

# AGENDA ITEM

**182 NOVEMBER 2016**

**DATE:** November 2, 2016

**TO:** Members, Audit Committee  
Members, Board of Trustees

**FROM:** Leah Wilson, Chief Operating Officer

**SUBJECT:** Proposed State Bar Policies Prohibiting 1) the Creation of Foundations and Nonprofit Corporations; and 2) the Pledging of Revenue from Membership Fees

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## EXECUTIVE SUMMARY

On May 12, 2016, the California State Auditor completed an audit of the State Bar and issued a report with recommendations. One stand-alone recommendation related to the State Bar's ability to pledge member fee revenue, and a second set of recommendations related to the State Bar's creation, use, and oversight of foundations and nonprofit corporations. This Agenda Item proposes two new State Bar policies that would resolve any issues raised by those recommendations by 1) eliminating the State Bar's ability to pledge member fee revenue; and 2) eliminating the State Bar's ability to create any foundations or nonprofit corporations.

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## DISCUSSION

On May 12, 2016, the California State Auditor completed an audit of the State Bar and issued a report with recommendations (<http://www.bsa.ca.gov/pdfs/reports/2015-047.pdf>). This Agenda Item proposes two new State Bar policies that would resolve any issues raised by one stand-alone recommendation and a second set of related recommendations.

1. Eliminating the ability to pledge member fee revenue

The State Auditor Report contains the following recommendation relating to the State Bar's pledging of member fee revenue:

To make certain that the Legislature is not limited in its ability to set member fees, the Legislature should require the State Bar to notify or seek its approval when the State Bar plans to pledge its member fee revenue for a period that exceeds 12 months or overlaps fiscal years.

(California State Auditor Report 2015-047, May 2016, page 51.)

This recommendation was made in light of Business and Professions Code section 6008.5, which contains language restricting the Legislature's ability to reduce the maximum membership fee if the State Bar has pledged income or revenue from membership fees. That statute provides:

Whenever the board has pledged, placed a charge upon, or otherwise made available all or any portion of the income or revenue from membership fees for the payment of security of an obligation of the State Bar or any interest thereon, and so long as any such obligation or any interest thereon remains unpaid, the Legislature shall not reduce the maximum membership fee below the maximum in effect at the time such obligation is created or incurred, and the provisions of this section shall constitute a covenant to the holder or holders of any such obligation.

(Bus. & Prof. Code, § 6008.5.)

The specific authorization to pledge income or revenues from membership fees is contained in Business and Professions Code section 6001, which provides, in part:

The State Bar of California is a public corporation. It is hereinafter designated as the State Bar.

The State Bar has perpetual succession and a seal and it may sue and be sued. It may, for the purpose of carrying into effect and promoting its objectives:

- (a) Make contracts.
- (b) Borrow money, contract debts, issue bonds, notes and debentures and secure the payment or performance of its obligations.
- (c) Own, hold, use, manage and deal in and with real and personal property.
- (d) Construct, alter, maintain and repair buildings and other improvements to real property.
- (e) Purchase, lease, obtain options upon, acquire by gift, bequest, devise or otherwise, any real or personal property or any interest therein.
- (f) Sell, lease, exchange, convey, transfer, assign, encumber, pledge, dispose of any of its real or personal property or any interest therein, including without limitation all or any portion of its income or revenues from membership fees paid or payable by members.
- (g) Do all other acts incidental to the foregoing or necessary or expedient for the administration of its affairs and the attainment of its purposes.

(Bus. & Prof. Code, § 6001, emphasis added.)

The State Auditor's recommendation was designed to make certain that the Legislature was not limited in its ability to set member fees, given the language in Business and Professions Code section 6008.5. Both versions of the 2017 fee bill (AB 2878 and SB 846) would have repealed

Section 6008.5, so any such limitations would have been removed. Neither bill was enacted. But Business and Professions Code section 6001 still contains authorization for the State Bar to pledge income or revenues from membership fees. In order to fully resolve any issues that may arise from the pledging of such income or revenues, and without waiting for a legislative fix, staff recommends that the State Bar eliminate the ability to pledge such income or revenues, thereby rendering moot the State Auditor's recommendation and any limitations contained under Business and Professions Code section 6008.5.

To effectuate this recommendation, the following new Board policy is recommended:

Notwithstanding Business and Professions Code section 6001, 6008.5, or any other provision of law, the State Bar shall not pledge, place a charge upon, or otherwise make available all or any portion of the income or revenue from membership fees for the payment of security of an obligation of the State Bar or any interest thereon.

2. Eliminating the ability to create foundations and nonprofit corporations

The State Auditor Report contains the following set of recommendations relating to the State Bar's creation, use, and oversight of foundations and nonprofit corporations:

To ensure that it retains appropriate supervision and control over the State Bar's financial affairs, the board should establish a policy that includes the following:

- A description of the parameters for the creation of nonprofit organizations limiting such organizations to the purposes consistent with the law and the State Bar's mission.
- A description of the board's oversight role in relation to the State Bar's nonprofit organizations.
- Requirements to make sure that the board reviews and approves all documents the State Bar uses in the creation and use of a nonprofit organization, including original and amended bylaws as well as agreements between the State Bar and the organization.
- Requirements ensuring that the board reviews, approves, and monitors regularly the budgets and other financial reports of any nonprofit organizations.
- Requirements that the State Bar develop policies and procedures to prevent the mingling of its funds and any nonprofit organization's funds.

To improve its oversight of the State Bar's financial affairs, the Legislature should require the State Bar to disclose the creation of and use of nonprofit organizations, including the nonprofits' annual budgets and reports on their financial condition explaining the sources and uses of the nonprofits' funding.

(California State Auditor Report 2015-047, May 2016, pages 51 – 52.)

Business and Professions Code section 6140 contains authority for the State Bar to raise revenue through membership fees. Business and Professions Code section 6001 (as quoted above in connection with the ability to pledge member fee revenue), enumerate in subdivisions (a) to (g) powers of the State Bar “for the purpose of carrying into effect and promoting its objectives.” Section 6001 further states:

Pursuant to those powers enumerated in subdivisions (a) to (g), inclusive, it is recognized that the State Bar has authority to raise revenue in addition to that provided for in Section 6140 and other statutory provisions. The State Bar is empowered to raise that additional revenue by any lawful means, including, but not limited to, the creation of foundations or not-for-profit corporations.

(Bus. & Prof. Code, § 6001, emphasis added.)

Both versions of the 2017 fee bill (AB 2878 and SB 846) would have amended section 6001 to add language providing that, “as of December 31, 2016, the State Bar shall not create any foundations or nonprofit corporations.” As noted above, neither bill was enacted. In order to fully resolve any issues that may arise from the creation of foundations or nonprofit corporations, and without waiting for a legislative fix, staff recommends that the State Bar eliminate the State Bar’s ability to create any foundations or nonprofit corporations. Adopting that policy would also moot the State Auditor’s recommendations, which are premised on the existence of foundations or nonprofit corporations and the State Bar’s ability to create new foundations and nonprofit corporations. No such foundations or nonprofit corporations currently exist.<sup>1</sup>

The effectuate staff’s recommendation, the following new Board policy is recommended:

Notwithstanding Business and Professions Code section 6001 or any other provision of law, the State Bar shall not create any foundations or nonprofit corporations.

### **FISCAL/PERSONNEL IMPACT**

No fiscal or personnel impact is anticipated.

### **RULE AMENDMENTS**

None

### **BOARD BOOK IMPACT**

Both new Board policies, if adopted, will need to be added to the Board Book.

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<sup>1</sup> Foundations and nonprofit corporations that once existed have been eliminated. Although the California Bar Foundation continues to operate as a non-profit public benefit corporation, it is now separate and independent from the State Bar.

## **BOARD COMMITTEE RECOMMENDATIONS**

The Audit Committee recommends that the Board of Trustees approve the following resolution:

**RESOLVED**, that the Board of Trustees hereby adopts the following Board policy:

Notwithstanding Business and Professions Code section 6001, 6008.5, or any other provision of law, the State Bar shall not pledge, place a charge upon, or otherwise make available all or any portion of the income or revenue from membership fees for the payment of security of an obligation of the State Bar or any interest thereon; and it is

**FURTHER RESOLVED**, that the Board of Trustees hereby adopts the following Board policy:

Notwithstanding Business and Professions Code section 6001 or any other provision of law, the State Bar shall not create any foundations or nonprofit corporations.