

AGENDA ITEM

MARCH 54-166

Legal Services Trust Fund Program:
Set Amount for Distribution for
2006-2007 IOLTA Grants

BCSR

03/17/06

Open / Action
Item III.B.

DATE: February 28, 2006

TO: Members of the Board of Committee on Stakeholder Relations
Members of the Board of Governors

FROM: Judy Garlow, Director, Legal Services Trust Fund Program

SUBJECT: Legal Services Trust Fund Program:
Set Amount for Distribution for 2006-2007 IOLTA Grants

Executive Summary

Each year, the Board of Governors sets an amount for distribution in Legal Services Trust Fund Program grants from interest on lawyer trust accounts ("IOLTA"). Since 1992, the method for setting the amount has been to allocate for the grants the amount of prior year revenue less administrative costs, adjusted by an amount by which cash on hand as of June 30 is projected to be more or less than a specific percent of the prior year's net revenue. Most recently, this cash-on-hand target has been 30 percent. After consultation with the Legal Aid Association of California, the Legal Services Trust Fund Commission is recommending adjusting this target for this year upward to approximately 50 percent, so as to take advantage of increased IOLTA revenue to put us in a position to cushion the effects of lower interests rates as needed in the future. Using this system will result in 2006-2007 grants of \$12.7 million, up about 6 percent from the \$12 million distributed in the 2005-2006 grant year.

BACKGROUND

The Board of Governors each year sets an amount for distribution in IOLTA grants to be administered by the Legal Services Trust Fund Program. That amount is distributed for the grant year beginning July 1. The amount is set in March or April, depending on the board meeting schedule, so that the Trust Fund Commission can notify each recipient program of a grant amount, give them 30 days to prepare proposed budgets, review the budgets and still get grant agreements signed and the checks mailed in July.

For each of the first eight grant periods (fiscal years 1984-1985 through 1991-1992), the amount approved for distribution was the total money projected to be on hand June 30. This amounted to the total revenue of the program in the year preceding the grant period, less administrative costs during the same period. In other words, the program collected money for a year and then gave it out in the following year.

At the beginning of the grant year, 100 percent of the money for grants was on hand. Grants were disbursed in quarterly payments. At the same time, money came in that would become the next year's grants, so the program always had on hand about one full year's revenue.

In 1992, the Board of Governors changed that system on the recommendation of the Legal Aid Association of California and the Trust Fund Commission. We moved away from a system where grants were made up only of money already in hand, and to a system of paying part of the grant out of income as it came in. The motivation for this change was the view that the program did not need to keep such a large amount of cash on hand, especially in times of low interest rates and correspondingly lower revenue.

The basic distribution method remained, as before, to allocate for grants the amount of prior year revenue less administrative costs. To determine the amount for distribution, this net prior year revenue amount was adjusted by the amount by which cash on hand as of June 30 was projected to be more or less than a set percentage of the prior year's revenue amount. When the original change was made in 1992, interest rates had begun to drop and the target was set at 75 percent, in order to increase grants by 6 percent over the previous year even though revenue was down about 7 percent. Subsequently, interest rates fell dramatically. The cash-on-hand target was reduced to 60 percent and then to 30 percent, where it has remained for the last 12 grant years.

In years when revenue is increasing, the money coming in exceeds the grant amount going out, and cash on hand builds up above 30 percent. That "extra" amount is added onto the grants for the next year, resulting in a larger increase. In years when revenue is decreasing, the money coming in is less than the grant amount going out, and cash on hand drops below 30 percent. We make up for that by holding back money to increase the cash on hand for the next year, resulting in a greater decrease in grants.

This system has had the desired effect of putting the money in the hands of grant recipients quickly, and has minimized the amount of the program's cash on hand. Because of the swings in interest rates in the last several years, however, it has also meant there were somewhat unpredictable swings in the amount of grants from year to year. As just one example, the total grant amount went up 22 percent in 2001 and then back down 38 percent the following year. Although the grants on average represent a small share of each recipient's total income, in many cases, the ups and downs have been significant. In a time of increasing revenue, the Trust Fund Commission decided to explore whether there might be a better approach.

PROPOSED CHANGE

The Commission has now discussed its proposed change with the Legal Aid Association of California, which consulted with all of the recipients of Trust Fund Program grants. LAAC came back to the Commission in support of the proposal, with a few relatively small suggestions that the Commission has incorporated into this recommendation.

The proposal is to increase cash on hand above 30 percent with the goal of decreasing the fluctuation in grants caused by sizable increases and decreases in interest rates. In years of increasing revenue, grants would be held to a smaller increase than is currently provided for, so as to increase cash on hand. Then in years of decreasing revenue, the cash on hand will be spent down again, to keep grants larger than they would otherwise have been.

The recommendation of the Commission and the legal services community involves a three-step calculation for years in which income is increasing:

- The amount for distribution will be allowed to increase by 5 percent before increasing cash on hand above the current 30 percent. For 2006-2007, this means an increase from \$12 million to \$12.7 million in total grants.
- The funds that would represent the next 10 percent increase--in this case, \$1.2 million--will go to increasing the cash on hand.
- In years when revenue increases more than that, the additional amount will be divided equally between increased grants and increased cash on hand, up to a cap of 75 percent of the previous year's available funds. For this year, there is \$229,520 to be shared equally between grants and increased cash on hand.

Two elements of this change will required ongoing discussion between the Legal Services Trust Fund Commission and the Legal Aid Association, to arrive at further recommendations as needed by this time next year. The first of these two elements is the system for distributing the funds held back when we come upon years of declining income. It is much more difficult to come up with an automatic formula for that. It is likely that a policy will be developed after consultation with the Legal Aid Association.

A second issue for ongoing discussion is the cap on the amount held back to increase cash on hand. LAAC suggested limiting the cash on hand to a specific target, in the range of 50 to 75 percent. The Trust Fund Commission has agreed to a 75 percent cap, and also agreed to discuss whether it should be smaller (or larger) than that. The amount for this year will be 53 percent. Between now and the next time the board goes through this process, a year from now, we can explore the most effective cap. This is a decision that must in any case be made annually, based on the particular income in that year.

CURRENT AND PROJECT REVENUE AND CASH ON HAND

Using this revised system for determining the grant amount will result in setting the grant amount for 2006-2007 at \$12.7 million. This grant amount is larger than the 2005-2006 distribution, due primarily to increased income from substantial increases in the balance on deposit in attorney-client trust accounts and also to small increases in the interest rates on checking accounts.

We currently expect net IOLTA revenue (income less expenses) for the period July 1, 2005 through June 30, 2006 to be \$14 million. At this income level, the program expects to have on hand as of June 30, 2006 about \$7.5 million, which is 53 percent of last year's net revenue. To calculate the grant amount for the coming year, we have added to last year's grant amount a 5 percent increase, plus half of the amount by which net revenue is greater than 15 percent of last year's grants.

RECOMMENDATION

The attached schedule shows the calculation, based on actual experience to date and projections through the rest of the grant year.

Because money will continue to be disbursed as it is received, the Trust Fund Commission will continue to monitor revenue closely and will return with recommendations if there are significant variances from the projections. The agreements signed with grant recipients will continue to include language to make clear that payment of these grants is contingent upon the Legal Services Trust Fund Program having sufficient money on hand from IOLTA revenue to make the scheduled payments. In addition, the Trust Fund Commission will meet with LAAC over the coming months to evaluate the effectiveness of the procedures used this year and what changes should be made for the future.

BOARD BOOK/ADMINISTRATIVE MANUAL IMPACT: None.

PROPOSED RESOLUTION

The Board Committee on Stakeholder Relations will have a recommendation at the time of your meeting. If you agree with this proposal, the following resolution would be appropriate:

RESOLVED, upon recommendation of the Board Committee on Stakeholder Relations, that the Board hereby approves that the distribution of IOLTA grants from the Legal Services Trust Fund Program for the grant period July 1, 2006 through June 30, 2007 shall be made in the order and manner provided by Business and Professions Code Section 6216, and the funds to be distributed shall be \$12,720,721 calculated as follows

- (1) The amount projected to be received by the Legal Services Trust Fund Program and the interest earned thereon from July 1, 2005 through June 30, 2006, totaling \$15,256,329, shall be allocated for the grant period July 1, 2006 through June 30, 2007.
- (2) The administrative costs to be deducted prior to distribution shall be the costs projected for the period July 1, 2005 through June 30, 2006, totaling \$1,220,280.
- (3) To be subtracted from the total amount prior to distribution shall be \$1,200,568, 10 percent of prior year net revenue reserved for cash on hand.
- (4) Also to be subtracted from the total amount prior to distribution shall be \$114,760, one-half of the amount over 15 percent of prior year net revenue reserved for cash on hand, and it is

FURTHER RESOLVED that grant payments are to be made from funds received pursuant to Business and Professions Code Section 6212 and the income earned from investment of such funds, and that payment of grants is contingent upon the State Bar having sufficient money on hand from such sources to make the scheduled payments; and it is

FURTHER RESOLVED that the Legal Services Trust Fund Commission is directed to monitor program revenue during the grant year and to recommend action to change the total grant amount for the year if needed in the event of significant variances from projections.

STATE BAR OF CALIFORNIA
Legal Services Trust Fund Distribution
Available Funds for Grant Period 2006-2007

DATE: FEBRUARY 21, 2006

AMOUNT

A. Revenue: 7/1/05 – 6/30/06

2005:	3rd Quarter	\$	3,726,984
	4th Quarter		3,679,345
2006:	1st Quarter (Projected)		3,900,000
	2nd Quarter (Projected)		<u>3,950,000</u>
Total Revenue		\$	15,256,329

B. Administrative Costs: 7/1/05 – 6/30/06

7/1/05 – 12/31/05	\$	734,972
1/1/06 – 6/30/06 (Budgeted)		815,308
Less Projected Equal Access Fund Reimbursements		<u>(330,000)</u>
Total Administrative Costs	\$	1,220,280

C. Cash-on-Hand Calculation

Cash on Hand 6/30/05	\$	5,547,400
Add: Net Revenue 7/1/05 – 6/30/06		14,036,049
Less: 2005-2006 Grants (Net of amounts from past years redistributed)		<u>(12,005,677)</u>
Projected Cash on Hand – 6/30/06 (53 percent of prior year net revenue)	\$	7,577,772

Grant Amount Calculation

2005-2006 Net Revenue	\$	14,036,049
Less 10 percent reserved for cash on hand		(1,200,568)
Less one-half of amount over 15 percent reserved for cash on hand	\$	<u>(114,760)</u>

Total Grant Amount for 2006-2007	\$	12,720,721
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Prior Year Distribution (2005-2006)	\$	12,005,677
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Percent Increase from Prior Year Distribution	6%
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ATTACHMENT

Selection Guidelines for State Bar Appointments to the ABA House of Delegates

The State Bar will strive to appoint members from its applicant pool meeting the following guidelines:

- One (1) delegate who qualifies as the young lawyer representative;
- Up to two (2) delegates to include the most immediate past member of the ABA Board of Governors and any immediate past officer of the ABA from the California ABA Delegation;
- Two (2) members who have not had substantial volunteer experience but who possess the leadership and other skills to be successful delegation members; and
- Six (6) delegates who have substantial bar experience, especially with the ABA, and are typical of other State Bar appointments.

Unless otherwise authorized by the Board of Governors, Each each member of the State Bar's ABA delegation would be eligible for reappointment to no more than three (3) consecutive two-year appointments or a maximum of six (6) consecutive years of service with the delegation. Delegates who have completed such service may apply in the future after a period of not less than two years from the date of the expiration of the delegate's last term of service with the State Bar.

All members will be encouraged to become broadly participant in ABA activities in order to fully represent the interests of California attorneys.

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- (4) Also to be subtracted from the total amount prior to distribution shall be \$114,760, one-half of the amount over 15 percent of prior year net revenue reserved for cash on hand, and it is

FURTHER RESOLVED that grant payments are to be made from funds received pursuant to Business and Professions Code Section 6212 and the income earned from investment of such funds, and that payment of grants is contingent upon the State Bar having sufficient money on hand from such sources to make the scheduled payments; and it is

FURTHER RESOLVED that the Legal Services Trust Fund Commission is directed to monitor program revenue during the grant year and to recommend action to change the total grant amount for the year if needed in the event of significant variances from projections.

RESOLVED, upon recommendation of the Committee on Group Insurance Programs, that the Board Committee on Operations, acting on behalf of the Board between regularly scheduled meetings, hereby approves the formal acknowledgment of Raphael Cotkin's 25 years of service to the State Bar of California; and it is

FURTHER RESOLVED, that that Board Committee on Operations, acting on behalf of the Board between regularly scheduled meetings, hereby authorizes the Committee on Group Insurance Programs to formally present this Board Resolution to Raphael Cotkin at it's Planning Session dinner on Monday, March 13, 2006.

[The above is a report of emergency fax-poll action taken by the Board Committee on Operations on behalf of the Board, March 3 - 6, 2006, between regularly scheduled Board meetings.]

RESOLVED, upon the recommendation of the Los Angeles County Bar Association, that the Board Committee on Operations, acting on behalf of the Board between meetings, approves the resolution adopted by the Los Angeles County Bar Association; and it is

FURTHER RESOLVED, that the Board Committee on Operations, acting on behalf of the Board between meetings, authorizes participation in this resolution in the Tribute Book by March 15, 2006, to be presented to the Chief Justice at the dinner in his honor on April 4, 2006.

[The above is a report of emergency fax-poll action taken by the Board Committee on Operations on behalf of the Board, March 3 - 6, 2006, between regularly scheduled Board meetings.]

Upon motion made, seconded and adopted, it was

RESOLVED, upon recommendation of the Board Committee on Operations, that the Board hereby rejects the Foundation's proposed change to the at-will termination clause, accepts the Foundation's change to the revenue, and modifies Article 2.3 of the MOU along the lines discussed, and delegate to the Executive Director the authority to communicate a final proposal to the Foundation; and it is