

OPEN SESSION AGENDA ITEM

54-124 JULY 2018

REGULATION AND DISCIPLINE COMMITTEE III.D.

DATE: July 19, 2018

TO: **Members, Regulation and Discipline Committee**
Members, Board of Trustees

FROM: Donna Hershkowitz, Chief of Programs

SUBJECT: Follow up on Client Security Fund Mandated Report to Legislature Regarding Options to Increase Timeliness of Payouts

EXECUTIVE SUMMARY

Business and Professions Code section 6140.56, added by Stats. 2017, Ch. 422 (SB 36), directed the State Bar to conduct a thorough analysis of the Client Security Fund (CSF) and that a report on the findings be submitted to the Legislature no later than March 15, 2018. The report, which was timely submitted to the Legislature, provided a detailed list of options for addressing the funding shortfall in the CSF with the goal of increasing timeliness of payouts. A number of the options have been implemented or are in the process of implementation. In its discussions on the draft report at the March Board meeting, the Board of Trustees (BOT) approved including all the options in the report, but asked staff to report back on the individual items for further consideration of whether the options should be pursued. In light of the recent reduction of the CSF reserve, the transfer of funds from LAP to CSF, as well as legislative input regarding the options listed in the report, it is recommended that the remaining items not be further pursued.

BACKGROUND

Business and Professions Code section 6140.56 (added by Stats. 2017, Ch. 422, (SB 36)) directed the State Bar to conduct a thorough analysis of the Client Security Fund (CSF) and report the findings to the Legislature no later than March 15, 2018. The report included a detailed list of options for addressing the funding shortfall in CSF.

The options included the following:

- Option 1: Reduce Maximum Payout to Applicants from \$100,000 to \$50,000;
- Option 2: Limit payouts to CA residents or matters with CA nexus;

- Option 3: Cease reimbursing losses attributable to loans and investments;
- Option 4: Transfer excess LAP funds to CSF;
- Option 5: Do not apply licensing fee waivers/scaling to the CSF portion of the licensing fee;
- Option 6: Add CSF assessment to fee for registering as Foreign Legal Consultant or Multi-Jurisdictional Practice program;
- Option 7: Reduce CSF reserve;
- Option 8: Impose income eligibility requirements/means test;
- Option 9: Limit amounts reimbursed for unearned fee cases;
- Option 10: Exclude from eligibility those who haven't filed a complaint with OCTC;
- Option 11: Adopt rule permitting monetary sanctions to be imposed in discipline matters (B&P 6086.13); and/or
- Option 12: Add a voluntary contribution to CSF to the licensing fee.

These options were discussed at the March Board meeting at which time the Board determined that it wanted some of the items to be pursued or considered more thoroughly and that it did not wish to pursue other options.

State Bar staff proposes that, as discussed below, the options that have already been implemented or are in the process of being implemented continue, but no further action be taken on the remaining items.

DISCUSSION

At the March 2018 Board meeting, the Board discussed the following options as possible ways for dealing with the CSF funding shortfall:

- Option 1: Transfer excess LAP funds to CSF;
- Option 2: Add CSF assessment to fee for registering as Foreign Legal Consultant or Multi-Jurisdictional Practice program;
- Option 3: Reduce CSF reserve;
- Option 4: Adopt rule permitting monetary sanctions to be imposed in discipline matters (B&P 6086.13);
- Option 5: Reduce Maximum Payout to Applicants from \$100,000 to \$50,000;
- Option 6: Limit amounts reimbursed for unearned fee cases;
- Option 7: Exclude from eligibility those who haven't filed a complaint with OCTC;
- Option 8: Add a voluntary contribution to CSF to the licensing fee.
- Option 9: Limit payouts to CA residents or matters with CA nexus;
- Option 10: Cease reimbursing losses attributable to loans and investments;
- Option 11: Do not apply licensing fee waivers/scaling to the CSF portion of the licensing fee;
- Option 12: Impose income eligibility requirements/means test.

The first 4 options have already been implemented or are in the process of implementation:

1. Transfer excess LAP funds to CSF: At the May Board meeting the Board approved the transfer of \$250,000.00 from LAP to CSF with the possibility of additional transfer of funds at a later date after decisions are made regarding the future structure of LAP.

2. Add CSF assessment to fee for registering as Foreign Legal Consultant or Multi-Jurisdictional Practice program: The fee for foreign legal consultants, registered in-house counsel, and registered legal services attorneys (the latter two being part of the MJP program) currently includes an amount equivalent to the amount licensees pay for support of CSF. That portion of the fee is now being transferred to CSF.
3. Reduce CSF reserve: At the May Board meeting the Board approved modifying the State Bar Reserve Policy to exclude CSF application payouts from the reserve calculation. This resulted in an additional \$1.5 million available for CSF reimbursements in 2018.
4. Adopt rule permitting monetary sanctions to be imposed in discipline matters (B&P 6086.13): This matter is on the July agenda with a request to go out for public comment.

The Board directed staff not to pursue options 5-8.

The Board requested that staff report back on options 9-12:

9. Limit payouts to CA residents or matters with CA nexus;
10. Cease reimbursing losses attributable to loans and investments;
11. Do not apply licensing fee waivers/scaling to the CSF portion of the licensing fee;
12. Impose income eligibility requirements/means test.

As the BOT recognized in its discussions in March Options 9, 10 and 12 would have negative impacts on the applicants to CSF. Option 11 involving licensing fee waivers and scaling, would likely have a negligible impact on CSF funding (reported at the March meeting as \$0.1 million additional revenue to CSF), but could result in difficulties for struggling attorneys to satisfy their licensing obligations. The legislature also expressed a lack of enthusiasm for options that would reduce benefits to CSF applicants. The Assembly Judiciary Committee analysis of this year's licensing bill - AB 3249 - included a section entitled "Study of Client Security Fund makes clear that it is underfunded and provides options to bridge the funding gap this [sic], some of which reduce benefits to clients who have been ripped off by dishonest attorneys." The title alone indicates the committee's concern about these types of options. The analysis goes on to note:

To address the shortfall in the CSF, the Bar makes a number of recommendations to reduce possible payouts to clients who have been victimized by dishonest attorneys and to improve collections. Recommend ways to reduce payouts to injured clients include:

- Limiting payouts to only California residents;
- Only paying clients who income falls below a specified threshold;
- Limiting payouts for failure to refund unearned fees; and
- Capping payouts

All of these options might improve the CSF fund balance, but at the expense of injured clients. Therefore, it is far preferable to consider ways to increase funds in the CSF.

In light of the negative impact on CSF applicants and licensees, and the actions already taken (including transferring over \$2 million to CSF to use for current year payouts) and in process (including legislation to improve collections and discipline sanctions currently before the BOT), the Board's previous reticence about these items, and the legislature's stated concerns about the Bar pursuing these items, staff is recommending that no further efforts be taken to pursue Options 9, 10, 11 and 12.

FISCAL/PERSONNEL IMPACT

None. Pursuit of these items could result in fewer reimbursements of CSF funds.

RULE AMENDMENTS

None

BOARD BOOK AMENDMENTS

None

STRATEGIC PLAN GOALS & OBJECTIVES

Goal: 2. Ensure a timely, fair, and appropriately resourced admissions, discipline, and regulatory system for the more than 250,000 lawyers licensed in California.

Objective: f. Support adequate funding of the Client Security Fund.

RECOMMENDATION

It is recommended that the Regulation and Discipline Committee and Board of Trustees approve the following resolution:

RESOLVED, that no further action on options 9, 10, 11 and 12, set forth in Attachment A, be pursued at this time.

ATTACHMENT LIST

A. Client Security Fund: Options to Increase Timeliness of Payouts

Attachment A
Client Security Fund: Options to Increase Timeliness of
Payouts BOT Action March 2018

| Option | Description | BOT Action: Do Not Pursue | BOT Action: Report Back | Completed |
|---------------|--|--|--|-------------------------------|
| 1 | Transfer excess LAP funds to CSF | | ✓ | ✓ |
| 2 | Add CSF for registering as FLC or with MJ program | | ✓ | ✓ |
| 3 | Reduce CSF reserve | | ✓ | ✓ |
| 4 | Adopt rule permitting sanctions to be imposed in discipline matters (B&P 6086.13) | | ✓ | In progress (July BOT mtg) |
| 5 | Reduce Maximum Reimbursement to 50,000 | X | | |
| 6 | Limit amounts reimbursed for unearned fee cases | X | | |
| 7 | Exclude from eligibility those who haven't filed a complaint with OCTC | X | | |
| 8 | Add a voluntary contribution to CSF to the licensing fee | X | | |
| 9 | Limit payouts to CA residents or matters with CA nexus | | ✓ | |
| 10 | Cease reimbursing losses attributable to loans and investments | | ✓ | |
| 11 | Do not apply licensing fee waivers/scaling to the CSF portion of the licensing fee | | ✓ | |
| 12 | Impose income eligibility requirements / means test | | ✓ | |