal restrictions imposed on federal agencies. LSC's broad discretion is constrained only by the limitations Congress imposes in the Legal Services Corporation Act and its annual appropriations acts.

The Legal Services Corporation Act and the D.C. Nonprofit Corporation Act confer broad investment authority and discretion, allowing LSC to establish Friends and to enter into a lease with Friends for office space. While Congress has imposed some limitations in the Legal Services Corporation Act and in annual appropriations acts, it has not made the Antideficiency Act applicable to LSC's transactions. Accordingly, LSC's transactions at issue here do not violate the Antideficiency Act.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Gary L. Kepplinger", with a long horizontal flourish extending to the right.

Gary L. Kepplinger
General Counsel