

DRAFT
NOVEMBER 16, 2016

Statement of Expenditures of
Mandatory Fees and
Independent Auditor's Report

The State Bar of California

Year Ended December 31, 2015

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
State Bar of California

Report on the Financial Statement

We have audited the accompanying Statement of Expenditures of Mandatory Fees of the State Bar of California ("State Bar") for the year ended December 31, 2015. The Statement is the responsibility of the State Bar's management.

Management's Responsibility for the Financial Statement

Management is responsible for the preparation and fair presentation of this financial statement in accordance with the *Keller* standard, as described in Note 2 of the financial statement; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on this financial statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statement in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the State Bar's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statement referred to above presents fairly, in all material respects, the chargeable and nonchargeable expenses of the State Bar for the year ended December 31, 2015, on the basis of presentation in accordance with the *Keller* standard, as described in Note 2 of the financial statement.

Emphasis of Matter

We draw attention to Note 2 to the financial statement, which describes that the accompanying financial statement was prepared to show the allocation of certain expenses into chargeable and nonchargeable categories pursuant to a ruling by the California Supreme Court referred to as the *Keller* standard, and is not intended to be a complete presentation of the State Bar's revenues and expenses in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Restriction of Use

Our report is intended solely for the information and use of the Board of Trustees, management of the State Bar of California, and members of the State Bar of California, as defined in Note 1 to the financial statement, and is not intended to be, and should not be, used by anyone other than these specified parties.

San Francisco, California
October, 2016

THE STATE BAR OF CALIFORNIA
STATEMENT OF EXPENDITURES OF MANDATORY FEES
YEAR ENDED DECEMBER 31, 2015

	Dollar Amount	Percentage of Total Program Expense
CHARGE EXPENSES AND RELATED		
PROGRAM REVENUE:		
Chief Trial Counsel	\$ 27,644,943	40.11%
State Bar Court	7,648,438	11.10%
Member Records and Compliance	2,328,630	3.38%
Professional Competence	1,710,707	2.48%
Probation	911,918	1.32%
Mandatory Fee Arbitration	640,477	0.93%
Judicial Evaluation	646,017	0.94%
Communications	1,515,244	2.20%
Commission on Access to Justice	13,244	0.02%
Center on Access to Justice	1,196,961	1.74%
Program Development (CYLA)	281,937	0.41%
Lawyer Assistance Program	1,189,026	1.73%
Client Security Fund	7,040,993	10.22%
General Fund Allocated Support Services Costs	19,222,703	27.89%
Program Revenue	(3,068,376)	-4.45%
Total Chargeable Program Expenses	<u>\$ 68,922,862</u>	<u>100.00%</u>

See accompanying notes to the statement of expenditures of mandatory membership fees.

**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES
YEAR ENDED DECEMBER 31, 2015**

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Entity – The State Bar of California (“State Bar”) was first formed as a public corporation by the California State Legislature’s passage of the State Bar Act on July 29, 1927. On November 8, 1960, voters amended the California Constitution to add the State Bar as a constitutional agency in the judicial branch of government. Membership in the State Bar and payment of an annual membership fee are required as a condition of the practice of law in the State of California.

Basis of Accounting – To ensure observance of limitations and restrictions placed on the use of resources available to the State Bar, the accounts of the State Bar are maintained in accordance with the principles of fund accounting. This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into funds established according to their nature and purpose.

Accounting principles generally accepted in the United States of America are applied by the State Bar in conformance with pronouncements of the Governmental Accounting Standards Board (“GASB”). Amounts in the Statement of Expenditures of Mandatory Fees (“Statement”) were derived from the State Bar’s audited 2015 financial statements.

Use of Estimates – The preparation of the Statement requires management to make estimates and assumptions. Actual results could differ from those estimates. These estimates and assumptions affect the reported amounts of chargeable and nonchargeable expenses during the reporting period.

2. BASIS OF PRESENTATION

The accompanying Statement was prepared for the purpose of showing the allocation of certain expenses into chargeable and nonchargeable categories. Although derived from the State Bar’s audited 2015 financial statements, the Statement is not a substitute for the financial statements, nor is it intended to be a complete presentation of the State Bar’s revenues and expenses in conformity with accounting principles generally accepted in the United States of America. Amounts reported in the Statement can be reconciled with amounts reported in the financial statements.

The State Bar Act sets the amount of the annual membership fee that the State Bar may charge lawyers for the license to practice law in California. The amount of the annual membership fee, however, is subject to certain adjustments. The United States Supreme Court in *Keller v. State Bar of California*, 496 U.S. 1 (1990) (“*Keller*”) held that the State Bar could not require California lawyers to pay, as mandatory fees, the expense of the State Bar’s political or ideological activity that was not necessarily or reasonably related to the State Bar’s purpose of regulating the legal profession or improving the quality of legal services. The Statement provides a basis of determination for the mandatory fees that each bar member must pay in order to practice law in California. It describes and separates programs and activities that are “chargeable” and “nonchargeable” to members under the *Keller* standard. In calculating the chargeable and nonchargeable expenses, absolute precision is not expected nor required pursuant to *Keller*, at 16, citing to procedural requirements outlined in *Chicago Teachers v. Hudson*, 475 U.S. 292, 310 (1986). Expenses included in the Statement are derived from expenses included in the general fund (except program costs funded by filing or other fees), client security fund, the lawyers assistance program fund, and the support and administration fund of the State Bar. Program revenue included in the Statement represents continuing legal education fees, law corporation registration fees, grant revenues, *CalBar Journal* revenues, and other program revenues that are used to fund the related program expenses.

**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES (Continued)
YEAR ENDED DECEMBER 31, 2015**

2. BASIS OF PRESENTATION (Continued)

Since January 1, 2000, amendments to the State Bar Act have provided each member with the option of deducting \$5 from the annual membership fee for lobbying and related activities outside of the parameters established in *Keller* (Cal. Bus. & Prof. Code §6140.05). In addition to these changes, in 2001, the Board of Trustees provided members the option of an additional \$5 deduction from membership fees for certain other programs. Although reasonable persons may disagree whether some of these programs and activities may be chargeable under the criteria in *Keller*, the Board of Trustees has elected to make them optional in their entirety.

Since January 1, 2000, the amount of expenses that the State Bar may incur for legislative activity outside of the parameters of *Keller* was restricted by statute to the total revenue collected from those members electing to pay the \$5 and not take the deduction from the annual membership fee under Cal. Bus. & Prof. Code §6140.05. Instead of categorizing its programs as within or outside of *Keller*, the State Bar has elected to restrict the expenses of all of its legislative activity to voluntary funds. Similarly, the State Bar has a \$5 deduction for activities under the State Bar's Bar Relations and Elimination of Bias program and limited its funding to voluntary fees paid by members not taking this deduction. Members who do not wish to support either the State Bar's Legislative Activities or its Bar Relations and Elimination of Bias program can deduct the amounts from their annual membership fees. As a result, no part of the mandatory membership fees that a lawyer must pay as a condition of practicing law are used to fund nonchargeable expenses. Therefore, for purposes of the Statement, there are no nonchargeable expenses for mandatory membership fees for the year ended December 31, 2015.

The following is a listing of the major expenses that the State Bar has categorized as chargeable, including a description of the programs or activities performed by category. The classification of a program expense as chargeable was based on the standards in *Keller* that have been applied to determine whether an expense was necessarily or reasonably incurred for the purpose of regulating the legal profession or improving the quality of legal services available to the people of the State of California. Nonchargeable expenses, as stated above, were funded by voluntary fees paid at the option of members. Determining which State Bar programs and activities are chargeable and nonchargeable requires that judgments be made by the State Bar.

Description of Categories – Chargeable Programs

a. Chief Trial Counsel

Receive, review, and analyze incoming communications which relate to disciplinary inquiries and complaints against attorneys. Investigate allegations of unethical and unprofessional conduct against attorneys who may have violated provisions of the State Bar Act, Rules of Professional Conduct, or other standards of professional conduct. Prosecute attorneys in formal disciplinary hearings in the State Bar Court for violations of the State Bar Act or Rules of Professional Conduct. Activities include, as appropriate, the preparation of formal disciplinary pleadings, conduct of formal and informal discovery, and representation of the State Bar as Trial Examiners in the actual hearings and subsequent review proceedings. (Bus. & Prof. Code §6043, 6044, 6049, 6077, 6078, 6092.5 et seq.)

b. State Bar Court

Adjudicate formal disciplinary matters resulting in the final imposition of discipline or, in certain instances involving suspension or disbarment, the recommendation of discipline to the California Supreme Court. (Bus. & Prof. Code §6086.5, 6086.65; Cal. Rules of Court, rules 9.13, 9.16, 9.18)

**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES (Continued)
YEAR ENDED DECEMBER 31, 2015**

2. BASIS OF PRESENTATION (Continued)

c. *Member Records and Compliance*

Member Records and Compliance maintains the Court's roll of attorneys of all persons admitted to the practice of law by the court. It also bills and collects fees, costs, and penalties imposed on licensed attorneys, including reimbursements to the Client Security Fund and disciplinary costs. It also keeps track of all members of the bar, including any record of discipline, and answers inquiries from courts, other governmental agencies, other states, and the public.

d. *Professional Competence*

Maintain and improve the standards of the legal profession to enhance attorney competence through: (1) promulgating and strengthening professional standards to protect the public; (2) assisting members to comply voluntarily with such standards (e.g., Ethics Hotline, California Compendium on Professional Responsibility, Lawyers Personal Assistance Program); and (3) planning and development of programs to enhance attorney competence. (Bus. & Prof. Code §6076, 6077)

e. *Probation*

The Office of Probation (OP) monitors disciplined attorneys who have been ordered to comply with probation or reprobation conditions pursuant to orders issued by the California Supreme Court and/or the State Bar Court. The OP also monitors cases where conditions have been imposed pursuant to Business and Professions Code, section 6007(h). Once these orders or agreements become effective, the OP establishes its own case files to maintain a record of compliance or non-compliance for each attorney.

OP staff monitor participating attorneys' compliance. The monitoring requires OP staff to contact the attorney being monitored and third parties such as former clients, service providers, and other departments of the State Bar. OP staff provides timely information to the attorney, Office of Chief Trial Counsel, and State Bar Court regarding non-compliance and are available to testify regarding such under oath in court.

f. *Mandatory Fee Arbitration*

The fee arbitration program (Business and Prof. Code § 6200 et seq.) provides for resolution of fee disputes between attorneys and clients. It is mandatory for the lawyer if the client requests arbitration. Most complaints come to the program independently of the Office of Trial Counsel's Intake Unit, and the availability of this service almost certainly prevents the filing of additional disciplinary complaints. Maintaining a program that decreases the number of additional complaints assists the disciplinary system in processing those cases that cannot otherwise be handled. Although it may be argued that the arbitration program is not necessarily an indispensable part of an attorney disciplinary process, the court held it is a valuable and justifiable component of a comprehensive disciplinary system. (Id., at 622.)

g. *Judicial Evaluation*

Judicial Evaluation: The Commission on Judicial Nominees Evaluation, established pursuant to Government Code section 12011.5, is the State Bar agency which evaluates all candidates who are under consideration for a judicial appointment by the Governor. The mission of the Commission is to assist the Governor in the judicial selection process and thereby to promote a California judiciary of quality and integrity by providing independent, comprehensive, accurate, and fair evaluations of candidates for judicial appointment and nomination.

**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES (Continued)
YEAR ENDED DECEMBER 31, 2015**

2. BASIS OF PRESENTATION (Continued)

As stated in *Hoffman v. State Bar of California* (2003) 113 Cal.App.4th 630, 635, the State Bar has the “constitutional responsibility, along with the Chief Justice of the Supreme Court and the houses of the Legislature, to appoint a specified number of members to the Judicial Council. (Cal. Const., art. VI, § 6.) Through the appropriate committee, the association is also required by statute to evaluate potential appointees for judicial office and report its recommendation to the Governor. (Gov.Code, § 12011.5, subds.(a), (c).) No candidate may be appointed until the State Bar has so reported, or the time for reporting has elapsed. (Id. at subd. (k).)” Having a strong judiciary evaluation system promotes public protection by helping ensure a fair legal system.

h. *Communications*

The State Bar’s Office of Communications and Stakeholder Engagement is responsible for ensuring that the general public and the legal community are informed about the agency’s public protection role and know how to access the Bar’s services and resources. The department is tasked with conveying critical information to Californians about how to protect themselves from attorney misconduct and what to do if that happens, including by filing complaints against attorneys or seeking compensation for harm through the Client Security Fund. A major emphasis is on activities that reach the public in California to ensure they know how to access the resources of the State Bar’s attorney discipline system, as well as to help attorneys understand their ethical obligations.

Communications provides important updates for attorneys licensed in California regarding rules and ethics guiding the profession, as well as ongoing education to improve competence. This office provides information about how to find a lawyer and information about access to legal services for low-income Californians.

i. *Commission on Access to Justice*

The California Commission on Access to Justice was established in 1997 to pursue long-term fundamental improvements in our civil justice system so that it is truly accessible for all, regardless of income, geography, language ability, or other factors. The Commission is comprised of members from all three branches of government, as well as business, labor, academic, religious and civic organizations.

The 26-member commission of lawyers and judges, as well as academic, business, labor, and community leaders, was established to explore ways to improve access to civil justice for Californians living on low and moderate incomes. The commission was instrumental in establishing the \$10 million Equal Access Fund for civil legal services to the indigent and works closely with the Judicial Council to improve access to the courts.

The improvement of the administration of justice and the public’s access to justice falls within the exclusive preserve of the judicial branch. (See *Superior Court v. Mendocino* (1996) 13 Cal.4th 45.) Further, this program improves the quality of legal services available to the people of California. (See *Keller*, supra, 497 U.S. at 14.)

j. *Center on Access to Justice*

This program addresses the development of policy and initiatives in collaboration with other institutions working to expand access to justice for low income Californians (e.g. Judicial Council; legal services entities; local, state and national organizations such as the American Bar Association and National Legal Aid and Defender Association).

Programs that affect the public’s access to justice fall within the exclusive preserve of the judicial branch. (See *Superior Court v. Mendocino* (1996) 13 Cal.4th 45.)

**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES (Continued)
YEAR ENDED DECEMBER 31, 2015**

2. BASIS OF PRESENTATION (Continued)

k. *Program Development – California Young Lawyers Association (CYLA)*

California Young Lawyers Association (CYLA) is the nation's largest association of young lawyers. This program encompasses legal training and education, and involvement in the practice of law, all areas over which this court has inherent authority. (In re Attorney Discipline System, supra, 19 Cal.4th 582, 592 and Warden v. State Bar (1999) 21 Cal.4th 628, 653 [dissent opn. Kennard, J.].) This program also improves the quality of legal services available to the people of California. (See Keller, supra, 497 U.S. at 14.) Additionally, CYLA provides pro bono opportunities. Pro bono work is expected of attorneys. (See Bus. & Prof. Code, § 6073 and In re Glass (2014) 58 Cal.4th 500, 526.) Therefore, CYLA falls within the regulatory activities of the judiciary.

l. *Lawyer Assistance Program*

The purpose of the Lawyer Assistance Program is to provide an alternative to the traditional State Bar disciplinary mechanism, with the goal of the program being the identification and rehabilitation of attorneys with impairment due to abuse of drugs or alcohol, or due to mental illness. This Office oversees the operation of the Lawyer Assistance Program and adopts reasonable rules and regulations as may be necessary or advisable for the purpose of implementing and operating the Lawyer Assistance program. (Bus. & Prof. Code §6231)

m. *Client Security Fund*

Receive, evaluate, and process applications made to the Client Security Fund by persons who have suffered monetary losses due to dishonest conduct of lawyers, and authorize recovery to eligible clients out of funds collected for this purpose. (Bus. & Prof. Code §6140.5)

- n. *General Fund Allocated Support Service*** –General and administrative expenses are incurred to provide staff and operational support to all programs and activities of the State Bar including, but not limited to: human resources; finance and member billing; information technology; purchasing and procurement; building maintenance and general services; legal counsel; the formulation, implementation, and administration of policies through the Board of Trustees and the Executive Offices. The “Overhead/Interfund Allocation/Intrafund Allocation” is the share of the administrative costs that are charged to the restricted fund programs for the support provided, using the methodology of the State of California for apportioning and recouping administrative support cost provided by the State’s general fund to its special fund programs.

Executive Offices	\$ 1,779,408
General Counsel	3,799,459
Office of Finance	5,101,372
Office of Human Resources	1,507,554
Office of Administrative Support - Los Angeles	2,300,948
Office of Support Services - San Francisco	3,421,711
Information Technology	5,801,112
Office of Real Property (includes lease space cost)	1,268,589
Building Fund	3,801,469
Overhead Allocation to Other Programs	(9,558,919)
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Overhead Allocation to General Fund	\$ 19,222,703
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**THE STATE BAR OF CALIFORNIA
NOTES TO THE STATEMENT OF EXPENDITURES OF
MANDATORY FEES (Continued)
YEAR ENDED DECEMBER 31, 2015**

2. BASIS OF PRESENTATION (Continued)

- o. ***Program Revenue*** – Program revenue related to chargeable expenses from the General Fund, Building Fund, Client Security Fund, Lawyers Assistance Fund, and the Support and Administration Fund of the State Bar.

CalBar Journal revenue	\$ 153,488
Law corporation registration fees	1,499,333
Continuing legal education fees	691,633
Grants revenue	15,000
Seminar/workshop revenue	20,740
Other	688,182
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Total	\$ 3,068,376
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3. OPTIONAL DEDUCTIONS

The State Bar sets an amount that members are not required to pay and may deduct from the annual membership fees. In 2015, these deductions were in an amount up to \$50. This amount included \$5 fixed by the California Legislature for legislative and related activities. The \$5 fixed by the State Bar's governing board for the optional programs in bar relations and the elimination of bias, and \$40 set by the Legislature for the Temporary Emergency Legal Services Voluntary Assistance Option. These deductions are allocated to the following activities:

a. *Lobbying*

Members may deduct the \$5 from the annual membership fee which would otherwise fund the State Bar's consideration of legislative measures (including proposals that improve the administration of justice, that may be outside the parameters of *Keller*) and related activities. All legislative activity by the State Bar is limited by statute and by action of its governing board to the amount paid by members who elect not to take the deduction. (Bus. & Prof. Code §6140.05)

b. *Bar Relations and Elimination of Bias Programs*

Members may deduct \$5 from the annual membership fee which would otherwise fund the elimination of bias and bar relations programs to eliminate bias in the judicial system and legal profession and to increase participation of attorneys who have been underrepresented in the administration and government of the State Bar's programs and activities, such as women, ethnic minority, gay, lesbian, and disabled attorneys, and will not fund the cost of communicating and maintaining relations with local bars and other voluntary associations.

c. *Legal Service Voluntary Assistance Option*

In 2015, members were allowed to deduct \$40 from the annual membership fee, which would otherwise fund the Legal Service Trust Fund Program to support nonprofit organizations that provide free civil legal services to low-income Californians. (Bus. & Prof. Code §6140.03)